FINAL : PAPER - 16

TAX MANAGEMENT & PRACTICE

FINAL

STUDY NOTES

The Institute of Cost Accountants of India
CMA Bhawan,12, Sudder Street, Kolkata - 700 016

First Edition : April, 2013

Revised Edition : October, 2013 (as per Finance Act, 2013)

Second Edition : December, 2014 (as per Finance (No. 2) Act, 2014)

Third Edition : March, 2016 (as per Finance Act, 2015)

Published by :
Directorate of Studies
The Institute of Cost Accountants of India (ICAI)
CMA Bhawan, 12, Sudder Street, Kolkata - 700 016
www.icmai.in

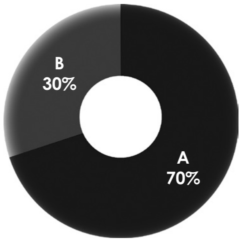
Printed at :
Repro India Limited
Plot No. 02, T.T.C. MIDC Industrial Area,
Mahape, Navi Mumbai 400 709, India.
Website : www.reproindialtd.com

Syllabus

PAPER 16: TAX MANAGEMENT & PRACTICE (TMP)

Syllabus Structure

A	Tax Management	70%
B	Tax Practice and Procedures	30%



ASSESSMENT STRATEGY

There will be written examination paper of three hours

OBJECTIVES

To gain expert knowledge about the direct and indirect tax laws in force and the relevant rules and principles emerging from leading cases, to provide an insight into practical aspects and apply the provisions of laws to various situations and to understand the various external Auditing Requirements under tax laws.

Learning aims

The syllabus aims to test the student's ability to :

- Tax planning and management under Direct and Indirect Taxes
- Explain case laws governing core provisions of the above Acts
- Explain tax assessment for various assessees and return filing procedures
- Explain powers of various assessing authorities
- Explain rebate, relief, refund under various provisions of these Acts
- Explain International Taxation and other relevant issues

Skill set required

Level C : Requiring skill levels of knowledge, comprehension, application, analysis, synthesis and evaluation

Section A : Tax Management	**70%**
1. Central Excise	
2. Customs law	
3. Service tax	
4. Export promotion schemes, foreign trade policies, EOU, SEZ, EXIM Policy (with special reference to impact on tax planning)	
5. Central Sales Tax and VAT Act	
6. Income Tax	
7. Wealth Tax **[Wealth Tax Act has been abolished w.e.f. A.Y. 2016-2017]**	
8. International Taxation	
Section B : Tax Practice and Procedures	**30%**
9. Case study analysis	

SECTION A: TAX MANAGEMENT [70 MARKS]

1. Central Excise

(a) The Central Excise Law – Assessments, Demands, Refund, Exemptions, Power of Officers

(b) Adjudication, Appeals, Settlement Commission, Penalties

(c) Central Excise Audit and Special Audit under 14A and 14AA of Central Excise Act

(d) Tariff Commission and other Tariff authorities

2. Customs Law

(a) Valuation, Customs Procedures, Import and Export Procedures, Baggage, Exemptions, Warehousing, Demurrage, Project Import and Re-imports

(b) Penalties and Offences

(c) Anti-dumping Duty – Valuation under Customs Law, application of cost accounting principles in assessment, Impact of tax on GATT 94, WTO, Anti Dumping processing

3. Service Tax

(a) Introduction, Nature of Service Tax, Service Provider and Service Receiver, Registration and related issues

(b) Negative List of Services, Exemptions and Abatements

(c) Valuation of Taxable Services

(d) Payment of service Tax, Returns of Service Tax

(e) CENVAT Credit Rules, 2004

(f) Place of Provision of Service Rules, 2012

(g) Other aspects of Service Tax

(h) Special Audit u/s 72A of the Finance Act, 1994 for Valuation of Taxable Services

4. Export Promotion Schemes, Foreign Trade Policies, EOU, SEZ, EXIM Policy (with special reference to impact on tax planning)

(a) Export Promotion Schemes,

(b) Export Oriented Units (EOU)

(c) Foreign Trade Policies

(d) Special Economic Zone (SEZ)

(e) EXIM Policy

5. Central Sales Tax and VAT Act

(a) Central Sales Tax

- (i) Assessment of transactions related to Stock Transfer, Branch transfer, Inter State Sale
- (ii) Returns and assessment procedures under Central Sales Tax (CST)

(b) Value Added Tax (VAT)

- (i) Assessment of transactions related to stock & branch transfer under State VAT Act
- (ii) Returns and assessment procedures under State VAT Act

6. Income Tax

(a) Assessment of Individuals, HUF, Firms (including LLP), Association of Persons(AOPs), Co-operative Societies, Trusts, Charitable and Religious Institutions, Mutual Associations, Companies (including Dividend Distribution Tax (DDT), Minimum Alternate Tax (MAT) and other special provisions relating to companies)

(b) Taxation of Non-Residents, Double taxation Relief, Double Taxation Avoidance Agreements (DTAAs)

(c) Return of Income and procedure of Assessment

(d) Search, Seizure & Survey and special procedure for Assessment of Search cases,

(e) Income of other persons included in Assessee's Total Income; Aggregation of Income and Set off or Carry Forward of Losses; Deductions in computing Total Income; Rebates & Reliefs; Applicable Rates of Tax and Tax Liability

(f) Advance Rulings; Settlement Commission, Appeals and Revision, Penalties and Prosecutions

(g) Business Reorganisation

(h) Income Tax Authorities

(g) Liability in Special Cases

7. Wealth Tax

Wealth Tax Act has been abolished w.e.f. A.Y. 2016-2017

8. International Taxation

(a) International Taxation & Transfer Pricing issues

(b) Application of Generally Accepted Cost Accounting Principles and techniques for determination of Arm's Length Price

(c) Indirect Taxation issues in cross-border services

(d) General Anti-Avoidance Rule (GAAR) – concept and application

(e) Advance Pricing Agreement (APA) – concept and application

SECTION B : TAX PRACTICE AND PROCEDURES [30 MARKS]

9. Case Study Analysis

Disclaimer: The contents of this subject / paper shall be reviewed every 6 months and shall be incorporated accordingly.

Content

TAX MANAGEMENT & PRACTICE

Study Note 3 : CENVAT Credit

Study Note 4 : Customs Law

Section A

Section B

Study Note 5 : Foreign Trade Policy

Study Note 6 : Service Tax

Study Note 7 : Adjudication, Penalties and Appeals in Indirect Taxes

Study Note 8 : Central Sales Tax and VAT act

Study Note 9 : Assessment of Various Entities & Tax Planning

Study Note 10 : Double Taxation Relief

Study Note 18 : Penalty & Prosecution

Study Note 19 : Tax Administration

Study Note 20 : Liability for Special Cases

Study Note 21 : Wealth Tax

Study Note 22 : Taxation of International Transactions

AMENDMENTS BROUGHT IN BY THE FINANCE ACT, 2015

AMENDMENTS MADE IN DIRECT TAX ACT

Rates of income-tax for Assessment Year 2016-17

1. Normal rates of Income Tax

(A) (I) In the case of every Individual (other than those covered in part (II) or (III) below) or Hindu undivided family or AOP/BOI (other than a co-operative society or any other AOP or BOI which is taxable at maximum marginal rate) whether incorporated or not, or every artificial judicial person

Upto ₹ 2,50,000	Nil
₹ 2,50,010 to ₹ 5,00,000	10%
₹ 5,00,010 to ₹ 10,00,000	20%
Above ₹10,00,000	30%

II. In the case of every individual, being a resident in India, who is of the age of 60 years or more but less than 80 years at any time during the previous year.

Upto ₹ 3,00,000	Nil
₹3,00,010 to ₹5,00,000	10%
₹5,00,010 to ₹ 10,00,000	20%
Above ₹ 10,00,000	30%

III. In the case of every individual, being a resident in India, who is of the age of 80 years or more at any time during the previous year.

Upto ₹ 5,00,000	Nil
₹5,00,010 to ₹10,00,000	20%
Above ₹ 10,00,000	30%

Note:-

1. **Special rates of income tax:** Besides the normal rates, special rates of tax are applicable in case of certain incomes in the hands of various persons. These rates are given in Chapter XII of the Income Tax Act which are covered under sections 111A to 115BBE.
2. **Rebate of income tax under section 87A:** This rebate is allowed to an individual who is resident in India and whose total income (including the income taxable at special rates) does not exceed ₹5,00,000. The rebate available shall be 100% of income tax payable (before cess) or ₹2,000, whichever is less.

Surcharge: The amount of income-tax computed in accordance with the above normal and special rates shall be increased by a surcharge at the rate of 12% of such income-tax in case of a person referred to in clause (A) above having a total income exceeding ₹1 crore.

Marginal relief: The total amount payable as income-tax and surcharge on total income exceeding ₹ 1 crore shall not exceed the total amount payable as income-tax on a total income of ₹ 1 crore by more than the amount of income that exceeds ₹1 crore.

Cess: 'Education Cess' @ 2%, and 'Secondary and Higher Education Cess (SHEC)' @ 1% on income tax (inclusive of surcharge if applicable) shall be chargeable.

Illustration 1.

Marginal relief

The total income of R for the assessment year 2016-17 is ₹ 1,01,20,000. Compute the tax payable by R for the assessment year 2016-17.

	₹	₹
Tax on ₹ 1 crore		
On first ₹2,50,000		Nil
Next ₹2,50,000 — 10%		25,000
Next ₹5,00,000 — 20%		1,00,000
Balance ₹90,00,000 — 30%		27,00,000
		28,25,000
Tax on ₹ 1,20,000 which is above ₹1 crore (₹ 1,20,000 @ 30%)		36,000
Total tax		28,61,000
Additional income above ₹1 crore	1,20,000	
Tax payable	36,000	
Balance income	84,000	
Surcharge on ₹28,61,000 @ 12% — ₹3,43,320		
∴ Surcharge in this case shall be ₹84,000 or ₹3,43,320 whichever is less due to marginal relief		84,000
Tax including surcharge		29,45,000
Add: Education cess & SHEC @ 3%		88,350
		30,33,350

Illustration 2.

What shall be your answer if the total income is ₹ 1,04,50,000 instead of ₹1,01,20,000.

		₹
Tax on ₹ 1 crore (as above)		28,25,000
Tax on ₹4,50,000 which is above ₹1 crore		1,35,000
		29,60,000
Additional income above ₹1 crore	4,50,000	
Less: Tax payable @ 30%	1,35,000	
Balance income	3,15,000	
Surcharge @ 12% on ₹ 29,60,000	3,55,200	
∴Surcharge in this case shall be ₹ 3,15,000 or ₹ 3,55,200 whichever is less		3,15,000
		32,75,000
Add: Education cess & SHEC @ 3%		98,250
		33,73,250

Illustration 3.

What will be your answer if the total income is ₹ 1,06,00,000

		₹
Tax on ₹ 1 crore		28,25,000
Tax on ₹ 6,00,000		1,80,000
Total tax		30,05,000
Additional income above ₹ 1 crore	6,00,000	
Less: Tax payable @ 30%	1,80,000	
Balance income	4,20,000	
Surcharge @ 12% on ₹ 30,05,000	3,60,600	
∴Surcharge in this case shall be ₹ 4,20,000 or ₹ 3,60,600 whichever is less (In this case there is no marginal relief)		3,60,600
		33,65,600
Add: Education cess & SHEC @ 3%		1,00,968
		34,66,568

(B) In the case of every co-operative society

(1) where the total income does not exceed ₹ 10,000	10% of the total income;
(2) where the total income exceeds ₹ 10,000 but does not exceed ₹ 20,000	₹ 1,000 plus 20% of the amount by which the total income exceeds ₹ 10,000;
(3) where the total income exceeds ₹20,000	₹3,000 plus 30% of the amount by which the total income exceeds ₹20,000.

Surcharge: The amount of income-tax computed as per the normal and special rates shall be increased by a surcharge at the rate of 12% of such income-tax in case of a co-operative society having a total income exceeding ₹ 1 crore.

Marginal relief: The total amount payable as income-tax and surcharge on total income exceeding ₹ 1 crore shall not exceed the total amount payable as income-tax on a total income of ₹ 1 crore by more than the amount of income that exceeds ₹ 1 crore.

Cess: 'Education Cess' @ 2% and SHEC @ 1% on income tax (inclusive of surcharge if applicable) shall be chargeable.

(C) In case of any firm (including limited liability partnership) — 30%.

Surcharge: The amount of income-tax computed as per the normal and special rates shall be increased by a surcharge at the rate of 12% of such income-tax in case of a firm having a total income exceeding ₹ 1 crore.

Marginal relief: The total amount payable as income-tax and surcharge on total income exceeding ₹ 1 crore shall not exceed the total amount payable as income-tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹ 1 crore.

Cess: 'Education Cess' @ 2% and SHEC @ 1% on income tax (inclusive of surcharge if applicable) shall be chargeable.

(D) In the case of a company

(i) For domestic companies: 30%.

Surcharge: The surcharge @ 7% of income tax computed as per the normal and special rates shall be levied if the total income of the domestic company exceeds ₹ 1 crore but does not exceed ₹10 crore.

The surcharge at the rate of 12% of income tax computed as per the normal and special rates shall be levied if the total income of the domestic company exceeds ₹10 crore.

Marginal relief: However, the total amount payable as income-tax and surcharge on total income exceeding ₹1 crore but not exceeding ₹10 crore, shall not exceed the total amount payable as income-tax on a total income of ₹ 1 crore, by more than the amount of income that exceeds ₹1 crore. The total amount payable as income-tax and surcharge on total income exceeding ₹10 crore, shall not exceed the total amount payable as income-tax and surcharge on a total income of ₹10 crore, by more than the amount of income that exceeds ₹10 crore.

Cess: 'Education Cess' @ 2%, and 'Secondary and Higher Education Cess' @ 1% on income tax (inclusive of surcharge if applicable) shall be chargeable.

(ii) For foreign company: 40%.

Surcharge: In case of companies other than domestic companies, the surcharge of 2% of income tax computed as per the normal and special rates shall be levied if the total income of such company exceeds ₹ 1 crore but does not exceed ₹10 crore.

The surcharge at the rate of 5% of income tax computed as per the normal and special rates shall be levied if the total income of the company other than domestic company exceeds ₹10 crore.

Marginal relief: However, the total amount payable as income-tax and surcharge on total income exceeding ₹ 1 crore but not exceeding ₹10 crore, shall not exceed the total amount payable as income-tax on a total income of ₹ 1 crore, by more than the amount of income that exceeds ₹1 crore. The total amount payable as income-tax and surcharge on total income exceeding ₹10 crore, shall not exceed the total amount payable as income-tax and surcharge on a total income of ₹10 crore, by more than the amount of income that exceeds ₹10 crore.

Cess: 'Education Cess' @ 2%, and 'Secondary and Higher Education Cess' @ 1% on income tax (inclusive of surcharge if applicable) shall be chargeable.

Amendments relating to Definitions

2. Amendment to section 2(13A)

Section 2(13A) defines "business trust". It has been amended with effect from the assessment year 2016-17. Under the amended definition "business trust" means a trust registered as,-

a. an Infrastructure Investment Trust under the Securities and Exchange Board of India (Infrastructure Investment Trusts) Regulations, 2014 made under the SEBI Act; or

b. a Real Estate Investment Trust under the Securities and Exchange Board of India (Real Estate Investment Trusts) Regulations, 2014 made under the SEBI Act, and

the units of which are required to be listed on a recognized stock exchange in accordance with the aforesaid regulations.

3. Rationalisation of definition of charitable purpose in the Income-tax Act [Section 2(15)] [W.e.f. A.Y. 2016-17]

(A) Yoga to be treated as separate limb of charitable purpose

The activity of Yoga has been one of the focus areas in the present times and international recognition has also been granted to it by the United Nations. Therefore, the Act has included 'yoga' as a separate category in the definition of charitable purpose on the lines of education.

Thus, 'yoga' like relief to the poor, education, medical relief, etc. will constitute an independent limb of charitable purpose and the trust can carry on commercial activities without any financial limit if such activity is incidental to the attainment of the objectives of the trust.

(B) Trust/institution covered under advancement of any other object of general public utility can do commercial activities upto 20% of its total receipts as against ₹25,00,000 allowed earlier

In so far as the advancement of any other object of general public utility is concerned, there is a need to ensure appropriate balance being drawn between the object of preventing business activity in the garb of charity and at the same time protecting the activities undertaken by the genuine organization as part of actual carrying out of the primary purpose of the trust or institution.

The Act has, therefore, merged the first and second provisos given under section 2(15) relating to the definition of charitable purpose to provide that the advancement of any other object of general public utility **shall not be a charitable purpose,** if it involves the carrying on of any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business, for a cess or fee or any other consideration, irrespective of the nature of use or application, or retention, of the income from such activity, **unless,—**

(i) such activity is undertaken in the course of actual carrying out of such advancement of any other object of general public utility; **and**

(ii) the aggregate receipts from such activity or activities, during the previous year, do not exceed 20% of the total receipts, of the trust or institution undertaking such activity or activities, for the previous year.

4. Subsidy or grant or cash incentive, duty drawback etc. deemed to be income [Section 2(24)(xviii)] [W.e.f. A.Y. 2016-17]

The Finance Act, 2015 has inserted clause (xviii) in section 2(24) which provides as under:

"assistance in the form of a subsidy or grant or cash incentive or duty drawback or waiver or concession or reimbursement (by whatever name called) by the Central Government or a State Government or any authority or body or agency in cash or kind to the assessee other than the subsidy or grant or reimbursement which is taken into account for determination of the actual cost of the asset in accordance with the provisions of Explanation 10 to section 43(1)." shall be deemed to be income.

Amendments relating to determination of residential status

5. CBDT empowered to prescribe the manner and procedure for computing period of stay in India of an Indian citizen who is a member of the crew of a foreign bound ship [Explanation 2 to section 6(1) inserted] [W. r. e. f. A.Y. 2015-16]

The provisions of section 6(1) provide the conditions under which an individual is held to be resident in India. The determination is based, inter alia, on the number of days during which such individual has been in India during a previous year.

In the case of foreign bound ships, where the destination of the voyage is outside India, there is uncertainty with regard to the manner and basis of determination of the period of stay in India for crew members of such ships who are Indian citizens.

In view of the above, the Act has inserted Explanation 2 to section 6(1) to provide that in the case of an Individual, being a citizen of India and a member of the crew of a foreign bound ship leaving India, the period or periods of stay in India shall, in respect of such voyage, be determined in the manner and subject to such conditions as may be prescribed.

6. The conditions for determining residential status in respect of a company amended [Substitution of section 6(3)] [W.e.f. A.Y. 2016-17]

The Act has substituted the existing clause (3) to section 6 by a new clause (3) to provide as under:

A company shall be said to be resident in India in any previous year, if—

(i) it is an Indian company; or

(ii) d uring that year, the control and management of its affairs is situated wholly in India.

Further, the Act has inserted the following Explanation under section 6(3) to define the place of effective management.

"For the purposes of this clause "place of effective management" means a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made."

Since POEM is an internationally well accepted concept, there are well recognised guiding principles for determination of POEM although it is a fact dependent exercise. However, in due course, a set of guiding principles to be followed in determination of POEM would be issued for the benefit of the taxpayers as well as, tax administration.

Amendments relating to income deemed to accrue or arise in India

7. Modifications pertaining to indirect transfer provisions [Sec. 9(1)(i)]

Section 9(1)(i) provides a set of circumstances in which income accruing or arising, directly or indirectly, is taxable in India. The said clause provides that all income accruing or arising, whether directly or indirectly, through or from any business connection in India, or through or from any property in India, or through or from any asset or source of income in India, or through the transfer of a capital asset situated in India shall be deemed to accrue or arise in India.

Modifications by the Finance Act, 2012 - The Finance Act, 2012 inserted certain clarificatory amendments in the provisions of section 9. The amendments, inter alia, included insertion of the Explanation 5 to section 9(1)(i) with retrospective effect from the assessment year 1962-63. The Explanation 5 (clarified that an asset or capital asset, being any share or interest in a company or entity registered or incorporated outside India, shall be deemed to be situated in India if the share or interest derives, directly or indirectly, its value substantially from the assets located in India.

- Meaning of the expression "substantially" -The Delhi High Court in the case of DIT v. Copal Research Ltd. [2014] 49 taxmann.com 125 (Delhi) examined the meaning of expression "substantially" and concluded that the expression "substantially" would necessarily have to be read as synonymous to "principally", "mainly" or at least "majority", Explanation 5 must be read restrictively and at best to cover situations where in substance the assets in India are transacted by transferring in shares of overseas holding companies and not to transactions where assets situated overseas are transacted which also derive some value on account of assets situated in India. In view of the above, the court held that gains arising from sale of a share of a company incorporated overseas, which derives less than 50 per cent of its value from assets situated in India would certainly not be taxable under section 9(1)(i), read with the Explanation 5 thereto.

Amendment - Considering the concerns raised by various stakeholders regarding the scope and impact of the above amendments, an Expert Committee under the Chairmanship of Dr. Parthasarathi Shome was constituted by the Government to go into various aspects relating to the amendments. The recommendations of the Expert Committee were considered and a number of recommendations (either in full or with partial modifications) have been accepted for implementation either by way of an amendment to the Act or by way of issuance of a clarificatory circular in due course. In order to give effect to the recommendations, the following amendments have been made (with effect from the assessment year 2016-17) to section 9 (and other sections) relating to indirect transfer -

"Substantial" - The share or interest of a foreign company or entity shall be deemed to derive its value substantially from the assets (whether tangible or intangible) located in India, if on the specified date the value of Indian assets,-

a. exceeds the amount of ₹ 10 crore; and

b. represents at least 50 per cent of the value of all the assets owned by the company or entity.

Value of asset - Value of an asset shall mean the fair market value of such an asset without reduction of liabilities, if any, in respect of the asset.

Specified date - The specified date of valuation shall be the date on which the accounting period of the company or entity ends (i.e., March 31 or accounting period end date, as the case may be) preceding the date of transfer. If, however, the book value of the assets of the company or entity on the date of transfer exceeds by at least 15 per cent of the book value of the assets as on the last balance sheet date preceding the date of transfer, then instead of the date mentioned above, the date of transfer shall be the specified date of valuation.

Mode of determination of fair market value - The manner of determination of fair market value of the Indian assets vis-a-vis global assets of the foreign company shall be prescribed in the rules.

Taxation on proportionate basis - The taxation of gains arising on transfer of a share or interest deriving, directly or indirectly, its value substantially from assets located in India will be on proportional basis. The method for determination of proportionality will be specified in the rules.

Exemption in case foreign entity that is transferred directly owns Indian assets - Exemption shall be available to the transferor of a share of, or interest in, a foreign entity if the transferor (along with its associated enterprises) -

a. neither holds the right of control or management;

b. nor holds voting power or share capital or interest exceeding 5 per cent of the total voting power or total share capital,

in the foreign company or entity directly holding the Indian assets.

Exemption in case foreign entity that is transferred indirectly owns Indian assets through another company - In case the transfer is of snares or interest in a foreign entity which does not hold the Indian assets directly then the exemption shall be available to the transferor if the transferor (along with its associated enterprises),-

a. neither holds the right of management or control in relation to such company or the entity,

b. nor holds any rights in such company which would entitle it to either exercise control or management of the direct holding company or entity or entitle it to voting power exceeding 5 per cent in the direct holding company or entity.

Exemption in the case of amalgamation/demerger - The transfer of shares in a foreign company (deriving value of assets substantially from assets situated in India) on account of amalgamation/demerger of foreign companies will be exempt from tax subject to the satisfaction of the following conditions of section 47(viab)/(vicc) –

In case of amalgamation	In case of demerger
1. At least 25 per cent of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company.	1. The shareholders, holding not less than 75 per cent in value of the shares of the demerged foreign company, continue to remain shareholders of the resulting foreign company.
2. Such transfer does not attract tax on capital gains in the country in which the amalgamating company is incorporated.	2. Such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated.
	3. The provisions of sections 391 to 394 of the Companies Act, 1956 shall not apply in case of demergers given above.

Reporting obligation on Indian concern - There shall be a reporting obligation on Indian concern through or in which the Indian assets are held by the foreign company or the entity. The Indian entity shall be obligated to furnish information relating to the off-shore transaction having the effect of directly or indirectly modifying the ownership structure or control of the Indian company or entity. In case of any failure on the part of Indian concern in this regard a penalty shall be leviable. The quantum of penalty in such case shall be -

a. a sum equal to 2 per cent of the value of the transaction in respect of which such failure has taken place in case where such transaction had the effect of directly or indirectly transferring the right of management or control in relation to the Indian concern; and

b. a sum of ₹ 5 lakh in any other case.

Example:

Consider the case given below -

Who is transferor	N Inc. (a company incorporated in country N)
Who is transferee	C Inc. (a company incorporated in country C)
What is transferred by N Inc.	Shares in E Inc.
In which country E Inc. is located	E Inc. is located in country E
Where shares are transferred	In country N or C or E or any other country (but not in India)
Where sale proceeds of shares are received by Nine.	Sale proceeds of shares are received in US Dollars in a country outside India
What is Indian connection in this transfer	E Inc. has assets (tangible/intangible) located in India
Whether capital gain arising to N Inc. is taxable in India	It depends upon additional information which is given below.

	Situation 1	**Situation 2**	**Situation 3**	**Situation 4**	**Situation 5**	**Situation 6**
Date of transfer	June 25, 2015	June 25, 2015	June 25, 2015	June 25, 2015	June 25, 2015	June 25, 2015
Last date of the accounting period of E Inc.	December 31,2014	December 31,2014	December 31,2014	December 31,2014	December 31,2014	December 31,2014
Book value of assets of E Inc. on June 25, 2015						
- located in India	₹ 56 crore	₹ 59 crore	₹ 57 crore	₹ 10 crore	₹ 11 crore ₹	₹ 10 crore
- located outside India	₹ 58 crore	₹ 57 crore	₹ 59 crore	₹ 5 crore	7 crore	₹ 8 crore
Book value of assets of E Inc. on December 31, 2014						
- located in India	₹ 60 crore	₹ 60 crore	₹ 60 crore	₹ 11 crore	₹ 10 crore ₹	₹ 11 crore
- located outside India	₹ 40 crore	₹ 40 crore	₹ 40 crore	₹ 7 crore	5 crore	₹ 4 crore

E Inc. has liabilities (pertaining to these assets) which are situated in India and outside India. There is no amalgamation or demerger of N Inc. and C Inc. N Inc. owns (individually and along with its associated enterprises) more than 5 per cent shares in E Inc. during 12 months ending on the date of transfer. However, N Inc. does not hold right of management or control in relation to E Inc. at any time during 12 months ending on the date of transfer. Book value of assets and fair market value of assets are the same.

Solution:

		Situation 1	Situation 2	Situation 3	Situation 4	Situation 5	Situation 6
Book value of global assets of E Inc. on December 31, 2014 (i.e., last date of accounting year immediately before date of transfer)	(a)	₹ 100 crore	₹ 100 crore	₹ 100 crore	₹ 18 crore	₹ 15 crore	₹ 15 crore
Book value of global assets of E Inc. on June 25, 2015 (i.e., date of transfer)	(b)	₹ 114 crore	₹ 116 crore	₹ 116 crore	₹ 15 crore	₹ 18 crore	₹ 18 crore
Whether (b) exceeds (a) by more than 15% of (a)	(c)	No	Yes	Yes	No	Yes	Yes
Specified date [it is last date of accounting year, if (c) is "No"] (otherwise it is date of transfer)	(d)	December 31,2014	June 25, 2015	June 25, 2015	December 31,2014	June 25, 2015	June 25, 2015
Fair market value of assets owned by E Inc. in India on specified date	(e)	₹ 60 crore	₹ 59 crore	₹ 57 crore	₹ 11 crore	₹ 11 crore	₹ 10 crore
Fair market value of assets owned by E Inc. outside India on specified date	(f)	₹ 40 crore	₹ 57 crore	₹ 59 crore	₹ 7 crore	₹ 7 crore	₹ 8 crore
Percentage of Indian assets of E Inc. on specified date [(e) ÷ {(e) + (f)}]	(g)	60%	50.86%	49.14%	61.11%	61.11%	55.56%
Whether income of N Inc. from transfer of shares in E Inc. is chargeable to tax in India		Yes [Note 1]	Yes [Note 1]	No [Note 2]	Yes [Note 1]	Yes [Note 1]	No [Note 3]

Notes -

1. Income of N Inc. in respect of transfer of shares in E Inc. outside India is taxable in India on proportionate basis, as the transaction satisfies the following conditions -
   a. fair market value of Indian assets of E Inc. on the specified date is more than ₹ 10 crore;
   b. Indian assets of E Inc. on the specified date are more than 50% of its global assets;
   c. transfer of shares is not on account of amalgamation/demerger of N Inc. and C Inc.;
   d. N Inc. owns (individually and along with its associated enterprises) more than 5 per cent shares in E Inc.
2. Indian assets of E Inc. on the specified date are not more than 50% of its global assets. Consequently, nothing is taxable in India in the hands of N Inc.
3. The fair market value of Indian assets of E Inc. on the specified date is not more than ₹10 crore. Consequently, nothing is taxable in India in the hands of N Inc.

Example:

In example above, assume that fair market value of assets is different from book value of assets. Fair market value of assets is given below (no change in book value as given in the original example) -

	Situation 1	Situation 2	Situation 3	Situation 4	Situation 5	Situation 6
Fair market value of assets of E Inc. on June 25, 2015						
– located in India	₹ 85 crore	₹ 60 crore	₹ 69 crore	₹ 17 crore	₹ 12 crore	₹ 11 crore
– located outside India	₹ 90 crore	₹ 58 crore	₹ 67 crore	₹ 8 crore	₹ 9 crore	₹ 10 crore

Fair market value of assets of E Inc. on December 31, 2014 - located in India - located outside India	₹ 70 crore ₹ 80 crore	₹ 61 crore ₹ 41 crore	₹ 61 crore ₹ 41 crore	₹ 12 crore ₹ 13 crore	₹ 10 crore ₹ 6 crore	₹ 12 crore ₹ 6 crore

Solution:

Determination of "specified date" is based upon book value of assets. Consequently, specified date (as given in the original example) will have to be adopted.

		Situation 1	Situation 2	Situation 3	Situation 4	Situation 5	Situation 6
Specified date (as given in the original example)	(d)	December 31,2014	June 25,2015	June 25,2015	December 31,2014	June 25,2015	June 25,2015
Fair market value of assets owned by E Inc. in India on specified date	(e)	₹ 70 crore	₹ 60 crore	₹ 69 crore	₹ 12 crore	₹ 12 crore	₹ 11 crore
Fair market value of assets owned by E Inc. outside India on specified date	(f)	₹ 80 crore	₹ 58 crore	₹ 67 crore	₹ 13 crore	₹ 9 crore	₹ 10 crore
Percentage of Indian assets of E Inc. on specified date [(e) ÷{(e)+(f)}]	(g)	46.67%	50.85%	50.74%	48%	57.14%	52.38%
Whether income of N Inc. from transfer of shares in E Inc. is chargeable to tax in India		No [Note 2]	Yes [Note 1]	Yes [Note 1]	No [Note 2]	Yes [Note 1]	Yes [Note 1]

Notes -

1. Income of N Inc. in respect of transfer of shares in E Inc. outside India is taxable in India on proportionate basis, as the transaction satisfies the following conditions -
   a. fair market value of Indian assets of E Inc. on the specified date is more than ₹10 crore;
   b. Indian assets of E Inc. on the specified date is more than 50% of its global assets;
   c. transfer of shares is not on account of amalgamation/demerger of N Inc. and C Inc.;
   d. N Inc. owns (individually and along with its associated enterprises) more than 5 per cent shares in E Inc.
2. Indian assets of E Inc. on the specified date are not more than 50% of its global assets. Consequently, nothing is taxable in India in the hands of N Inc.

In example above, assume that there is amalgamation/demerger of N Inc. and C Inc. However, amalgamation/demerger does not satisfy the conditions of section 47(viab)/(vicc).

- As conditions of section 47(viab)/(vicc) are not satisfied, exemption is not available to N Inc. Consequently, N Inc. is chargeable to tax in Situations 2, 3, 5 and 6.

In example above, assume that N Inc. owns (individually and along with its associated enterprises) 5 per cent (or less) shares in E Inc. during 12 months ending on the date of transfer.

- Nothing will be taxable in the hands of N Inc. in India if N Inc. does not hold right of management or control in relation to E Inc. at any time during 12 months ending on the date of transfer. Conversely, if N Inc. holds such right of management or control in relation to E Inc., it will be chargeable to tax in Situations 2, 3, 5 and 6.

8. Interest paid by Indian PE to its foreign head office bank [Sec. 9(1)(v)]

When interest is payable by an Indian branch of a foreign bank to its overseas head office, it is deductible while computing income of Indian branch. Moreover, in the hands of recipient head office, the same is not taxable in India as payer and recipient are the same. Tax is not deductible by the payer Indian branch.

Many judicial rulings are available on this point - Sumitomo Mitsui Banking Corpn. v. DIT [2012] 19 taxmann.com 364 (Mum.), Bank of Tokyo Mitsubishi UFJ Ltd. v. ADIT[2014] 49 taxmann.com 441 (Delhi-Trib.), Deutche Bank AG v. Asstt. DIT[2014] 47 taxmann.com 378 (Mum.-Trib.), ADIT v. Mizuho Corporate Bank Ltd. [2014] 48 taxmann.com 104 (Mum.-Trib.).

Amendment - To supersede the aforesaid ruling, section 9(1)(v) has been amended with effect from the assessment year 2016-17. The modified version is applicable if the following conditions are satisfied -

1. The assessee is a non-resident and engaged in the business of banking.
2. Interest is payable by the permanent establishment in India of such non-resident to the head office or any permanent establishment or any other part of such non-resident outside India.

If the above two conditions are satisfied, the permanent establishment in India shall be deemed to be a person separate and independent of the non-resident person of which it is a permanent establishment and the provisions of the Act relating to computation of total income, determination of tax and collection and recovery would apply.

Section 9(1)(v) has been amended in order to provide that in the case of a non-resident, being a person engaged in the business of banking, any interest payable by the permanent establishment in India of such non-resident to the head office or any permanent establishment or any other part of such non-resident outside India shall be deemed to accrue or arise in India and shall be chargeable to tax in addition to any income attributable to the permanent establishment in India.

Accordingly, the PE in India shall be obligated to deduct tax at source on any interest payable to either the head office or any other branch or PE, etc., of the non-resident outside India. Further, non-deduction would result in disallowance of interest claimed as expenditure by the PE and may also attract levy of interest and penalty in accordance with relevant provisions of the Act.

9. Fund Managers in India not to constitute business connection of offshore funds [Section 9A] [W.e.f. A.Y. 2016-17]

There are a large number of fund managers who are of Indian origin and are managing the investment of offshore funds in various countries. These persons are not locating in India due to the above tax consequence in respect of income from the investments of offshore funds made in other jurisdictions.

In order to facilitate location of fund managers of off-shore funds in India, section 9A has been inserted in the Act in line with international best practices which provides as under,—

(1) 'Fund management activity' in case of an 'eligible investment fund' carried out through an 'eligible fund manager' shall not constitute business connection in India [Section 9A(1)]

(2) 'Eligible investment fund' will not be treated as resident in India even if 'eligible fund manager' is situated in India [Section 9A(2)]

Amendments relating to income exempt from tax

10. Income of Swachh Bharat Kosh and Clean Ganga Fund to be exempt from income-tax [Section 10(23C)] [W.r.e.f. A.Y. 2015-16]

Considering the importance of Swachh Bharat Kosh and Clean Ganga Fund, the Act has amended section 10(23C) of the Act so as to exempt the income of Swachh Bharat Kosh and Clean Ganga Fund set up by the Central Government from income-tax.

11. Exemption to income of Core Settlement Guarantee Fund (SGF) set up by the recognised Clearing Corporations [Section 10(23EE)] [Inserted w.e.f. A.Y. 2016-17]

Section 10(23EE) has been inserted to exempt the income of the Core SGF set up by recognised clearing corporation in accordance with regulation as the Central Government may by notification in the Official Gazette specify in this behalf.

12. Income of Investment Fund other than the income chargeable under the head PGBP to be exempt [Section 10(23FBA)] [W.e.f. A.Y. 2016-17]

13. Proportionate income received by unit holder from investment fund which was taxable under PGBP in the hands of the investment fund to be exempt [Section 10(23FBB)] [Inserted w.e.f. A.Y. 2016-17]

14. Income by way of renting or leasing or letting out any real estate asset owned directly by a real estate investment trust to be exempt in the hands of real estate investment trust [Section 10(23FCA)] [Inserted w.e.f. A.Y. 2016-17]

15. Exemption u/s 10(38) in respect of long-term capital gain to be available to the sponsor of business trust [Section 10(38)] [W.e.f. A.Y. 2016-17]

16. Rationalisation of provisions of section 11 relating to accumulation of Income by charitable trusts and institutions [Section 11 & 13] [W.e.f. A.Y. 2016-17]

The following amendments have been made by the Finance Act, 2015 relating to accumulation of income by charitable trusts and institutions:

(A) Amendment of the provisions relating to the income which is treated as deemed to have been applied in the previous year [Clause (2) of the Explanation to section 11(1)] [W.e.f. A.Y. 2016-17]

The existing clause (2) to the Explanation to section 11(1) provides as under:

If the income applied to charitable or religious purposes during the previous year falls short of 85% of the income derived during the year either:

(a) for the reason that whole or part of the income has **not been received during the previous year,** or

(b) for any other reason,

then the charitable trust has been given the option to spend such income for charitable or religious purposes in the following manner:

(i) In case of (a) either during the previous year in which the income is so received or in the immediately following previous year.

(ii) In case of (b) during the previous year immediately following the previous year in which the income was derived.

To avail the facility of the above extended period of application of income, the **trust has to exercise such option in writing before the due date of filing return under section 139(1).**

The words given in bold above have been substituted by the following words:

The trust has to excise such option before the expiry of the time allowed under section 139(1) for furnishing the return of income **in such form or manner as may be prescribed.**

In other words, the words 'in writing' have been substituted by the words in such form or manner as may be prescribed.

(B) Provisions relating to accumulation of income in excess of 15% of the income earned amended [Section 11(2)] [W.e.f. A.Y. 2016-17]

As per section 11(1)(a), the assessee is allowed to accumulate indefinitely upto 15% of the income earned during the year for application for charitable or religious purposes in India in future. If the assessee wants to accumulate or set apart the income in addition to 15% of the income, he cannot do so unless certain conditions prescribed under section 11(2) are satisfied. In this case, the amount accumulated in excess of 15% shall be deemed to have been applied for charitable or religious purposes in India during the previous year itself.

Conditions to be satisfied under existing section 11(2):

(1) Such assessee should give a notice, in writing, in the prescribed form [F. No. 10] and manner, to the Assessing Officer specifying:

(a) the purpose for which the income is being accumulated or set apart;

(b) the period for which the income is to be accumulated or set apart. Such period should not exceed 5 years in any case.

(2) The money so accumulated or set apart should be invested or deposited in the form or mode specified in section 11(5).

In order to remove the ambiguity regarding the period within which the assessee is required to file Form 10, and to ensure due compliance of the above conditions within time, the existing conditions mentioned in sub-section (2) of section 11 have been substituted by the following:

Exemption under section 11(2) shall be allowed subject to the following conditions being satisfied:

"(a) such person furnishes a statement in the prescribed form and in the prescribed manner to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is to be accumulated or set apart, which shall in no case exceed five years;

(b) the money so accumulated or set apart is invested or deposited in the forms or modes specified in section 11(5);

(c) the statement referred to in clause (a) is furnished on or before the due date specified under section 139(1) for furnishing the return of income for the previous year.

Provided that in computing the period of five years referred to in clause (a), the period during which the income could not be applied for the purpose for which it is so accumulated or set apart, due to an order or injunction of any court, shall be excluded.

Consequential amendment due to the new conditions specified under section 11(2)

Exemption under section 11(2) not be allowed unless the statement mentioned in section 11(2)(a) and the return of income of the trust is furnished before the due date of filing the return specified under section 139(1) [Section 13(9) inserted w.e.f. A.Y. 2016-17]

As per section 13(9), nothing contained in section 11(2) shall operate so as to exclude any income from the total income of the previous year of a person in receipt thereof, if—

(i) the statement referred to in clause (a) of section 11(2) (mentioned above) in respect of such income is not furnished on or before the due date specified under section 139(1) for furnishing the return of income for the previous year; or

(ii) the return of income for the previous year is not furnished by such person on or before the due date specified under section 139(1) for furnishing the return of income for the said previous year.

In other words, benefit of accumulation shall not be allowed under section 11(2) unless the said statement in prescribed form as well as the return of income are furnished before the due date of filing the return of income specified under section 139(1).

Amendments relating to "income from Business and Profession"

17. Allowance of balance 50% additional depreciation [Third proviso to section 32(1)(ii) inserted] [W.e.f. A.Y. 2016-17]

To encourage investment in plant or machinery by the manufacturing and power sector, additional depreciation of 20% of the cost of new plant or machinery acquired and installed is allowed under the existing provisions of section 32(1)(iia) of the Act over and above the general depreciation allowance. On the lines of allowability of general depreciation allowance, the second proviso to section 32(1) inter alia provides that the additional depreciation would be restricted to 50% when the new plant or machinery acquired and installed by the assessee, is put to use for the purposes of business or profession for a period of less than one hundred and eighty days in the previous year. Non-availability of full 100% of additional depreciation for acquisition and installation of new plant or machinery in the second half of the year may motivate the assessee to defer such investment to the next year for availing full 100% of additional depreciation in the next year. To remove the discrimination in the matter of allowing additional depreciation on plant or machinery used for less than 180 days and used for 180 days or more, the Act has inserted following third proviso to section 32(1)(ii).

Provided also that where an asset referred to in section 32(1)(iia) (i.e. eligible for addition depreciation @ 20%) or the **first proviso to section 32(1)(iia) (i.e. eligible for addition depreciation @ 35%),** as the case may be, is acquired by the assessee during the previous year and is put to use for the purposes of business for a period of less than one hundred and eighty days in that previous year, and the deduction under this sub-section in respect of such asset is restricted to 50% of the amount calculated at the percentage prescribed for an asset under section 32(1)(iia) for that previous year, then, the deduction for the balance 50% of the amount calculated at the percentage prescribed for such asset under section 32(1)(iia) shall be allowed under this sub-section in the immediately succeeding previous year in respect of such asset.

18. Incentives for the State of Andhra Pradesh, State of Bihar, State of Telangana or State of West Bengal [Section 32(1)(iia) & 32AD] [W.e.f. A.Y. 2016-17]

In order to encourage the setting up of industrial undertakings in the backward areas of the State of Andhra Pradesh, State of Bihar, State of Telangana or State of West Bengal, the Act has provided following Income-tax incentives:

(A) Additional Depreciation at the rate of 35 %

To incentivise investment in new plant or machinery, additional depreciation of 20% is allowed under the existing provisions of section 32(1)(iia) of the Act in respect of the cost of plant or machinery acquired and installed by certain assessees. This depreciation allowance is allowed over and above the deduction allowed for general depreciation under section 32(1)(ii) of the Act. In order to incentivise acquisition and installation of plant and machinery for setting up of manufacturing units in the notified backward area in the State of Andhra Pradesh, or in the State of Bihar, or in the State of Telangana or in the State of West Bengal, the Act has allowed higher additional depreciation at the rate of 35% (instead of 20%) in respect of the actual cost of new machinery or plant (other than a ship and aircraft) acquired and installed by a manufacturing undertaking or enterprise which is set up in the notified backward area in the State of Andhra Pradesh, or in the State of Bihar, or in the State of Telangana or in the State of West Bengal on or after 1.4.2015. This higher additional depreciation shall be available in respect of acquisition and installation of any new machinery or plant for the purposes of the said undertaking or enterprise during the period beginning on the 1.4.2015 and ending before 1.4.2020. The eligible machinery or plant for this purpose shall not include the machinery or plant which are currently not eligible for additional depreciation as per the existing proviso to section 32(1)(iia) of the Act.

Consequential amendments have been made in the second proviso to section 32(1)(ii) of the Act for applying the existing restriction of the allowance to the extent of 50% for assets used for the purpose of business for less than 180 days in the year of acquisition and installation. However, the balance 50% of the allowance will be allowed in the immediately succeeding financial year.

(B) Investment in new plant and machinery in notified backward areas in certain States [Section 32AD]

(1) Manufacturing unit eligible for deduction @ 15% of actual cost of new asset being eligible plant and machinery [Section 32AD(1)]

A new section 32AD has been inserted in the Act to provide for an additional investment allowance of an amount equal to 15% of the cost of new asset acquired and installed by an assessee (whether company or non-company), if—

(a) he sets up an undertaking or enterprise for manufacture or production of any article or thing on or after 01.04.2015 in any backward area notified by the Central Government in this behalf in the State of Andhra Pradesh, or in the State of Bihar, or in the State of Telangana or in the State of West Bengal; and

(b) the new assets are acquired and installed for the purposes of the said undertaking or enterprise during the period beginning from 01.04.2015 & ending before 01.04.2020.

The deduction will be available for the assessment year relevant to the previous year in which the new asset is installed. But in order to avail benefit under section 32AD, the new asset must both be acquired and installed on or after 01.04.2015 but on or before 31.03.2020.

This deduction shall be available over and above the existing deduction available under section 32AC of the Act which is allowed only to a company assessee. Accordingly, if an undertaking is set up in the notified backward areas in the State of Andhra Pradesh, or in the State of Bihar, or in the State of Telangana or in the State of West Bengal by a company, it shall be eligible to claim deduction under the existing provisions of section 32AC of the Act as well as under the new section 32AD if it fulfills the conditions (such as investment above a specified threshold of ₹ 25 crore) specified in the said section 32AC and conditions specified under section 32AD.

(2) Meaning of new asset [Section 32AD(4)]

"New asset" means any new plant or machinery (other than a ship or aircraft), but does not include—

(a) any plant or machinery which before its installation by the assessee was used either within or outside India by any other person;

(b) any plant or machinery installed in any office premises or any residential accommodation, including accommodation in the nature of a guest house;

(b) any office appliances including computers or computer software;

(c) any vehicle;

(d) any plant or machinery, the whole of the actual cost of which is allowed as deduction (whether by way of depreciation or otherwise) in computing the income chargeable under the head "Profits and gains of business or profession" of any previous year.

Note:-

The above "new asset" acquired and installed should not to be sold or otherwise transferred within a period of 5 years from the date of its installation except in connection with amalgamation or demerger.

(3) Consequences if the new asset acquired and installed is transferred within a period of 5 years from the date of its installation except in connection with the amalgamation or demerger or reorganization of business [Section 32AD(2)]

If any new asset acquired and installed by the assessee is sold or otherwise transferred except in connection with the amalgamation or demerger or reorganisation of business referred to in section 47(xiii), (xiiib) or (xiv), within a period of 5 years from the date of its **installation,** the consequence of the same shall be as under:

1. The amount of deduction allowed under section 32AD(1) in respect of such new asset shall be deemed to be income chargeable under the head profit and gains of business and profession of the previous year in which new asset is sold or otherwise transferred.

2. In addition to the above, if any capital gain arises under section 50 on account of transfer of such new asset, that too shall become taxable in that previous year.

(4) Consequences if amalgamated company or resulting company or the successor referred to in section 47(xiii), (xiiib) or (xiv), as the case may be, transfers such assets within 5 years from the date of installation by the amalgamating company or demerged company or the predecessor referred to in section 47(xiii), (xiiib) or (xiv) [Section 32AD(3)]

If after amalgamation or demerger or reorganisation of business referred to in section 47(xiii), (xiiib) or (xiv), the amalgamated company or the resulting company or the successor, as the case may be, sells or transfers any such asset within 5 years from the date of its installation by the amalgamating company or the demerged company or the predecessor referred to in section 47(xiii), (xiiib) or (xiv), then the amalgamated company or resulting company or the successor shall be taxed in the same manner as it would have been taxed in the hands of the amalgamating or demerged company or the predecessor, as the case may be.

19. Prescribed conditions relating to maintenance of accounts, audit etc to be fulfilled by the approved in-house R&D facility [Section 35(2AB)] [W.e.f. A.Y. 2016-17]

In order to have a better and meaningful monitoring mechanism for weighted deduction allowed under section 35(2AB) of the Act, the Act has amended the provisions of section 35(2AB)(3) of the Act to provide that deduction under the said section shall be allowed if the company enters into an agreement with the prescribed authority for cooperation in such research and development facility and **fulfills such conditions with regard to maintenance of account and audit thereof and furnishing of reports in such manner as may be prescribed.**

20. Interest on borrowing for acquisition of an asset, till the date the asset is first put to use not to be allowed as deduction in all cases [Proviso to section 36(1)(iii)] [W.e.f. A.Y. 2016-17]

As per existing provisions of the proviso to section 36(1)(iii), no deduction shall be allowed in respect of any amount of interest paid, in respect of capital borrowed for acquisition of new asset **for extension of existing business or profession** (whether capitalised in the books of account or not) and such amount of interest is for the period beginning from the date on which the capital was borrowed for acquisition of the asset till the date on which such asset was first put to use. Hence, such interest shall be added to the cost of the asset.

The Finance Act, 2015 has omitted the words **"for extension of existing business or profession".**

Hence, the interest on money borrowed for acquisition of a new asset shall not be allowed as deduction till the asset is put to use, whether such asset is acquired for extension of existing business or otherwise. However, such interest shall be added to the cost of the asset.

21. Bad debts to be allowed as deduction only in the year in which they become irrecoverable on the basis of recently notified income computation and disclosure standards without recording the same in the accounts [Section 36(1)(vii)] [W.e.f. A.Y. 2016-17]

Where the amount of debt or part thereof which has been taken into account in computing the income of the assessee of the previous year in which the amount of such debt or part thereof becomes irrecoverable or of an earlier previous year on the basis of income computation and disclosure standards notified under section 145(2) without recording the same in the accounts, then, such debt or part thereof shall be allowed in the previous year in which such debt or part thereof becomes irrecoverable and it shall be deemed that such debt or part thereof has been written off as irrecoverable in the accounts for the purposes of this clause.

22. Expenditure incurred by a cooperative society engaged in the business of manufacture of sugar for purchase of sugarcane at a specified price to be allowed as deduction [Section 36(1)(xvii)] [W.e.f. A.Y. 2016-17]

The amount of expenditure incurred by a cooperative society engaged in the business of manufacture of sugar for purchase of sugarcane at a price which is equal to or less than the price fixed or approved by the Government shall be allowed as a deduction.

Amendments relating to Capital Gains

23. Transfer of shares of a foreign company in a scheme of amalgamation not to be regarded as a transfer [Section 47(viab)] [W.e.f. A.Y. 2016-17]

Any transfer, in a scheme of amalgamation, of a capital asset, being a share of a foreign company, referred to in Explanation 5 to section 9(1)(i), which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the amalgamating foreign company to the amalgamated foreign company shall not be regarded as transfer, if—

(A) at least 25% of the shareholders of the amalgamating foreign company continue to remain shareholders of the amalgamated foreign company; and

(B) such transfer does not attract tax on capital gains in the country in which the amalgamating company is incorporated;

Further, section 49(1)(iii)(e) of the Income-tax Act has also been amended to include transfer under section 47(viab) and to provide that the cost of acquisition of an asset acquired by the amalgamated company shall be the cost for which the amalgamating company acquired the capital asset as increased by the cost of improvement incurred or borne by the amalgamating company or the amalgamated company.

24. Transfer of shares of a foreign company in a scheme of demerger not to be regarded as a transfer [Section 47(vicc)] [W.e.f. A.Y. 2016-17]

Any transfer in a demerger, of a capital asset, being a share of a foreign company, referred to in Explanation 5 to section 9(1)(i), which derives, directly or indirectly, its value substantially from the share or shares of an Indian company, held by the demerged foreign company to the resulting foreign company shall not be regarded as transfer, if,—

(a) the shareholders, holding not less than three-fourths in value of the shares of the demerged foreign company, continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country in which the demerged foreign company is incorporated:

Provided that the provisions of sections 391 to 394 of the Companies Act, 1956 shall not apply in case of demergers referred to in this clause.

Further, section 49(1)(iii)(e) of the Income-tax Act has been amended to include transfer under section 47(vicc) and to provide that the cost of acquisition of an asset acquired by resulting company shall be the cost for which the demerged company acquired the capital asset as increased by the cost of improvement incurred by the demerged company.

25. Tax neutrality on merger of similar schemes of Mutual Funds [Section 47(xviii)] [Inserted w.e.f. A.Y. 2016-17]

Securities and Exchange Board of India has been encouraging mutual funds to consolidate different schemes having similar features so as to have simple and fewer numbers of schemes. However, such mergers/consolidations are treated as transfer and capital gains are imposed on unitholders under the Income-tax Act.

In order to facilitate consolidation of such schemes of mutual funds in the interest of the investors, the Act has provided tax neutrality to unit holders upon consolidation or merger of mutual fund schemes by inserting clause (xviii) in section 47.

Clause (xviii) provides as under:

any transfer by a unit holder of a capital asset, being a unit or units, held by him in the consolidating scheme of a mutual fund, made in consideration of the allotment to him of a capital asset, being a unit or units, in the consolidated scheme of the mutual fund shall not be regarded as transfer.

Provided that the consolidation is of two or more schemes of equity oriented fund **or** of two or more schemes of a fund other than equity oriented fund.

Consequential amendments in other provisions due to insertion of clause (xviii) in section 47

(1) Cost of acquisition of the units of the consolidated scheme acquired in lieu of units held in a consolidating scheme [Section 49(2AD)] [Inserted w.e.f. A.Y. 2016-17]

Where the capital asset, being a unit or units in a consolidated scheme of a mutual fund, became the property of the assessee in consideration of a transfer referred to in section 47(xviii), the cost of acquisition of the asset shall be deemed to be the cost of acquisition to him of the unit or units in the consolidating scheme of the mutual fund.

(2) Period of holding of units of consolidated scheme of mutual funds [Explanation 1 to section 2(42A)] [W.e.f. A.Y. 2016-17]

The following sub-clause (hd) has been inserted in the Explanation 1 to section 2(42A) for determining the time period of holding of the units acquired under the consolidated scheme:

"in the case of a capital asset, being a unit or units, which becomes the property of the assessee in consideration of a transfer referred to in section 47(xviii), there shall be **included** the period for which the unit or units in the consolidating scheme of the mutual fund were held by the assessee".

26. Amendment to section 49

The following amendments have been made to section 49 with effect from the assessment year 2016-17:

- Securities and Exchange Board of India has been encouraging mutual funds to consolidate different schemes having similar features so as to have simple and fewer number of schemes. To provide tax neutrality, section 47 has been amended (as given above). Besides, section 49 has been amended with effect from the assessment year 2016-17 to provide the following –
    1. The cost of acquisition of the units of consolidated scheme shall be the cost of units in the consolidating scheme.
    2. Period of holding of the units of the consolidated scheme shall include the period for which the units in consolidating schemes were held by the assessee.
- Where shares in a company is acquired by a non-resident assessee on redemption of Global Depository Receipts [referred to in section 115AC(1)(b) held by such assessee], the cost of acquisition of such shares shall be calculated on the basis of the price prevailing on any recognised stock exchange on the date on which a request for such redemption was made.

27. Cost of acquisition of a capital asset in the hands of resulting company to be the cost for which the demerged company acquired the capital asset [Section 49(1)(iii)(e)] [W.e.f. A.Y. 2016-17]

Under section 47(vib) of the Income-tax Act any capital asset transferred by the demerged company to the resulting company in the scheme of demerger is not regarded as transfer if the resulting company is an Indian company. In such cases the cost of such asset in the hands of resulting company should be cost of such asset in the hands of demerged company as increased by the cost of improvement, if any, incurred by the demerged company. Further, the period of holding of such asset in the hands of resulting company should include the period for which the asset was held by the demerged company. Under the existing provisions of the Income-tax Act, there is no express provision to this effect. Accordingly, section 49(1)(iii)(e) of the Income-tax Act has been amended to include transfer under section 47(vib) and to provide that the cost of acquisition of an asset acquired by resulting company shall be the cost for which the demerged company acquired the capital asset as increased by the cost of improvement incurred by the demerged company.

Amendments relating to deductions from Gross Total Income

28. Tax benefits under section 80C for the girl child under the Sukanya Samriddhi Account Scheme [Section 80C] [W.r.e.f. A.Y. 2015-16]

Pursuant to the Budget announcement in July 2014, a special small savings instrument for the welfare of the girl child was introduced under the Sukanya Samriddhi Account Rules, 2014. The following tax benefits had been envisaged in the Sukanya Samriddhi Account scheme:

(i) The investments made in the Scheme will be eligible for deduction under section 80C of the Act.

(ii) The interest accruing on deposits in such account will be exempt from income tax.

(iii) The withdrawal from the said scheme in accordance with the rules of the said scheme will be exempt from tax.

The Scheme has been notified under section 80C(2)(viii) vide Notification number 9/2015 S.O.210(E), F. No. 178/3/2015-ITA-I dated 21.01.2015.

The Act has formulized the above benefits envisaged in the Sukanya Samriddhi Account scheme by making the following amendments in the Income Tax Act:

(1) Deduction under section 80C: As per section 80C(2), subscription made to Sukanya Samriddhi Account scheme by the individual in the name of any of the following persons referred to in section 80C(4)(ba) shall be eligible for deduction under section 80C:

   (i) individual, or (ii) any girl child of that individual, or (iii) any girl child for whom such person is the legal guardian, if the scheme so specifies.

(2) Withdrawal from the Sukanya Samriddhi Account shall be exempt under section 10(11A).

A new clause (11A) has been inserted in section 10 of the Act so as to provide that any payment from an account opened in accordance with the Sukanya Samriddhi Account Rules, 2014 made under the Government Saving Bank Act, 1873 shall not be included in the total income of the assessee. As a result, the interest accruing on deposits in, and withdrawals from any account under the scheme would be exempt.

Illustration:

R, an individual resident in India, aged 54 years, submits you the following information for the previous year 2015-16:

	₹
Income under the head salary	6,80,000
Income from house property (self occupied for residence)	(-) 2,00,000
Income from other sources	1,60,000
Amount deposited in PPF	1,20,000
Amount deposited in Sukanya Samridhi Account in the name of girl child	70,000

Compute the tax payable by R for the assessment year 2016-17.

Solution:

Computation of total income and tax payable R for the assessment year 2016-17

	₹	₹
Income under the head salary	6,80,000	
Less: Loss from House Property (self occupied)	2,00,000	4,80,000
Income from house property	(-) 2,00,000	
Less: Set off from income under the head salary	2,00,000	---
Income from other sources		1,60,000
Gross total income		6,40,000
Less: Deduction u/s 80C		
PPF	1,20,000	
Sukanya Samridhi Account	70,000	
	1,90,000	
But limited to maximum ₹ 1,50,000		1,50,000
Total income		4,90,000

	₹	₹
Tax on ₹4,90,000		
First ₹2,50,000	Nil	
Balance ₹2,40,000 — 10%	24,000	
	24,000	
Less: Rebate u/s 87A		
100% of tax or ₹ 2,000 whichever is less	2,000	
	22,000	
Add: Education cess and SHEC @ 3%	660	
	22,660	

29. Raising the limit of deduction under 80CCC [Section 80CCC] [W.e.f. A.Y. 2016-17]

Under the existing provisions contained in section 80CCC(1), an assessee, being an individual is allowed a deduction upto ₹ 1,00,000 in the computation of his total income, of an amount paid or deposited by him to effect or keep in force a contract for any annuity plan of Life Insurance Corporation of India or any other insurer for receiving pension from a fund set up under a pension scheme.

In order to promote social security, the Act has amended section 80CCC(1) so as to raise the limit of deduction under section 80CCC from ₹ 1,00,000 to ₹ 1,50,000, within the overall limit provided in section 80CCE.

30. Additional deduction under 80CCD [Section 80CCD] [W.e.f. A.Y. 2016-17]

Under the existing provisions contained in section 80CCD(1) of the Income-tax Act, 1961 if an individual, employed by the Central Government on or after 1.1.2004, or being an individual employed by any other employer, or any other assessee being an individual has paid or deposited any amount in a previous year in his account under a notified pension scheme, a deduction of such amount not exceeding 10% of his salary in the case of an employee and 10% of the gross total income in case of any other individual is allowed. Similarly, the contribution made by the Central Government or any other employer to the said account of the individual under the pension scheme is also allowed as deduction under section 80CCD(2), to the extent it does not exceed 10% of the salary of the individual in the previous year. Section 80CCD(1A) provides that the amount of deduction under sub-section (1) shall not exceed ₹1,00,000. Till date, under section 80CCD, only the National Pension System (NPS) has been notified by the Ministry of Finance.

With a view to encourage people to contribute towards NPS, the following amendments have been made in section 80CCD:

(i) **Section 80CCD(1A) omitted:** Section 80CCD(1A) which allowed the deduction under section 80CCD(1) to the maximum extent of ₹ 1,00,000 has been omitted. Due to this omission, deduction under section 80CCD(1) will now be allowed within the overall limit of ₹ 1,50,000 provided in section 80CCE.

(ii) **Deduction of ₹ 50,000 under section 80CCD(1B):** In addition to the enhancement of the limit under section 80CCD(1), the Act has inserted a new sub-section (1B) to section 80CCD so as to provide for a deduction in respect of any amount paid, upto ₹50,000 for contributions made by any individual assessees under the NPS, **whether or not any deduction is allowed under section 80CCD(1).**

However, no deduction under section 80CCD(1B) shall be allowed in respect of the amount on which a deduction has been claimed and allowed under section 80CCD(1).

Consequential amendments have also made in section 80CCD(3) to specify that amount which was eligible for deduction under section 80CCD(1B) if, later on, withdrawn as per the scheme shall be taxable. Further, according to section 80CCD(4), the amount so contributed under section 80CCD(1B) shall not be eligible for deduction under section 80C.

Illustration:

R, aged 61 years, a resident in India, submits you the following information for the previous year ending 31-3-2016.

	₹
Income under the head salary	6,00,000
Income from house property	1,10,000
Income from other sources	30,000

He has contributed 10% of basic salary and dearness allowance amounting to ₹50,000 to National Pension Scheme referred to in section 80CCD(1) to which his employer contributes equal amount. He has also deposited ₹ 1,20,000 to his PPF. In addition to amount contributed under section 80CCD(1), he has deposited a sum of ₹ 45,000 in new pension scheme under section 80CCD(1B). Compute the tax payable by R for the assessment year 2016-17.

Solution:

Computation of total income and tax payable by R for the assessment year 2016-17

	₹	₹
Income under the head salary		6,00,000
Income from house property		1,10,000
Income from other sources		30,000
		7,40,000
Less: Deductions under Chapter VI-A		
Section 80C — PPF	1,20,000	
Section 80CCD — Employee contribution	50,000	
	1,70,000	
Limited to ₹ 1,50,000 under section 80CCE	1,50,000	
Employers contribution to National Pension Scheme (Not covered in the overall ceiling of ₹ 1,50,000 under section 80CCE)	50,000	
Contribution to National Pension Scheme covered under section 80CCD(1B)	45,000	2,45,000
Total income		4,95,000

		₹
Tax on ₹ 4,95,000		
First ₹ 3,00,000		Nil
Balance ₹ 1,95,000 — 10%		19,500
		19,500
Less: Rebate u/s 87A 100% of tax or ₹ 2,000 whichever is less		2,000
		17,500
Add: Education cess & SHEC @ 3%		525
		18,025
Rounded off		18,030

31. Amendment in section 80D relating to deduction in respect of health insurance premia [Section 80D] [W.e.f. A.Y. 2016-17]

The existing provisions contained in section 80D, inter alia, provide for deduction of—

(a) upto ₹ 15,000 to an assessee, being an individual in respect of health insurance premia, paid by any mode, other than cash, to effect or to keep in force an insurance on the health of the assessee or his family or any contribution made to the Central Government Health Scheme or any other notified scheme or any payment made on account of preventive health check up of the assessee or his family; and

(b) an additional deduction of ₹15,000 is provided to an individual assessee to effect or to keep in force insurance on the health of the parent or parents of the assessee.

A similar deduction is also available to a Hindu undivided family (HUF) in respect of health insurance premia, paid by any mode, other than cash, to effect or to keep in force insurance on the health of any member of the HUF.

The section also presently provides for a deduction of ₹ 20,000 in both the cases if the person insured is a senior citizen of sixty years of age or above.

The quantum of deduction allowed under section 80D to individuals and HUF in respect of premium paid for health insurance had been fixed vide Finance Act, 2008 at ₹ 15,000 and ₹20,000 (for senior citizens). In view of continuous rise in the cost of medical expenditure, the Act has amended section 80D so as to raise the limit of deduction from ₹ 15,000 to ₹ 25,000. Consequently, the limit of deduction for senior citizens has been raised from ₹ 20,000 to ₹30,000.

Further, very senior citizens are often unable to get health insurance coverage and are therefore unable to take tax benefit under section 80D. Accordingly, as a welfare measure towards very senior citizens, the Act has provided that the whole of the amount paid on account of medical expenditure in respect of a very senior citizen, (if no payment has been made to keep in force an insurance on the health of such person), as does not exceed ₹30,000 shall be allowed as deduction to any of the following persons who has paid such amount:

(a) An individual, provided the amount is incurred by the assessee on himself or any member of his family

(b) HUF, provided the amount is incurred for very senior citizen who is the member of HUF

(c) An individual, provided is the amount incurred for very senior citizen who is the parent of such individual

The aggregate deduction available to any individual in respect of health insurance premia and the medical expenditure incurred would however be limited to ₹ 30,000. Similarly aggregate deduction for health insurance premia and medical expenditure incurred in respect of parents would be limited to ₹30,000.

Example

		₹
(i)	For Individual and his family	
	Health insurance premia	21,000
(ii)	For parents	
	Health insurance of Mother	18,000
	Medical expenditure on father (very senior citizen)	15,000
	Deduction eligible u/s 80D ₹ 21,000 + ₹ 30,000	51,000

Note:-

1. Meaning of senior citizen: "Senior citizen" means an individual resident in India who is of the age of sixty years or more at any time during the relevant previous year.
2. Meaning of very senior citizen: "Very senior citizen" means an individual resident in India who is of the age of eighty years or more at any time during the relevant previous year.

32. Raising the limit of deduction under section 80DD for person with disability and person with severe disability [Section 80DD] [W.e.f. A.Y. 2016-17]

The existing provisions of section 80DD, inter alia, provide for a deduction to an individual or HUF, who is a resident in India, who has incurred—

(a) Expenditure for the medical treatment (including nursing), training and rehabilitation of a dependant, being a person with disability as defined under the said section; or

(b) Paid any amount to LIC or any other insurer in respect of a scheme for the maintenance of a disabled dependant.

The section presently provides for a deduction of ₹ 50,000 if the dependant is suffering from disability and ₹1,00,000 if the dependant is suffering from severe disability (as defined under the said section).

The limits under section 80DD in respect of a person with disability were fixed at ₹ 50,000 by Finance Act, 2003. Further, the limit under section 80DD in respect of a person with severe disability was last enhanced from ₹ 75,000 to ₹ 1,00,000 by Finance (No. 2) Act, 2009.

In view of the rising cost of medical care and special needs of a disabled person, the Act has amended section 80DD so as to raise the limit of deduction in respect of a person with disability from ₹ 50,000 to ₹ 75,000 and in respect of a person with severe disability from ₹1,00,000 to ₹1,25,000.

33. Raising the limit of deduction under section 80DDB [W.e.f. A.Y. 2016-17]

Under the existing provisions of section 80DDB of the Act, an assessee, resident in India is allowed a deduction of a sum not exceeding forty thousand rupees, being the amount actually paid, for the medical treatment of certain chronic and protracted diseases such as Cancer, full blown AIDS, Thalassaemia, Haemophilia etc. specified in rule 3A(2) of Income Tax Rules, 1962. This deduction is allowed up to sixty thousand rupees where the expenditure is in respect of a senior citizen i.e. a person who is of the age of sixty years or more at any time during the relevant previous year.

The above deduction is available to an individual for medical expenditure incurred on himself or a dependant relative. It is also available to a Hindu undivided family (HUF) for such expenditure incurred on its members. Dependant in case of an individual means the spouse, children, parents, brother or sister of an individual and in case of an HUF means a member of the HUF, wholly or mainly dependant on such individual or HUF for his support and maintenance.

Under the existing provisions of this section, a certificate in the prescribed form, from a neurologist, an oncologist, a urologist, a haematologist, an immunologist or such other specialist working in a Government hospital is required. It has been represented that the requirement of a certificate from a doctor working in a Government hospital causes undue hardship to the persons intending to claim the aforesaid deduction. Government hospitals at many places do not have doctors specialising in the above branches of medicine. For this and other reasons, it may be difficult for the taxpayer to obtain a certificate from a Government hospital.

In view of the above, the Act has amended section 80DDB to provide that the assessee will be required to obtain a prescription from a specialist doctor for the purpose of availing this deduction.

Section 80DDB has been further amended to provide for a higher limit of deduction of upto ₹80,000, for the expenditure incurred in respect of the medical treatment of a "very senior citizen". A "very senior citizen" defined as an individual resident in India who is of the age of eighty years or more at any time during the relevant previous year.

34. Tax benefits for Swachh Bharat Kosh and Clean Ganga Fund [Section 80G] [W.r.e.f. A.Y. 2015-16]

With a view to encourage and enhance people's participation in the national effort to improve sanitation facilities and rejuvenation of river Ganga, the Act has amended section 80G of the Act so as to allow 100% deduction from the total income on account of donations made by the specified assessee to the following two funds:

(i) donations made by any assessee (resident and non-resident) to the Swachh Bharat Kosh set up by the Central Government, and

(ii) donations made by a resident assessee to Clean Ganga Fund set up by the Central Government.

However, any sum spent in pursuance of Corporate Social Responsibility under section 135(5) of the Companies Act, 2013 for die above purpose, will not be eligible for deduction from the total income of the assessee.

35. 100% deduction for National Fund for Control of Drug Abuse [Section 80G] [W.e.f. A.Y. 2016-17]

The National Fund for Control of Drug Abuse is a fund created by the Government of India in the year 1989, under section 7A of the Narcotic Drugs and Psychotropic Substances Act, 1985. Since, National Fund for Control of Drug Abuse is also a Fund of national importance, the Act has amended section 80G so as to provide 100% deduction in respect of donations made to the said National Fund for Control of Drug Abuse.

36. Deduction for employment of new workmen [Section 80JJAA] [W.e.f. A.Y. 2016-17]

The existing provisions contained in section 80JJAA of the Act, inter alia, provide for deduction to an Indian company, deriving profits from manufacture of goods in a factory. The quantum of deduction allowed is equal to thirty per cent of additional wages paid to the new regular workmen employed by the assessee in such factory, in the previous year, for three assessment years including the assessment year relevant to the previous year in which such employment is provided.

Section 80JJAA(2)(a), inter alia, provides that no deduction under section 80JJAA(1) shall be available if the factory is hived off or transferred from another existing entity or acquired by the assessee company as a result of amalgamation with another company.

Clause (i) of Explanation to the section defines "Additional wages" to mean the wages paid to the new regular workmen in excess of 100 workmen employed during the previous year.

With a view to encourage generation of employment, the Act has made the following changes in section 80JJAA:

(i) Section 80JJAA(1) has been amended so as to extend the benefit to all assessees having manufacturing units rather than restricting it to company assessees only.

(ii) Section 80JJAA(2)(a) has been amended so as to provide that no deduction under section 80JJAA(1) shall be available if the factory is acquired by the assessee by way of transfer from any other person or as a result of any business re-organisation.

(iii) Clause (i) of the Explanation has been amended so as to provide "additional wages" to mean the wages paid to the new regular workmen in excess of 50 workmen (instead of 100) employed during the previous year.

37. Raising the limit of deduction under section 80U for persons with disability and severe disability [Section 80U] [W.e.f. A.Y. 2016-17]

In view of the rising cost of medical care and special needs of a disabled person, the Act has amended section 80U(1) so as to raise the limit of deduction in respect of a person with disability from ₹50,000 to ₹75,000.

Further, the proviso to section 80U(1) has been amended so as to raise the limit of deduction in respect of a person with severe disability from ₹ 1,00,000 to ₹ 1,25,000.

Amendments relating to Specified Domestic Transactions

38. Raising the threshold limit for specified domestic transactions [Sec. 92BA]

The existing threshold limit for specified domestic transactions of ₹ 5 crore under section 92BA has been extended to ₹ 20 crore from the assessment year 2016-17.

Amendments relating to General Anti-Avoidance Rule (GAAR)

39. Deferment of provisions relating to General Anti-Avoidance Rule (GAAR) [Sec. 95]

Implementation of GAAR has been deferred by 2 years. GAAR provisions will now be applicable to the income of the previous year 2017-18 (assessment year 2018-19) and subsequent years. Further, investments made up to March 31, 2017 will be protected from the applicability of GAAR.

Amendments relating to Determination of Tax in certain special cases

40. Amendment to section 111A

The second proviso to section 111A(1) provides that the provisions of section 111A shall not be applicable in respect of any income arising from transfer of units of a business trust which were acquired by the assessee in exchange of the shares of a special purpose vehicle.

Amendments - The said second proviso has been omitted with effect from the assessment year 2016-17. After the amendment, section 111A will be applicable in respect of any income arising from transfer of units of a business trust which were acquired by the assessee in exchange of the shares of a special purpose vehicle.

41. Reduction in rate of tax on income by way of royalty and fees for technical services in case of non-residents [Sec. 115A]

Royalty and fees for technical services (FTS) received by a non-resident from the Government or an Indian concern, which is not effectively connected with permanent establishment, if any, of the nonresident in India, is currently taxable at the rate of 25 per cent (+SC+EC+SHEC) of gross amount. The rate of 25 per cent has been reduced to 10 per cent (+SC+EC+SHEC) with effect from the assessment year 2016-17.

42. Modification in the taxation scheme of Global Depository Receipts (GDRs) [Sec. 115ACA]

The Depository Receipts Scheme, 2014 was notified by the Department of Economic Affairs in October 2014. This scheme replaces "Issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme, 1993".

New scheme - Under new scheme, Depository Receipts (DRs) can be issued against the securities of listed, unlisted or private or public companies against underlying securities which can be debt instruments, shares or units, etc. Further, both the sponsored issues and unsponsored deposits and acquisitions are permitted under the new scheme. DRs can be freely held and transferred by both residents and non-residents.

Modification in present taxation scheme - The tax benefits under section 115ACA were intended to be provided in respect of sponsored GDRs and listed companies only. Therefore, the present scheme of section 115ACA has been amended (with effect from the assessment year 2016-17) to continue the tax benefits only in respect of such GDRs as were defined in the earlier depository scheme. Under the modified version, "Global Deposit Receipts" means an instrument in the form of a depository receipt or certificate created by the Overseas Depository Bank outside India and issued to investors against the issue of,-

a. ordinary shares of issuing company, being a company listed on a recognised stock exchange in India; or

b. foreign currency convertible bonds of issuing company.

Amendments relating to Minimum Alternate Tax

43. Modification in the scheme of Minimum Alternate Tax [Sec. 115JB]

The following amendments have been made to the scheme of minimum alternate tax under section 115JB from the assessment year 2016-17 onwards –

Share of profit from AOP - In some cases, income of AOP is taxable at the maximum marginal rate of tax (or taxable at a rate higher than maximum marginal rate of tax). Share of profit from such AOP is not taxable in the hands of its members by virtue of section 86. If a joint stock company (say, X Ltd.) is a member of such AOP, share of profit from AOP is not taxable for computing income of the X Ltd. (under normal provisions other than minimum alternate tax provisions). However, under the present provisions, such share of profit from AOP is liable to minimum alternate tax (MAT) in the hands of X Ltd., as there is no provision to exclude such income within the parameters of section 115JB – CIT v. B. Seenaiah & Co. Projects Ltd. [2014] 150 ITD 189 (Hyd. - Trib.), Goldgerg Finance (P.) Ltd. v. CIT [2015] 152 ITD 766 (Mum. - Trib.).

To supersede the above rulings, section 115JB has been amended so as to provide that share of profit from AOP, credited to the profit and loss account of a company (on which no income-tax is payable in accordance with the provisions of section 86), shall be excluded while computing book profit. Likewise, any expenditure (debited to the profit and loss account), corresponding to such income, shall be added back to convert net profit into book profit.

Capital gains, interest, royalty, technical fees of foreign companies - The following incomes of a foreign company will not be subject to minimum alternate tax (MAT) –

Income of foreign company (on which MAT will not be applicable)	Relevant conditions to avoid MAT
a Capital gains arising on transactions in securities Interest, royalty or technical fees chargeable to tax under sections 115A to 115BBE	1. These incomes are credited in the profit and loss account. 2. Income-tax payable in respect of these incomes under normal provisions (other than provisions governing MAT) is less than 18.5 per cent.

Above incomes shall be excluded while computing book profit. Any expenditure (debited to profit and loss account), corresponding to these incomes, shall be added back to convert net profit into book profit.

Notional gain /loss on transfer of shares in SPV to business trust -The following income will not be subject to MAT -

a. notional capital gain on transfer of a share in a special purpose vehicle (SPV) to a business trust in exchange of units allotted by that trust referred to in section 47(xvii); or

b. notional gain resulting from any change in carrying amount of said units.

The above incomes shall be excluded while computing book profit (if these are credited to profit and loss account). Any notional loss [pertaining to (a) or (b) (supra)] shall be added back to convert net profit into book profit (whether or not such notional losses are debited to profit and loss account).

Gain or loss on transfer of units referred to in section 47(xvii) - In respect of transfer of units referred to in section 47(xvii) the following adjustments will be made –

1. Gain on transfer of units referred to in section 47(xvii) shall be deducted from net profit (if it is credited to profit and loss account).

2. Loss on transfer of units referred to in section 47(xvii) shall be added to net profit (whether or not it appears in profit and loss account).

3. The amount of loss on transfer of units referred to in section 47(xvii) computed by taking into account the cost of the shares exchanged with units referred to in the said clause or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through profit or loss account, as the case may be, shall be deducted from net profit to convert it into book profit.

4. Amount of gain [if any, pertaining to transaction mentioned in (3) (supra)] shall be added to net profit to convert it into book profit as per profit and loss account.

44. Amendment to section 115U

Section 115U has been amended (with effect from the assessment year 2016-17) to provide that the existing pass through scheme contained in sections 10(23FB) and 115U shall not apply to investment funds covered by the new regime provided in section 115UB.

45. Modification in taxation regime for Real Estate Investment Trusts (REIT) and Infrastructure Investment -Trusts (InvIT) [Sec. 115UA]

Business trust includes a Real Estate investment Trust (REIT) or an Infrastructure Investment Trust (InvIT) which is registered under regulations framed by SEBI in this regard.

Tax incidence on offloading units of a business trust acquired in exchange of shareholding in SPV - The existing tax regime for the business trust and their investors (as contained in different sections), inter alia, provides for the following -

1. The listed units of a business trust (when traded on a recognised stock exchange) are liable to securities transaction tax (STT). Long-term capital gains is exempt under section 10(38) and the short-term capital gains is taxable at the rate of 15 per cent under section 111A.

2. In case of capital gains arising to the sponsor at the time of exchange of shares in Special Purpose Vehicle (SPV), being the unlisted company through which income generating assets are held indirectly by the business trusts, with units of the business trust, the taxation of gains is deferred.

3. The tax on such gains is to be levied at the time of disposal of units by the sponsor. However, the preferential capital gains regime (consequential to levy of STT) available to other unit holders of a business trust, is not available to the sponsor in respect of these units at the time of their transfer. For the purpose of computing capital gain, the cost of these units is considered as cost of the shares to the sponsor. The holding period of shares is included in computing the holding period of such units.

4. The pass through is provided in respect of income by way of interest received by the business trust from SPV (i.e., there is no taxation of such interest income in the hands of the trust and no withholding tax at the level of SPV). However, TDS at the rate of 5 per cent (in case of payment of interest component of income distributed to non-resident unit holders) and at the rate of 10 per cent (in respect of payment of interest component of distributed income to a resident unit holder) is required by the trust.
5. The dividend received by the trust is subject to dividend distribution tax at the level of SPV and is exempt in the hands of the trust, and the dividend component of the income distributed by the trust to the unit holders is also exempt.

Illogical tax treatment of capital gains - The deferral of capital gains provided to the sponsor of business trust places such a sponsor at a disadvantageous tax position vis-a-vis direct listing of the shares of the SPV. In case sponsor holding the shares of the SPV decides to exit through the Initial Public Offer (IPO) route, then the benefit of concessional tax regime relating to capital gains arising on transfer of shares subject to levy of STT is available to him. The tax on short-term capital gains in such cases is levied at the rate of 15 per cent under section 111A and the long-term capital gain is exempt under section 10(38). The benefit of concessional regime is, however, not available to the sponsor at the time it offloads units of business trust acquired in exchange of its shareholding in the SPV through IPO at the time of listing of business trust on stock exchange.

Amendment - In order to provide uniformity in the case given above, the following amendments have been made -

1. The sponsor would get the same tax treatment on offloading of units under an initial offer on listing of units as it would have been available had he offloaded the underlying shareholding through an IPO.
2. The Finance (No. 2) Act, 2004 has been amended (with effect from June 1, 2015) to provide that STT shall be levied on sale of such units of business trust which are acquired in lieu of shares of SPV, under an Initial offer at the time of listing of units of business trust on similar lines as in the case of sale of unlisted equity shares under an IPO.
3. Section 111A has been amended (with effect from the assessment year 2016-17) to provide the benefit of concessional tax regime of tax at 15 per cent on short-term capital gain. Similarly, section 10(38) has been amended (with effect from the assessment year 2016-17) to provide exemption to long-term capital gain. These benefits will be available to the sponsor on sale of units received in lieu of shares of SPV subject to levy of STT.

Example:

X is a shareholder in S Ltd., a SPV. On January 5, 2015, he gets 1,000 unlisted units in DEF, a business trust, by surrendering his shareholding in S Ltd. These unlisted units in DEF are transferred under an IPO as follows -

- 500 units are transferred on March 30, 2015.
- 300 units are transferred on May 10, 2015.
- 200 units are transferred on June 10, 2015.

Solution:

Tax treatment will be as follows -

1. **Transfer of 500 units on March 30, 2015 -** Capital gain is taxable for the assessment year 2015-16. The amended provisions are applicable from the assessment year 2016-17. Long-term capital gain/short-term capital gain will be taxable under normal provisions. The concessional tax treatment of section 111A in the case of short-term capital gain and exemption under section 10(38) are not available.

2. **Transfer of 300 units on May 10, 2015 -** Units are transferred during the previous year 2015-16 (i.e., assessment year 2016-17). The amended provisions of sections 10(38) and 111A are applicable from the assessment year 2016-17. However, the concession given by these sections is applicable only if securities transaction tax is payable. For this purpose, the Finance (No. 2) Act, 2004 is amended only from June 1, 2015. On May 10, 2015, securities transaction tax is not applicable. Consequently, long-term capital gain/short-term capital gain will be taxable under normal provisions. In the absence of securities transaction tax, the concessional tax treatment of section 111A in the case of short-term capital gain and exemption under section 10(38) are not available.

3. **Transfer of 200 units on June 10, 2015 -** Units are transferred during the previous year 2015-16 (i.e., assessment year 2016-17). Securities transaction tax is applicable from June 1,2015. Short-term capital gain will be taxable in the hands of X under section 111A at the rate of 15% (+SC+EC+SHEC). However, long-term capital gain will be exempt by virtue of section 10(38).

Example:

Suppose in above example, X holds 1,000 unlisted units in DEF directly (no investment through SPV). These units are transferred on the dates given in the example.

Solution:

Securities transaction tax is applicable in the 3 cases. Consequently, in these cases short-term capital gain will be taxable in the hands of X under section 111A at the rate of 15% (+SC+EC+SHEC). However, long-term capital gain will be exempt by virtue of section 10(38).

Rental income of REITs - In case of a business trust, being REITs, the income is predominantly in the nature of rental income. This rental income arises from the assets held directly by REIT or held by it through an SPV. The rental income received at the level of SPV gets passed through by way of interest or dividend to the REIT, the rental income directly received by the REIT is taxable at REIT level and does not get pass through benefit.

Amendments - In order to provide pass through to the rental income arising to REIT from real estate property directly held by it, the following amendments have been made from the assessment year 2016-17-

1. Any income of a business trust, being REIT by way of renting or leasing or letting out any real estate asset owned directly by such business trust shall be exempt under section 10(23FCA).

2. The distributed income (or any part thereof) received by a unit holder from the REIT, which is in the nature of income by way of renting or leasing or letting out any real estate asset owned directly by such REIT, shall be deemed to be income of such unit holder and shall be charged to tax.

3. The REIT shall deduct tax at source on rental income allowed to be passed through. In case of resident unit holder, tax shall deducted at the rate of 10 per cent under section 194LBA and in case of distribution to non-resident unit holder, the tax shall be deducted at rate in force as applicable for deduction of tax on payment to the non-resident of any sum chargeable to tax [i.e., at 30 per cent (+SC+EC+SHEC) if the recipient is a non-resident (not being a foreign company) or at 40 per cent (+SC+EC+SHEC) if the recipient is a foreign company].

4. No tax deduction shall be made under section 194-I where the income by way of rent is credited or paid by a tenant to a business trust, being a REIT, in respect of any real estate asset held directly by such REIT.

Example:

DEF is a real estate investment trust (REIT). It owns house properties in different parts of Maharashtra. Besides, it holds controlling interest in A Ltd. (A Ltd., an Indian company, is SPV created by DEF for the purpose of owning commercial properties). Annual taxable income of DEF is calculated as follows –

	₹ in crore
Rental income from properties directly owned by DEF (annual value : ₹ 13 crore - municipal tax : ₹ 3 crore - standard deduction : ₹ 3 crore)	7
Long-term capital gain on sale of land and buildings directly owned by DEF (computed as per section 48 after deducting indexed cost of acquisition)	20
Interest from A Ltd.	13
Dividend from A Ltd.	10
Total	50

DEF distributes ₹ 40 crore to its unitholders. X is one of the unitholders. He holds 10 per cent units in DEF and is entitled to ₹ 4 crore (before TDS).

The above information pertains to (a) previous year 2014-15 (Situation 1) or (b) previous year 2015-16 (Situation 2).

Solution:

Income of DEF – (₹ in crore)

	AY 2015-16	AY 2016-17
Rental income [exempt under section 10(23FCA)]	7	Nil
Long-term capital gain	20	20
Interest from A Ltd. [exempt under section 10(23FC]	Nil	Nil
Dividend [exempt under section 10(34)]	Nil	Nil
Net Income	27	20
Income-tax [(30% of ₹ 7 crore + 20% of ₹ 20 crore), (20% of ₹ 20 crore)]	6.1	4
Add: Surcharge	0.61	0.48
Income-tax and surcharge	6.71	4.48
Add: Education cess	0.2013	0.1344
Tax liability of DEF	6.9113	4.6144

Income of X –

	AY 2015-16	AY 2016-17
Rental income [₹ 4 crore × ₹ 7 crore ÷ ₹ 50 crore]: ₹0.56 crore	Exempt[1]	0.56
Long-term capital gain [₹4 crore × ₹ 20 crore ÷ ₹ 50 crore]: ₹ 1.6 crore	Exempt[1]	Exempt[1]
Interest [₹ 4 crore × ₹ 13 crore ÷ ₹ 50 crore]: ₹ 1.04 crore	1.04	1.04
Dividend [₹4 crore × ₹ 10 crore ÷ ₹ 50 crore]: ₹ 0.8 crore	Exempt[1]	Exempt[1]
Net income	1.04	1.6

[1] Exempt under section 10(23FD).

46. Pass through status to Category I and Category II Alternative Investment Funds [Sec. 115UB]

The existing provisions of section 10(23FB) provide that any income of a Venture Capital Company (VCC) or a Venture Capital Fund (VCF) from investment in a Venture Capital Undertaking (VCU) shall be exempt from taxation. Section 115U provides that income accruing or arising or received by a person out of investment made in a VCC or VCF shall be taxable in the same manner, on current year basis, as if the person had made direct investment in the VCU.

These sections provide a tax pass through (i.e., income is taxable in the hands of investors instead of VCF/VCC) only to the funds, being set-up as a company or a trust, which are registered (i) before May 21, 2012 as a VCF under SEBI (Venture Capital Funds) Regulations, 1996, or (ii) as venture capital fund [being one of the sub-categories under Category-I Alternative investment fund (AIF) regulated by SEBI (AIF) Regulations, 2012] with effect from May 21, 2012. The existing pass through is available only in respect of income which arises to the fund from investment in VCU, being a company which satisfies the conditions provided in SEBI (VCF) Regulations, 1996 or SEBI (AIF) Regulations, 2012 (AIF regulations).

Under the AIF regulations, various types of AIFs have been classified under three separate categories as Category I, II and III AIFs -

– **Category I** includes AIFs that invest in start-ups or early stage ventures or social ventures or small and medium enterprises (SMEs) or infrastructure or other sectors or areas, which the Government or regulators consider as socially or economically desirable. Category I AIFs are the funds which have positive spillover effects on economy and for which the Government/SEBI/other regulators in India might consider providing incentives or concessions.

– **Category II** AIFs are funds including private equity funds or debt funds which do not fall in Category I and III and which do not undertake leverage or borrowing other than to meet day-to-day operational requirements.

– **Category III** AIFs are funds which employ diverse or complex trading strategies and may employ leverage including through investment in listed or unlisted derivatives. These AIFs are hedge funds or funds, which trade with a view to making short-term returns, or such other funds, which are open ended, for which no specific incentives or concessions are given by the Government or any other regulators.

These funds can be set-up as a trust, company, limited liability partnership and any other body corporate. Similarly, investment by AIFs can be in entities which can be a company, firm, etc.

Pooled investment vehicles (other than hedge funds) engaged in making passive investments have been accorded pass through in certain tax jurisdictions. In order to rationalize the taxation of Category I and Category II AIFs (hereafter referred to as investment fund), a special tax regime has been provided under section 115UB. The salient features of the special regime are given below -

• Income of a person (being a unit holder of an investment fund) out of investments made in the investment fund shall be chargeable to income-tax in the same manner as if it was the income accruing or arising to (or received by) such person, had the investments (made by the investment fund) been made directly by him.

• Income in the hands of investment fund, other than income from profits and gains of business, shall be exempt from tax. The income in the nature of profits and gains of business or profession shall be taxable in the case of investment fund. If investment fund is a company or a firm, such business income will be taxable at the rate applicable to the company or firm. Conversely, if such fund is a person other than company or firm, business income will be taxable at the maximum marginal rate of tax (i.e., at 34.608 per cent for the assessment year 2016-17).

• Income in the hands of investor which is of the same nature as income by way of profits and gain of business at investment fund level shall be exempt.

• Where any income, other than income which is taxable at investment fund level, is payable to a unit holder by an investment fund, the fund shall deduct income-tax at the rate of 10 per cent under section 194LBB (with effect from June 1, 2015).

• The income paid or credited by the investment fund shall be deemed to be of the same nature and in the same proportion in the hands of the unit holder as if it had been received by, or had accrued or arisen to, the investment fund.

- If in any year there is a loss at the fund level (either current loss or the loss which remained to be set off), the loss shall not be allowed to be passed through to the investors but would be carried over at fund level to be set off against income of the next year in accordance with the provisions of Chapter VI.
- The provisions of dividend distribution tax under section 115-O or tax on distributed income under section 115R shall not apply to the income paid by an investment fund to its unit holders.
- The income received by the investment fund would be exempt from TDS requirement [a notification to this effect will be issued under section 197A(1F)].
- It shall be mandatory for the investment fund to file its return of income. The investment fund shall also provide to the prescribed income-tax authority and the investors, the details of various components of income, etc., for the purposes of the scheme.
- The existing pass through regime shall continue to apply to VCF/VCC which had been registered under SEBI (VCF) Regulations, 1996. Remaining VCFs (being part of Category I AIFs) shall be subject to the new pass through regime.

Example:

DEF is an investment fund. There are 20 unit holders. X is one of the unit holders holding 1 unit. For the previous year 2015-16, DEF reports the following income -

₹ in crore

Business income	8
Long-term capital gains	10
Income from other sources	2

After payment of income-tax, the entire post-tax income is distributed to unit holders. Income of X from other sources is bank interest of ₹ 24,60,000. Find out the net income and tax liability of DEF under the following situations -

Situation 1 [DEF (AOP)] - DEF is an Indian trust and has registration certificate as Category I Alternate Investment Fund under SEBI (AIF) Regulations.

Situation 2 [DEF (LLP)] - DEF in the above case is a limited liability partnership in India.

Situation 3 [DEF (Co.)] - DEF in the above case is an Indian company.

Solution:

Computation of income and tax of DEF –

	DEF (AOP) ₹	DEF (LLP) ₹	DEF (Co.) ₹
Business income	8,00,00,000	8,00,00,000	8,00,00,000
Long-term capital gains [exempt under section 10(23FBA)]	-	-	-
Income from other sources [exempt under section 10(23FBA)]	-	-	-
Net income	8,00,00,000	8,00,00,000	8,00,00,000
Tax liability [34.608% (being maximum marginal rate of tax, i.e., IT : 30%, SC : 12%, EC : 3%) in the case of AOP, 34.608% (being applicable rate, i.e., IT : 30%, SC : 12%, EC : 3%) in the case of LLP and 33.063% (being applicable rate, i.e., IT : 30%, SC : 7%, EC : 3%) in the case of company]	2,76,86,400	2,76,86,400	2,64,50,400

Notes –

1. At the time of distribution of income to unit holders, there is no distribution tax or dividend tax under section 115-O or section 115R.

2. When income (pertaining to long-term capital gains and income from other sources) is distributed to unit holders, DEF will deduct tax at source at the rate of 10% (no surcharge/education cess) under section 194LBB. However, there is no TDS if income is paid/credited during April 1, 2015 and May 31, 2015. Moreover, when business income is distributed to unit holders, TDS provisions are not applicable.
3. Minimum alternate tax/alternate minimum tax provisions will not have any impact in the above computation of tax liability.

Computation of income and tax of X - X holds 1 out of 20 (i.e., 5%) units. His income will be calculated as follows -

	₹
Business income received from DEF [exempt under section 10(23FBB)]	Nil
Long-term capital gains received from DEF (5% of ₹ 10,00,00,000)	50,00,000
Income from other sources -	
- received from DEF (i. e., 5% of ₹ 2,00,00,000)	10,00,000
- bank interest	24,60,000
Net income	84,60,000
Income-tax (20% of ₹ 50,00,000 and normal tax on the balance)	18,63,000
Add: Surcharge	Nil
Tax and surcharge	18,63,000
Add: Education cess	55,890
Tax liability	19,18,890

Example:

In the above example, income of DEF pertaining to the previous year 2015-16 is as follows (in place of income given in the table in the original example) –

	₹ In Core
Business income	(-)6
Long-term capital gains	(-)2
Income from other sources	7

No other change in data/information.

Solution:

Computation of income of DEF for the assessment year 2016-17

	DEF (AOP) ₹	**DEF (LLP) ₹**	**DEF (Co.) ₹**
Business loss (it is adjusted against income from other sources)			
Long-term capital loss (it cannot be set off during the current year, it will be carried forward by DEF)	Nil	Nil	Nil
Income from other sources (₹ 7 crore - business loss of ₹ 6 crore)	-	-	-
Less: Exemption under section 10(23 FBA)	1,00,00,000	1,00,00,000	1,00,00,000
Net income	1,00,00,000	1,00,00,000	1,00,00,000
	Nil	Nil	Nil

Computation of income and tax of X - Income of X will be ₹ 29,60,000 (being 5% of ₹ 1 crore + bank interest of ₹ 24,60,000).

Example:

In example above, income of DEF pertaining to the previous year 2016-17 is as follows -

	₹ In Core
Business income	1
Long-term capital gains	5
Income from other sources	4

No other change in data/information.

Solution:

Computation of income of DEF for the assessment year 2017-18 -

	DEF (AOP) ₹	DEF (LLP) ₹	DEF (Co.) ₹
Business income	1,00,00,000	1,00,00,000	1,00,00,000
Long-term capital gains (₹ 5 crore - brought forward long-term capital loss of ₹ 2 crore) [₹ 3 crore is exempt under section 10(23 FBA)]	-		
Income from other sources [₹ 4 crore is exempt under section 10(23FBA)]	-		
Net income	1,00,00,000	1,00,00,000	1,00,00,000
Tax liability* [34.608% (being maximum marginal rate of tax, i.e., IT: 30%, SC : 12%, EC : 3%) in the case of AOP, 30.9% (being applicable rate, i.e., IT: 30%, SC : nil, EC : 3%) in the case of LLP or in the case of company]	34,60,800	30,90,000	30,90,000

*It is assumed that tax rates for the assessment years 2016-17 and 2017-18 will be the same.

Computation of income and tax of X - Income of X will be ₹ 59,60,000 [i.e., long-term capital gain : ₹ 15,00,000 (being 5% of ₹ 3 crore) + income from other sources : ₹ 44,60,000 (being 5% of ₹ 4 crore + bank interest of ₹ 24,60,000)].

Amendments relating to Income-Tax Authorities - Powers

47. Amendment to section 132B

The existing provisions contained in section 132B provide that the assets seized under section 132 or requisitioned under section 132A may be adjusted against the amount of existing liability under the Income-tax Act, the Wealth-tax Act, etc., and the amount of liability determined on completion of assessment. This provision has been amended with effect from June 1, 2015 to provide that the asset seized under section 132 or requisitioned under section 132A may be adjusted against the amount of liability arising on an application made before the Settlement Commission under section 245C(1).

Amendments relating to filing of returns, assessments and re-assessment

48. Compulsory filing of return in relation to assets, etc. located outside India [Fourth proviso to section 139(1)] [W.e.f. A.Y. 2016-17]

Fourth proviso to section 139(1) provides that a person, being a resident other than not ordinarily resident in India, who is not required to furnish a return under section 139(1) and who during the previous year has:

(a) (i) any asset located outside India, or

(ii) any financial interest in any entity located outside India like right to share profit in any entity outside India as partner or member of AOP, etc.

(b) signing authority in any account located outside India,

shall furnish, on or before the due date, a return in respect of his income or loss for the previous year in such form and verified in such manner and setting forth such other particulars as may be prescribed.

The Act has substituted the above fourth proviso by the following:

A person, being a resident other than not ordinarily resident in India within the meaning of section 6(6), who is not required to furnish a return under this sub-section and who at any time during the previous year,—

(a) holds, as a beneficial owner or otherwise, any asset (including any financial interest in any entity) located outside India or has signing authority in any account located outside India; or

(b) is a beneficiary of any asset (including any financial interest in any entity) located outside India,

shall furnish, on or before the due date, a return in respect of his income or loss for the previous year in such form and verified in such manner and setting forth such other particulars as may be prescribed.

Provided also that nothing contained in the fourth proviso shall apply to an individual, being a beneficiary of any asset (including any financial interest in any entity) located outside India when income, if any, arising from such asset is includible in the income of the person referred to in clause (a) of that proviso in accordance with the provisions of this Act.

Note:-

"Beneficial owner" in respect of an asset means an individual who has provided, directly or indirectly, consideration for the asset for the immediate or future benefit, direct or indirect, of himself or any other person.

"Beneficiary" in respect of an asset means an individual who derives benefit from the asset during the previous year and the consideration for such asset has been provided by any person other than such beneficiary.

49. Prescribed form of return of income to also require the assessee to furnish certain additional particulars relating to assets held by him [Section 139(6)] [W.e.f. A.Y. 2016-17]

The Act has amended section 139(6) to provide that, besides other particulars required to be furnished in the form, the form of return of income shall require the assessee to give particulars relating to assets of the prescribed nature and value, held by him as a beneficial owner or otherwise or in which he is a beneficiary.

50. Furnishing of return of income also made mandatory for certain funds or institution [Section 139(4C) & (4F)] [W.e.f. A.Y. 2016-17]

(a) Universities or educational institutions or hospitals or other institutions referred to in section 10(23C) (iiiab) and (iiiac) mandatorily required to furnish return of income [Section 139(4C)] [W.e.f. A.Y. 2016-17]

Under the Income Tax Act, exemption under section 10(23C)(iiiab) and (iiiac), subject to specified conditions, is available to such university or educational institution, hospital or other institution which is **wholly or substantially** financed by the Government.

Under the existing provisions of section 139(4C), besides other institutions specified under that clause, all entities whose income is exempt under section 10(23C)(iiiad), (iiiae), (iv), (v), (vi), (via), are mandatorily required to file their return of income.

The Act has amended section 139(4C) to provide that entities covered under section 10(23C)(iiiab) and (iiiac) i.e. university or educational institution, hospital or other institution which is wholly or substantially financed by the Government shall also be mandatorily required to file their return of income.

In other words, all universities or educational institutions or hospitals or other institution whether financed by the Government or not or whether their gross receipts exceed ₹1 crore or not, will be required to file return of income as per section 139(4C).

(b) Investment fund referred to in section 115UB mandatory required to furnish return of income [Section 139(4F)] [Inserted w.e.f. A.Y. 2016-17]

Every investment fund referred to in section 115UB, which is not required to furnish return of income or loss under any other provisions of this section, shall furnish the return of income in respect of its income or loss in every previous year and all the provisions of this Act shall, so far as may be, apply as if it were a return required to be furnished under section 139(1).

51. Simplification of approval regime for issue of notice for re-assessment [Section 151] [W.e.f. 01-06-2015]

Section 151 of the Act provides for sanction from certain authorities before issue of notice for reassessment of income under section 148. Under certain specified circumstances, the Assessing Officer is required to obtain sanction before issue of notice under section 148. Section 151 specifies different sanctioning authorities based on-(i) whether scrutiny under section 143(3) or section 147 has been made earlier or not, (ii) whether notice is proposed to be issued within or after four years from the end of relevant assessment year, and (iii) the rank of the Assessing Officer proposing to issue notice.

To bring simplicity, section 151 has been substituted by the new section 151 which provides as under:

(1) Where the notice is to be issued after the expiry of 4 years [Section 151(1)]: No notice shall be issued under section 148 by an Assessing Officer, after the expiry of a period of four years from the end of the relevant assessment year, unless the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner is satisfied, on the reasons recorded by the Assessing Officer, that it is a fit case for the issue of such notice.

(2) In any other case: In a case other than a case falling under section 151(1), no notice shall be issued under section 148 by an Assessing Officer, who is below the rank of Joint Commissioner, unless the Joint Commissioner is satisfied, on the reasons recorded by such Assessing Officer, that it is a fit case for the issue of such notice.

However, for the purposes of section 151(1) and section 151(2), the Principal Chief Commissioner or Chief Commissioner or the Principal Commissioner or Commissioner or the Joint Commissioner, as the case may be, being satisfied on the reasons recorded by the Assessing Officer about fitness of a case for the issue of notice under section 148, need not issue such notice himself. [Section 151(3)]

52. Assessment of income of a person other than the person in whose case search has been initiated [Sec. 153C]

Section 153C relates to assessment of income of any other person. The existing provisions provide that where the Assessing Officer is satisfied that any money, bullion, jewellery or other valuable article or thing or books of account or documents seized or requisitioned belong to a person other than searched person, then the books of account, documents, etc., shall be handed over to the Assessing Officer having jurisdiction over such other person and that Assessing Officer shall proceed against such other person. On a plain reading of section 153C, it is evident that the Assessing Officer of the searched person must be "satisfied" that inter alia any document seized or requisitioned "belongs to" a person other than the searched person.

Originals v. Photocopies - Finding of photocopies in the possession of a searched person does not necessarily mean and imply that they (i.e., photocopies) "belong" to the person who holds the originals.

Possession of documents and possession of photocopies of documents are two separate things. Take the case of a search on the premises of Jay Ltd. During search photocopies of certain documents belonging to Peesee Ltd. are recovered from the premises of Jay Ltd. "Photocopies" are owned by Jay Ltd. but original documents belong to Peesee Ltd. Unless it is established that the documents in question (i.e., photocopies in this example) do not belong to Jay Ltd., the question of invoking section 153C does not arise and proceedings cannot be started on Peesee Ltd. - Pepsico India Holdings (P.) Ltd. v. CIT [2014] 50 taxmann.com 299 (Delhi).

Amendment - To supersede the above observations, section 153C has been amended with effect from June 1, 2015. The amended section provides that notwithstanding anything contained in sections 139, 147, 148, 149, 151 and 153, where the Assessing Officer is satisfied that,-

a. any money, bullion, jewellery or other valuable article or thing, seized or requisitioned, belongs to; or

b. any books of account or documents, seized or requisitioned, pertains or pertain to, or any information contained therein, relates to,

any person, other than the searched person, then the books of account or documents or assets seized or requisitioned shall be handed over to the Assessing Officer having jurisdiction over such other person and that Assessing Officer shall proceed against each such other person. hereunto

53. Amendment to section 154

Provisions of section 154 (rectification of mistakes) have been amended with effect from June 1, 2015 so as to insert the reference of "collector" in different sub-sections. Consequently, intimation generated after processing of TCS statement can be rectified under section 154.

54. Amendment to section 156

The existing provisions contained in the proviso to section 156 provide that where any sum is determined to be payable by the assessee or by the deductor under section 143(1) or section 200A(1), the intimation under these sections shall be deemed to be a notice of demand for the purposes of section 156.

The scope of above provision has been extended (with effect from June 1, 2015) to cover intimation generated after processing of TCS statements. The amended provisions provide that where any sum is determined to be payable by the assessee or the deductor or the collector under section 143(1), section 200A(1) or section 206CB(1), the intimation under these sub-sections shall be deemed to be a notice of demand for the purposes of section 156.

Amendments relating to Special procedure for avoiding Repetitive Appeals

55. Procedure for appeal by revenue when an identical question of law is pending before Supreme Court [Sec. 158AA]

Presently, special provisions for avoiding repetitive appeals are given by section 158A.

Existing provisions of section 158A - Section 158A provides that during pendency of proceedings in his case for an assessment year an assessee can submit a claim before the Assessing Officer or any appellate authority that a question of law arising in the instant case for the assessment year under consideration is identical with the question of law already pending in his own case before the High Court or Supreme Court for another assessment year. If the Assessing Officer or any appellate authority agrees to apply the final decision on the question of law in that earlier year in the present year, he will not agitate the same question of law once again for the present year before higher appellate authorities. The Assessing Officer or any appellate authority before whom his case is pending can admit the claim of the assessee. As and when the decision on the question of law becomes final, they will apply the ratio of the decision of the High Court or Supreme Court for that earlier case to the relevant year's case also.

Section 158A not applicable if revenue has to file appeal for subsequent years - There is presently no parallel provision for revenue to not file appeal for subsequent years where the Department is in appeal on the same question of law for an earlier year. As a result, appeals are filed by the revenue year after year on the same question of law until it is finally decided by the Supreme Court, thus, multiplying litigations.

New provisions of section 158AA - New section 158AA has been inserted with effect from June 1, 2015. It is applicable when department is in appeal before the Supreme Court. It provides that where any question of law arising in the case of an assessee for any assessment year is identical with a question of law arising in his case for another assessment year which is pending before the Supreme Court (in an appeal or in a special leave petition) filed by the revenue, against the order of the High Court in favour of the assessee, the Commissioner or Principal Commissioner may (instead of directing the Assessing Officer to appeal to the Appellate Tribunal), direct the Assessing Officer to make an application to the Appellate Tribunal in the prescribed form within 60 days from the date of receipt of order of the Commissioner (Appeals) stating that an appeal on the question of law arising in the relevant case may be filed when the decision on the question of law becomes final in the earlier case.

The Commissioner or Principal Commissioner shall proceed under above provisions only if an acceptance is received from the assessee to the effect that the question of law in the other case is identical to that arising in the relevant case. However, in case no such acceptance is received the Commissioner or Principal Commissioner shall proceed in accordance with the provisions contained in section 253(2)/(2A) and, accordingly, may, if he objects to the order passed by the Commissioner (Appeals), direct the Assessing Officer to appeal to the Appellate Tribunal.

Where the order of the Commissioner (Appeals) is not in conformity with the final decision on the question of law in the other case (if the Supreme Court decides the earlier case in favour of the Department), the Commissioner or Principal Commissioner may direct the Assessing Officer to appeal to the Appellate Tribunal against such order within 60 days from the date on which the order of the Supreme Court is communicated to the Commissioner or Principal Commissioner.

Amendments relating to TDS

56. Employer to obtain evidence/proof regarding deductions, exemptions or allowances claimed by the employee while estimating the income of the employee for the purpose of deduction of tax under section 192 [Section 192] [W.e.f. 01.06.2015]

Under section 192 of the Act, the person responsible for paying (DDO) income chargeable under the head “salaries” under the Act is authorised to allow certain deductions, exemptions or allowances or set-off of certain loss as per the provisions of the Act for the purposes of estimating income of the assessee or computing the amount of the tax deductible under the said section. The evidence/proof/particulars for some of the deductions/exemptions/ allowances/set-off of loss claimed by the employee such as rent receipt for claiming exemption of HRA, evidence of interest payments for claiming loss from self occupied house property etc. is generally not available with the DDO. In these circumstances, the DDO has to depend upon the evidence/particulars furnished, if any, by the employees in support of their claim of deductions, exemptions, etc. As the existing provisions of the Act do not contain any guidance regarding nature of evidence/documents to be obtained by the DDO, there is no uniformity in the approach of the DDO in this matter.

In order to bring clarity in this matter, sub-section (2D) has been inserted in section 192, w.e.f. 01.06.2015 which provides as under:

The person responsible for making the payment referred to in section 192(1) shall, for the purposes of estimating income of the assessee or computing tax deductible under section 192(1), obtain from the assessee the evidence or proof or particulars of prescribed claims (including claim for set-off of loss) under the provisions of the Act **in such form and manner as may be prescribed.**

57. TDS on income in respect of payment of accumulated balance due to an employee under Employees Provident Fund and Miscellaneous Provisions Act, 1952 [Section 192A] [W.e.f. 1-6-2015]

Under the existing provisions of rule 8 of Schedule IV-A of the Act, the withdrawal of accumulated balance by an employee from the RPF is exempt from taxation. However, in order to discourage pre-mature withdrawal and to promote long term savings, it has been provided that such withdrawal shall be taxable if the employee makes withdrawal before continuous service of five years (other than the cases of termination due to ill health, closure of business, etc.) and does not opt for transfer of accumulated balance to new employer. Rule 9 of the said Schedule further provides computation mechanism for determining tax liability of the employee in respect of such pre-mature withdrawal. For ensuring collection of tax in respect of these withdrawals, rule 10 of Schedule IV-A provides that the trustees of the RPF, at the time of payment, shall deduct tax as computed in rule 9 of Schedule IV-A.

Rule 9 of Schedule IV-A of the Act provides that the tax on withdrawn amount is required to be calculated by recomputing the tax liability of the years for which the contribution to RPF has been made by treating the same as contribution to unrecognized provident fund. The trustees of private PF schemes, being generally part of the employer group, have access to or can easily obtain the information regarding taxability of the employee making pre-mature withdrawal for the purposes of computation of the amount of tax liability under rule 9 of the Schedule-IV-A of the Act. However, at times, it is not possible for the trustees of EPFS to get the information regarding taxability of the employee such as year-wise amount of taxable income and tax payable for the purposes of computation of the amount of tax liability under rule 9 of the Schedule-IV-A of the Act.

Therefore, a new section 192A has been inserted w.e.f. 01.06.2015 for deduction of tax which provides as under:

Notwithstanding anything contained in this Act, the trustees of the Employees' Provident Fund Scheme, 1952, framed under section 5 of the Employees' Provident Funds and Miscellaneous Provisions Act, 1952 or any person authorised under the scheme to make payment of accumulated balance due to employees, shall, in a case where the accumulated balance due to an employee participating in a recognised provident fund is includible in his total income owing to the provisions of rule 8 of Part A of the Fourth Schedule not being applicable, at the time of payment of the accumulated balance due to the employee, deduct income-tax thereon at the rate of 10%.

However, no deduction under this section shall be made where the amount of such payment or, as the case may be, the aggregate amount of such payment to the payee is less than ₹ 30,000.

Rate of TDS if PAN is not provided [Second proviso to section 192A]: Any person entitled to receive any amount on which tax is deductible under this section shall furnish his Permanent Account Number to the person responsible for deducting such tax, failing which tax shall be deducted at the maximum marginal rate.

58. Rationalisation of provisions relating to deduction of tax on interest (other than interest on securities) [Section 194A] [W.e.f. 1-6-2015]

The following amendments have been made in section 194A relating to deduction of tax on interest other than interest on securities:

1. Co-operative banks to deduct TDS on time deposits if interest exceeds ₹ 10,000 [Section 194A(3)(v) w.e.f. 01.06.2015]

Section 194A(1) read with section 194A(3)(i) of the Act provide for deduction of tax on interest (other than interest on securities) over a specified threshold, i.e. ₹ 10,000 for interest payment by banks, co-operative society engaged in banking business (co-operative bank) and post office and ₹5,000 for payment of interest by other persons.

There is no difference in the functioning of the co-operative banks and other commercial banks, the Finance Act, 2006 and Finance Act, 2007 amended the provisions of the Act to provide for co-operative banks a taxation regime which is similar to that for the other commercial banks. However, section 194A(3)(v) of the Act provides a general exemption from making tax deduction from payment of interest by all co-operative societies to its members, the co-operative banks tried to avail this exemption by making their depositors as members of different categories. This has led to dispute as to whether the co-operative banks, for which the specific provisions of tax deduction exist in the form of section 194A(1), section 194A(3)(i)(b) and section 194A(3)(viia)(b) of the Act, can take the benefit of general exemption provided to all co-operative societies from deduction of tax on payment of interest to members. There is no rationale for treating the co-operative banks differently from other commercial banks in the matter of deduction of tax and allowing them to avail the exemption meant for smaller credit co-operative societies formed for the benefit of small number of members.

In view of the above, the Act has amended the provisions of the section 194A of the Act to expressly provide from the prospective date of 1st June, 2015 that the exemption provided from deduction of tax from payment of interest to members by a co-operative society under section 194A(3)(v) of the Act shall not apply to the payment of interest on time deposits by the co-operative banks to its members.

However, the existing exemption provided under section 194A(3)(viia)(a) of the Act to primary agricultural credit society or a primary credit society or a co-operative land mortgage bank or a co-operative land development bank from deduction of tax in respect of interest paid on deposit shall continue to apply. Therefore, these co-operative credit societies/banks referred to in said clause (viia)(a) would not be required to deduct tax on interest payment to depositors even after the above amendment. Further, the existing exemption provided under section 194A(3)(v) of the Act from deduction of tax from interest paid by a cooperative society to another co-operative society shall continue to apply to the co-operative bank and, therefore, a co-operative bank shall not be required to deduct tax from the payment of interest on time deposit to a depositor, being a co-operative society.

2. Definition of time deposits amended [Explanation 1 under section 194A(3) w.e.f. 01.06.15]

The existing definition of "time deposits" provided in the section 194A of the Act **excludes** recurring deposit from its scope. Therefore, payment of interest on recurring deposits by banking company or co-operative bank is currently not subject to TDS. The recurring deposit is also made for a fixed tenure and, therefore, the same is akin to time deposit. The Act has therefore, amended the definition of 'time deposits' so as to **include** recurring deposits within its scope for the purposes of deduction of tax under section 194A of the Act. However, the existing threshold limit of ₹ 10,000 for non-deduction of tax shall also be applicable in case of interest payment on recurring deposits to safeguard interests of small depositors.

3. Tax on time deposits to be deducted bank wise instead of branch wise [Second proviso to section 194A(3)(i) inserted w.e.f. 01.06.2015]

Currently, provisions of proviso to section 194A(3)(i) of the Act provide that the interest income for the purpose of deduction of tax by the banking company or the co-operative bank or the public company shall be computed with reference to **a branch of these entities.** As currently, most of these entities are computerised and follow core banking solutions for crediting interest, there is no rationale for continuing branch wise calculation of interest by the entities who have adopted core banking solutions. The Act has therefore amended the provisions of section 194A of the Act to provide that the computation of interest income for the purposes of deduction of tax under section 194A of the Act should be made **with reference to the income credited or paid by the banking company or the co-operative bank or the public company which has adopted core banking solutions.**

4. Tax on interest on compensation amount of Motor Accident Claim to be deducted at the time of payment instead of accrual basis [Section 194A(3)(ix) & (ixa)]

Under section 194A(3)(ix) of the Act, tax is not required to be deducted from the interest credited or paid on the compensation amount awarded by the Motor Accident Claim Tribunal if the amount of such interest credited or paid during a financial year does not exceed ₹ 50,000. Finance (No. 2) Act, 2009 amended the provisions of section 56 of the Act as well as substituted section 145A of the Act to, inter alia, provide that interest income received on compensation or enhanced compensation shall be deemed to be the income of the year in which the same has been received. However, the existing provisions of section 194A of the Act provides for deduction of tax from interest paid or credited on compensation, whichever is earlier. Section 145A(b) of the Act provides an exception to method of accounting contained in section 145 of the Act and mandates for taxation of interest on compensation on receipt basis only. Therefore, deduction of tax on such interest on mercantile/accrual basis results into undue hardship and mismatch.

The Act has therefore, amended the provisions of section 194A of the Income-tax Act, 1961 to provide that deduction of tax under section 194A of the Act from interest payment on the compensation amount awarded by the Motor Accident Claim Tribunal compensation shall be made only at the time of payment, if the amount of such payment or aggregate amount of such payments during a financial year exceeds ₹ 50,000.

In other words, no tax shall be deducted at source from interest on compensation amount awarded by Motor Accident Claim Tribunal in the following cases:

(a) If such interest is credited during the financial year,

(b) If such interest or aggregate of such interest or paid during the financial year does not exceed ₹ 50,000.

59. Clarification regarding deduction of tax from payments made to transporters [Section 194C] [W.e.f. 1-6-2015]

Under the existing provisions of section 194C of the Act payment to contractors is subject to tax deduction at source (TDS) at the rate of 1% in case the payee is an individual or Hindu undivided family and at the rate of 2% in case of other payees if such payment exceeds ₹30,000 or aggregate of such payment in a financial year exceeds ₹75,000. Prior to 01.10.2009, section 194C of the Act provided for exemption from TDS to an individual transporter who did not own more than two goods carriage at any time during the previous year. Subsequently, Finance (No. 2) Act, 2009 substituted section 194C of the Act with effect from 01.10.2009, which inter alia provided for non- deduction of tax from payments made to the contractor during the course of plying, hiring and leasing goods carriage if the contractor furnishes his Permanent Account Number (PAN) to the payer.

The memorandum explaining the provisions of Finance (No. 2) Bill, 2009 indicates that the intention was to exempt only small transport operators (as defined in section 44AE of the Act) from the purview of TDS on furnishing of Permanent Account Number (PAN). Thus, the intention was to reduce the compliance burden on the small transporters. However, the current language of section 194C(6) of the Act does not convey the desired intention and as a result all transporters, irrespective of their size, are claiming exemption from TDS under the existing provisions of section 194C(6) of the Act on furnishing of PAN.

As there is no rationale for exempting payment to all transporters, irrespective of their size, from the purview of TDS, the Act has amended the provisions of section 194C of the Act to expressly provide that the relaxation under section 194C(6) of the Act from non-deduction of tax shall only be applicable to the payment in the nature of transport charges (whether paid by a person engaged in the business of transport or otherwise) made to an contractor who is engaged in the business of transport i.e. plying, hiring or leasing goods carriage and who is eligible to compute income as per the provisions of section 44AE of the Act (i.e. a person who is not owning more than 10 goods carriage at any time during the previous year) and who has also furnished a declaration to this effect along with his PAN.

60. Amendment to section 194-I

Section 194-I has been amended with effect from June 1, 2015. A proviso has been inserted to provide that no deduction shall be made under section 194-I where the income by way of rent is credited or paid to a business trust, being a real estate investment trust, in respect of any real estate asset, referred to in section 10(23FCA), owned directly by such business trust.

61. Amendment to section 194LBA

Section 194LBA is applicable if a business trust distributes any income referred to in section 115UA [being of the nature referred to in section 10(23FC] to its unit holder. In order to provide pass through to the rental income arising to real estate investment trust from real estate property directly held by it, the scope of section 194LBA has been modified. The amended provisions are applicable from June 1, 2015. Under the modified version, real estate investment trust shall deduct tax at source on rental income allowed to be passed through. In case of resident unit holder, tax shall be deducted at the rate of 10 per cent under section 194LBA and in case of distribution to non-resident unit holder, the tax shall be deducted at rate in force as applicable for deduction of tax on payment to the non-resident of any sum chargeable to tax [i.e., at 30 per cent (+SC+EC+SHEC) if the recipient is a non-resident (not being a foreign company) or at 40 per cent (+SC+EC+SHEC) if the recipient is a foreign company].

62. Tax deduction from income in respect of units of investment fund [Sec. 194LBB]

Section 194LBB has been inserted with effect from June 1, 2015. Provisions of this section are given below –

Time of tax deduction - Tax deduction is applicable if a business trust distributes any income referred to in section 115UB [not being business income of the nature referred to in section 10(23FBB)] to its unit holders. Tax is deductible at the time of credit of such payment to the account of the payee or at the time of payment thereof in cash or by the issue of a cheque or draft or by any other mode, whichever is earlier.

Rate of TDS - Tax is deductible at the rate of 10 per cent. If the recipient does not have PAN, tax is deductible at the rate of 20 per cent.

Lower TDS certificate - Provisions of section 197 or section 197A are not applicable.

63. Extension of eligible period of concessional tax rate under section 194LD

The existing provisions of section 194LD provide for lower withholding tax at the rate of 5 per cent in case of interest payable at any time on or after June 1, 2013 but before June 1, 2015 to foreign institutional investors and qualified foreign investors on their investments in Government securities and rupee denominated corporate bonds provided the rate of interest does not exceed the rate notified by the Central Government in this regard.

The limitation date of the eligibility period for benefit of reduced rate of tax available under section 194LC in respect of external commercial borrowings (ECB) has been extended from June 30, 2015 to June 30, 2017 by the Finance (No.2) Act, 2014. On similar lines, section 194LD has been amended to provide that the concessional rate of 5 per cent withholding tax on interest payment under this section will now be available on interest payable up to June 30, 2017.

64. Amendment to section 195(6)

Section 195(6) provides that the person responsible for making payment/credit to a non-resident/ foreign company shall furnish the information relating to payment of any sum in such form and manner as may be prescribed by the Board.

The above provisions of section 195(6) have been amended with effect from June 1, 2015. The amended provisions provide that the person responsible for paying to a non-resident/foreign company, any sum (whether or not chargeable under the provisions of this Act in the hands of recipient) shall furnish the information relating to payment of such sum, in such form and manner, as may be prescribed.

65. Amendment to section 200

Sub-section (2A) has been inserted in section 200 with effect from June 1, 2015. It provides that in case of an office of the Government, where TDS has been paid to the credit of the Central Government without the production of a challan, the Pay and Accounts Officer/Treasury Officer/Cheque Drawing and Disbursing Officer/any other person, who is responsible for crediting TDS to the credit of the Central Government, shall deliver to the prescribed income-tax authority, or to the person authorised by such authority, a statement in such form, verified in such manner, setting forth such particulars and within such time as may be prescribed.

66. Amendment to section 200A

Section 200A provides for processing of TDS statements for determining the amount payable or refundable to the deductor. However, as section 234E was inserted after the insertion of section 200A, the existing provisions of section 200A do not provide for determination of fee payable under section 234E at the time of processing of TDS statements.

Therefore, the above provision has been amended with effect from June 1, 2015 so as to enable computation of fee payable under section 234E at the time of processing of TDS statement under section 200A.

67. Rationalisation of provisions relating to Tax Deduction at Source (TDS) and Tax Collection at Source (TCS) [Section 197A, 200, 200A, 206CB] [W.e.f. 1-6-2015]

The following amendments have been made to rationalise the provisions relating to TDS & TCS:

Fee payable under section 234E to be included for determination of amount payable/refundable while processing of TDS statement [Section 200A]: Finance (No. 2) Act, 2009 inserted section 200A in the Act which provides for processing of TDS statements for determining the amount payable or refundable to the deductor. However, as section 234E was inserted after the insertion of section 200A in the Act. The existing provisions of section 200A of the Act does not provide for determination of fee payable under section 234E of the Act at the time of processing of TDS statements. The Act has therefore, amended the provisions of section 200A of the Act so as to enable computation of fee payable under section 234E of the Act at the time of processing of TDS statement under section 200A of the Act.

Enabling of filing of Form 15G/15H for payment made under life insurance policy [Section 197A] [W.e.f. 1-6-2015]

The Finance (No. 2) Act, 2014, inserted section 194DA in the Act with effect from 01.10.2014 to provide for deduction of tax at source at the rate of 2% from payments made under life insurance policy, which are chargeable to tax. It has been further provided that no deduction shall be made if the aggregate amount of payment during a financial year is less than ₹1,00,000. In spite of providing high threshold for deduction of tax under this section, there may be cases where the tax payable on recipient's total income, including the payment made under life insurance, will be nil.

Similarly, newly inserted section 192A provides for deduction of tax at source at the rate of 10% from payment of accumulated balance due to an employee from recognized provident fund. It has been further provided that no deduction shall be made if the aggregate amount of payment during a financial year **is less than ₹ 30,000.** In this case also tax payable on recipient's total income, including the payment made from recognised provident fund may be nil.

The existing provisions of section 197A of the Act inter alia provide that tax shall not be deducted, if the recipient of the certain payment on which tax is deductible furnishes to the payer a self-declaration in prescribed Form No. 15G/15H declaring that the tax on his estimated total income of the relevant previous year would be nil. The Act has amended section 197A(1A) and (1C) for making the recipients of payments referred to in section 192A and 194DA also eligible for filing self-declaration in Form No. 15G/15H for non-deduction of tax at source in accordance with the provisions of section 197A.

68. Relaxing the requirement of obtaining TAN for certain deductors [Section 203A] [W.e.f. 1-6-2015]

Under the provisions of section 203A of the Act, every person deducting tax (deductor) or collecting tax (collector) is required to obtain Tax Deduction and Collection Account Number (TAN) and quote the same for reporting of tax deduction/collection to the Income-tax Department. However, currently, for reporting of tax deducted from payment over a specified threshold made for acquisition of immovable property (other than rural agricultural land) from a resident transferor under section 194-IA of the Act, the deductor is not required to obtain and quote TAN and he is allowed to report the tax deducted by quoting his Permanent Account Number (PAN).

The obtaining of TAN creates a compliance burden for those individuals or Hindu Undivided Family (HUF) who are not liable for audit under section 44AB of the Act. The quoting of TAN for reporting of Tax Deducted at Source (TDS) is a procedural matter and the same result can also be achieved in certain cases by mandating quoting of PAN especially for the transactions which are likely to be one time transaction such as single transaction of acquisition of immovable property from non-resident by an individual or HUF on which tax is deductible under section 195 of the Act.

To reduce the compliance burden of these types of deductors, the Act has inserted sub-section (3) to section 203A to provide as under:

The provisions of this section (section 203A) shall not apply to such person, as may be notified by the Central Government in this behalf.

In other words, the requirement of obtaining and quoting of TAN under section 203A of the Act shall not apply to the notified deductors or collectors.

69. Amendment to section 206C

Sub-section (3A) has been inserted in section 206C with effect from June 1, 2015. It provides that in case of an office of the Government, where TCS has been paid to the credit of the Central Government without the production of a challan, the Pay and Accounts Officer/Treasury Officer/Cheque Drawing and Disbursing Officer/any other person, who is responsible for crediting TCS to the credit of the Central Government, shall deliver to the prescribed income-tax authority, or to the person authorised by such authority, a statement in such form, verified in such manner, setting forth such particulars and within such time as may be prescribed.

Further, sub-section (3B) has been inserted with effect from June 1, 2015. It provides that person collecting tax at source may also deliver to the prescribed authority, a correction statement for rectification of any mistake or to add, delete or update the information furnished in the quarterly statement.

70. Processing of quarterly TCS statements [Sec. 206CB]

Currently, there does not exist any provision in the Act to enable processing of the TCS statement filed by the collector as available for processing of TDS statement. The mechanism of TCS statement is similar to TDS statement. Section 206CB has been inserted (with effect from June 1, 2015) to provide for processing of TCS statements on the line of existing provisions for processing of TDS statement contained in section 200A. This provision also incorporates the mechanism for computation of fee payable under section 234E.

Intimation - After processing of TCS statement, an intimation is generated specifying the amount payable or refundable. This intimation generated after processing of TCS statement will be (i) subject to rectification under section 154; (ii) appealable under section 246A; and (iii) deemed as notice of demand under section 156.

71. Interest for late payment of amount due as specified in TCS intimation [Sec. 220]

As the intimation generated after processing of TCS statement shall be deemed as a notice of demand under section 156, the failure to pay the tax specified in the intimation shall attract levy of interest as per the provisions of section 220(2). However, section 206C(7) also contains provisions for levy of interest for non-payment of tax specified in the intimation to be issued. To remove the possibility of charging interest on the same amount for the same period of default both under section 206C(7) and section 220(2), section 220 has been amended. The amended section 220 provides that where interest is charged for any period under section 206C(7) on the tax amount specified in the intimation, then no interest shall be charged under section 220(2) on the same amount for the same period.

72. Amendment to section 234B

The following amendments have been made to the scheme of section 234B with effect from June 1, 2015-

- The existing provisions contained in section 234B(3) provide that where the total income is increased on reassessment under section 147/153A, the assessee shall be liable for interest at the rate of 1 per cent on the amount of increase in total income. This interest is presently calculated for the period commencing from date of determination of total income under section 143(1) or on regular assessment and ending on the date of reassessment under section 147/153A.

Interest is charged under section 234B on the principle that the amount of tax determined on the total income [whether determined in intimation under section 143(1) or assessment or reassessment under section 143(3)/147/153A] was the taxpayer's true liability right from the beginning and it was with reference to that amount the advance tax should have been paid within the prescribed due date. Accordingly, section 234B(3) has been amended to provide that the period for which the interest is to be computed will begin from the first day of the assessment year and end on the date of determination of total income under section 147 or section 153A.

- A new sub-section (2A) has been inserted to provide that where an application for settlement is made under section 245C(1), the assessee shall be liable to pay simple interest at the rate of 1 per cent for every month (or part of a month) comprised in the period commencing on the first day of April of such assessment year and ending on the date of making such application, on the additional amount of income-tax. Further, where as a result of an order of the Settlement Commission under section 245D(4) for any assessment year, the amount of total income disclosed in the application under section 245C(1) is increased, the assessee shall be liable to pay simple interest at the rate of 1 per cent for every month (or part of a month) comprised in the period commencing on the first day of April of such assessment year and ending on the date of such order, on the amount by which the tax on the total income determined on the basis of such order exceeds the tax on the total income disclosed in the application filed under section 245C(1).

Where, as a result of a rectification order under section 245D(6B), the amount on which interest was payable under the above provisions has been increased or reduced, as the case may be, the interest shall be increased or reduced accordingly.

73. Settlement Commission

Provisions regulating settlement of cases have been amended with effect from June 1, 2015 as follows -

- An assessee can make an application to the Settlement Commission at any stage of a "case" relating to him. "Case" is defined as any proceeding for assessment/reassessment which may be pending before an Assessing Officer on the date on which an application is made. The proceeding for assessment or reassessment under section 147 is deemed to commence from the date of issue of notice under section 148. Issue relating to escapement of income is often involved in more than one assessment year. In such a case the assessee becomes eligible to approach Settlement Commission only for the assessment year for which notice under section 148 has been issued. Therefore, to take the proceeding for all other assessment years where there is escapement, the assessee becomes eligible only after notice under section 148 has been issued for all such assessment years.

In order to obviate the need for issue of notice in all such assessment years for commencement of pendency, Explanation (i) to section 245A(b) has been amended. After the amendment, a proceeding for assessment or reassessment or recomputation under section 147 shall be deemed to have commenced—

a. from the date on which a notice under section 148 is issued for any assessment year;

b. from the date of issuance of such notice referred to in sub-clause (a), for any other assessment year or assessment years for which a notice under section 148 has not been issued but such notice could have been issued on such date, if the return of income for the other assessment year or assessment years has been furnished under section 139 or in response to a notice under section 142.

In other words, where a notice under section 148 is issued for any assessment year, the assessee can approach Settlement Commission for other assessment years as well (for which notice could have been issued on such date) even if notice under section 148 for such other assessment years has not been issued. However, a return of income for such other assessment years should have been furnished under section 139 or in response to notice under section 142.

- The existing provision contained in the Explanation (iv) to section 245A(b) provides that a proceeding for any assessment year [other than the proceedings of assessment or reassessment referred to in the Explanation (i)/(iii)/(iiia)] shall be deemed to have commenced from the first day of the assessment year and concluded on the date on which the assessment is made. This provision has been amended to provide that a proceeding for any assessment year [other than the proceedings of assessment or reassessment referred to in the Explanation (i)/(iii)/(iiia)] shall be deemed to have commenced from the date on which a return of income is furnished under section 139 or in response to notice under section 142 and concluded on the date on which the assessment is made or on the expiry of 2 years from the end of relevant assessment year, in a case where no assessment is made.
- The existing provision contained in section 245D(6B) provides that the Settlement Commission may, at any time within a period of 6 months from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed under section 245D(4).

There is no provision for additional time where the assessee or the Commissioner files an application for rectification towards the end of the limitation period. Accordingly, the above provision has been amended to provide that the Settlement Commission may, with a view to rectifying any mistake apparent from the record, amend any order passed by it -

a. at any time within a period of 6 months from the end of month in which the order was passed;
b. at any time within the period of 6 months from the end of the month in which an application for rectification has been made by the Principal Commissioner or the Commissioner or the applicant, as the case may be.

Moreover, no application for rectification shall be made by the Principal Commissioner or the Commissioner or the applicant after the expiry of 6 months from the end of the month in which an order under section 245D(4) is passed by the Settlement Commission.

- The existing provision contained in section 245H(1) provides that the Settlement Commission may, if it is satisfied that any person who made the application for settlement under section 245C has co-operated with the Settlement Commission in the proceedings before it and has made a full and true disclosure of his income and the manner in which such income has been derived, grant to such person, immunity from prosecution.

  As immunity is provided from prosecution by the Settlement Commission, section 245H(1) has been amended so as to provide that the Settlement Commission while granting immunity to any person shall record the reasons in writing in the order passed by it.
- The existing provision contained in section 245HA(1) provides for abatement of proceedings in different situations. This section has been amended to provide that where in respect of any application made under section 245C, an order under section 245D(4) has been passed without providing the terms of settlement the proceedings before the Settlement Commission shall abate on the day on which such order was passed.
- The existing provision contained in section 245K provides that where an application of a person has been allowed to be proceeded with under section 245D(1), then such person shall not be subsequently entitled to make an application before Settlement Commission. It further provides that in certain situations the person shall not be entitled to apply for settlement before Settlement Commission.

The restriction is presently applicable to a person, who makes the application under section 245C for settlement. Therefore, an individual who has approached the Settlement Commission once can subsequently approach again through an entity controlled by him. This defeats the purpose of restricting the opportunity of approaching the Settlement Commission only once for any person. Accordingly, section 245K has been modified to provide that any person related to the person who has already approached the Settlement

Commission once, also cannot approach the Settlement Commission subsequently. The "related person" is explained below -

Person who has approached the Settlement Commission	'Related persons" who cannot approach Settlement Commission subsequently
1. Where such person is an individual	Any company in which such person holds more than 50 per cent of the shares or voting power at any time, or any firm or association of persons or body of individuals in which such person is entitled to more than 50 per cent of the profits at any time, or any Hindu undivided family in which such person is a karta.
2. Where such person is a company	Any individual who held more than 50 per cent of the shares or voting power in such company at any time before the date of application before the Settlement Commission by such person.
3. Where such person is a firm or association of persons or body of individuals	Any individual who was entitled to more than 50 per cent of the profits in such firm, association of persons or body of individuals, at any time before the date of application before the Settlement Commission by such person
4. Where such person is an Hindu undivided family	The karta of that Hindu undivided family.

74. Amendment to section 245-0

With effect from April 1, 2015, a person shall be qualified for appointment as law Member from the Indian Legal Service, if he is an Additional Secretary to the Government of India or if he is qualified to be an Additional Secretary to the Government of India.

75. Amendment to section 246A

Section 246A has been amended with effect from June 1, 2015. After the amendment, the intimation generated after processing of TCS quarterly statements will be appealable within the parameters of section 246A.

76. Orders passed under section 10(23C)(vi)/(via) made appealable before ITAT [Sec. 253]

Section 10(23C)(vi) provides that any income received by a person on behalf of any university or other educational institution existing solely for educational purposes and not for purpose of profit, is not liable to tax. Likewise, section, 10(23C)(via) provides that any income received by a person on behalf of any hospital or other institution for treatment of persons suffering from illness or mental defectiveness or treatment of persons during convalescence or persons requiring medical attention, existing solely for philanthropic purposes and not for the purpose of profit, is not liable for tax. However, exemption is available under these provisions only if the educational institute or the hospital is approved by the prescribed authority.

In the above cases, if the prescribed authority refuses to grant approval (which can have significant financial implications for the educational or medical institution), the order of prescribed authority is not appealable before ITAT under the existing provisions of section 253(1). Therefore, section 253(1) has been amended with effect from June 1, 2015. Under the amended provisions an assessee aggrieved by the order passed by the prescribed authority under section 10(23C)(vi)/(via) may appeal to the Appellate Tribunal.

77. Raising of the income-limit in the cases that may be decided by single member bench of ITAT [Sec. 255]

The existing provisions of section 255(3) provides that single member bench may dispose of any case which pertains to an assessee whose total income as computed by the Assessing Officer does not exceed ₹ 5 lakh. With effect from June 1, 2015, the monetary limit of ₹ 5 lakh has been increased to ₹ 15 lakh.

78. Revision of order that is erroneous in so far as it is prejudicial to the interests of revenue [Sec. 263]

If the Principal Commissioner or Commissioner considers that any order passed by the Assessing Officer is "erroneous in so far as it is prejudicial to the interests of the revenue", he may, after giving the assessee an opportunity of being heard and after making an enquiry, pass an order modifying the assessment made by the Assessing Officer or cancelling the assessment and directing fresh assessment.

Amendment - The interpretation of expression "erroneous in so far as it is prejudicial to the interests of the revenue" has been a contentious one. In order to provide clarity on the issue, Explanation 2 has been inserted in section 263(1) with effect from June 1, 2015. This Explanation provides that an order passed by the Assessing Officer shall be deemed to be erroneous in so far as it is prejudicial to the interests of the revenue, if, in the opinion of the Principal Commissioner or Commissioner,—

a. the order is passed without making inquiries or verification which should have been made;

b. the order is passed allowing any relief without inquiring into the claim;

c. the order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or

d. the order has not been passed in accordance with any decision, prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person.

79. Mode of taking or accepting certain loans, deposits and specified sums and mode of repayment of loans or deposits and specified advances [Sees. 269SS and 269T]

In order to curb generation of black money by way of dealings in cash in immovable property transactions, sections 269SS and 269T have been amended with effect from June 1,2015. After the amendment, no person shall accept from any person any loan or deposit or any sum of money, whether as advance or otherwise, in relation to transfer of an immovable property otherwise than by an account-payee cheque/draft or by electronic clearing system through a bank account, if the amount of such loan or deposit or such specified sum is ₹ 20,000 or more. Likewise, no person shall repay any loan or deposit made with it or any specified advance received by it, otherwise than by an account-payee cheque/draft or by electronic clearing system through a bank account, if the amount or aggregate amount of loans or deposits or specified advances is ₹ 20,000 or more. The specified advance shall mean any sum of money in the nature of an advance, by whatever name called, in relation to transfer of an immovable property whether or not the transfer takes place.

Consequential amendments have been made to sections 271D and 271E to provide penalty for failure to comply with the amended provisions of section 269SS and 269T, respectively.

80. Amount of tax sought to be evaded for the purpose of concealment penalty under section 271(1)(c)

Under the existing provision contained in section 271(1)(c) penalty for concealment of income or furnishing inaccurate particulars of income is levied on the "amount of tax sought to be evaded", which has been defined, inter alia, as the difference between the tax due on the income assessed and the tax which would have been chargeable had such total income been reduced by the amount of concealed income.

Concealment of income where tax is payable under MAT - Problems have arisen in the computation of amount of tax sought to be evaded where the concealment of income or furnishing inaccurate particulars of income occurs in the computation of income under provisions of minimum alternate tax (MAT)/alternate minimum tax (AMT) under sections 115JB and 115JC and also under general provisions (i.e., computation of income ignoring MAT/AMT). Courts have held that penalty under section 271(1)(c) cannot be levied in cases where the concealment of income occurs under general provisions and the tax is paid under the provisions of MAT/AMT under sections 115JB and 115JC – CIT v. Aleo Manali Hydro Power (P.) Ltd. [2013] 38 taxmann.com 288 (All.), CIT v. Jindal Polyester & Steel Ltd [2014] 52 taxmann.com 259 (All.).

Is there any revenue loss if tax is payable under MAT/AMT but concealment occurs under general provisions - Tax paid under the provisions of section 115JB or 115JC over and above the tax liability arising under general provisions is available as MAT/AMT credit for set off against future tax liability. Understatement of income and the tax liability thereon under general provisions results in larger amount of such credit becoming available to the assessee for set off in future years. If it is not checked, it will ultimately result in revenue loss in future. Therefore, where concealment of income, as computed under the general provisions, has taken place, penalty under section 271(1)(c) should be leviable even if the tax liability of the assessee for the year has been determined under provisions of MAT/AMT.

Amendment - Accordingly, section 271(1)(c) has been amended from the assessment year 2016-17. The amended version provides that the amount of tax sought to be evaded shall be the summation of tax sought to be evaded under the general provisions and the tax sought to be evaded under the provisions of MAT/ AMT under sections 115JB and 115JC. If, however, amount of concealment of income on any issue is considered both under the general provisions and provisions of MAT/AMT then such amount shall not be considered in computing tax sought to be evaded under provisions of MAT/AMT. Further, in a case where the provisions of MAT/AMT are not applicable, the computation of tax sought to be evaded under the provisions of MAT/AMT shall be ignored.

New definition of "tax sought to be evaded" - To make the above calculations, "tax sought to be evaded" shall be determined in accordance with the following formula -

Tax sought to be evaded = (A-B) + (C-D)	
A =	Amount of tax on the total income assessed as per the provisions other than the provisions contained in section 115JB or section 115JC (hereinafter referred to as "general provisions"
B =	Amount of tax that would have been chargeable had the total income assessed as per the general provisions been reduced by the amount of income in respect of which particulars have been concealed or inaccurate particulars have been furnished
C =	Amount of tax on the total income assessed as per the provisions contained in section 115JB or section 115JC
D =	Amount of tax that would have been chargeable had the total income assessed as per the provisions contained in section 115JB or section 115JC been reduced by the amount of income in respect of which particulars have been concealed or inaccurate particulars have been furnished.

The following points should be noted -

1. Where on any issue concealed income is considered both under MAT/AMT provisions contained in section 115JB or section 115JC and under general provisions, such amount shall not be reduced from total income assessed while determining the amount under Item D.

2. In a case where the provisions contained in section 115JB or section 115JC are not applicable, Item (C- D) in the formula shall be ignored.

3. Where in any case the amount of concealed income has the effect of reducing the loss declared in the return or converting that loss into income, the amount of tax sought to be evaded shall be determined in accordance with the above formula with the modification that the amount to be determined for Item (A - B) in the formula shall be the amount of tax that would have been chargeable on the income in respect of which particulars have been concealed or inaccurate particulars have been furnished had such income been the total income.

Example:

The following information is noted from the records of X Ltd. for the assessment year 2016-17 -

	General provisions ₹	MAT ₹
Income/book profit as per return of income	6,00,000	14,00,000
Add: Addition on estimate basis (not representing concealed income)	50,000	Nil
Add: Amount of concealed income (as per assessment order)	40,000	Nil
Net income/book profit (as per assessment order)	6,90,000	14,00,000
Tax liability/MAT	2,13,210	2,66,770

Tax payable as per assessment order is ₹ 2,66,770. What is tax sought to be evaded for the purpose of concealment penalty under section 271(1)(c)?

Solution:

Tax sought to be evaded will be calculated as follows -

	₹
A = Normal tax on ₹ 6,90,000	2,13,210
B = Normal tax on (₹ 6,90,000 - ₹ 40,000)	2,00,850
C = MAT on ₹ 14,00,000	2,66,770
D = MAT on (₹ 14,00,000 - nit)	2,66,770
Tax sought to be evaded = (A-B) + (C-D)	12,360

Example:

The following information is noted from the records of X Ltd. for the assessment year 2016-17:

	General provisions ₹	MAT ₹
Income/book profit as per return of income	7,00,000	16,00,000
Add: Addition on estimate basis (not representing concealed income)	10,000	Nil
Add: Amount of concealed income (sale to A Ltd. not recorded in books of account as discovered by the Assessing Officer) (as per assessment order)	30,000	30,000
Add: Amount of concealed income (being deliberate attempt to conceal income by claiming higher deduction under section 35, even no explanation is offered) (as per assessment order)	70,000	Nil
Add: Deferred tax (being deliberate attempt by X Ltd. to declare lower book profit by not adding deferred tax which appeared on the debit side or profit and loss account) (as per assessment order)	Nil	80,000
Net income/book profit (as per assessment order)	8,10,000	17,10,000
Tax liability/MAT	2,50,290	3,25,840

Tax payable as per assessment order is ₹ 3,25,840. What is tax sought to be evaded for the purpose of concealment penalty under section 271(1)(c)?

Solution:

Tax sought to be evaded will be calculated as follows -

	₹
A = Normal tax on ₹ 8,10,000	2,50,290
B = Normal tax on (₹ 8,10,000 - ₹ 30,000 - ₹ 70,000)	2,19,390
C = MAT on ₹ 17,10,000	3,25,840
D = MAT on (₹ 17,10,000 - ₹ 80,000) (₹ 30,000 will not be reduced as it is also considered for computing normal income)	3,10,597
Tax sought to be evaded = (A- B) + (C - D)	46,143

Example:

The following information is noted from the records of X Ltd. for the assessment year 2016-17 –

	General provisions ₹	MAT ₹
Income/book profit as per return of income	(-) 6,00,000	17,00,000
Add: Addition on estimate basis (not representing concealed income)	5,000	Nil
Add: Amount of concealed income (sale to A Ltd. not recorded in books of account as discovered by the Assessing Officer) (as per assessment order)	15,000	15,000
Add: Amount of concealed income (being deliberate attempt to conceal income by claiming higher deduction under section 35, even no explanation is offered) (as per assessment order)	7,50,000	Nil
Add: Deferred tax (being deliberate attempt by X Ltd. to declare lower book profit by not adding deferred tax which appeared on the debit side or profit and loss account) (as per assessment order)	Nil	45,000
Net income/book profit (as per assessment order)	1,70,000	17,60,000
Tax liability/MAT	52,530	3,35,368

Tax as per assessment order is ₹ 3,35,368. What is tax sought to be evaded for the purpose of concealment penalty under section 271(1)(c)?

Solution:

Tax sought to be evaded is calculated on the basis of the following formula -

Tax sought to be evaded = (A-B) + (C-D)

This formula is generally followed. If, however, by adding concealed income loss declared in the return of income is reduced or loss declared in the return of income is converted into income, the above formula will be modified. (A-B) in the above formula will be tax that would have been chargeable on the income in respect of which particulars have been concealed. There is no modification in (C- D). In this example, loss declared in the return of income is converted into income (because of addition of concealed income). Consequently, (A-B) will be replaced by tax on concealed income (i.e., tax on ₹ 7,65,000 which comes to ₹ 2,36,385).

Tax sought to be evaded will be calculated as follows -

	₹
A -B = As calculated above	2,36,385
C = MAT on ₹ 17,60,000	3,35,368
D = MAT on (₹ 17,60,000 - ₹ 45,000) (₹ 15,000 will not be reduced as it is also considered for computing normal income)	3,26,793
Tax sought to be evaded = (A - B) + (C- D)	2,44,960

81. Amendments to sections 271D and 271E

Section 271D provides that if a person accepts any loan or deposit in contravention of the provisions of section 269SS, he shall be liable to pay, by way of penalty, a sum equal to the amount of the loan or deposit so accepted. Likewise, section 271E provides that if a person repays any loan or deposit referred to in section 269T otherwise than in accordance with the provisions of that section, he shall be liable to pay, by way of penalty, a sum equal to the amount of the loan or deposit so repaid. These two sections have been amended with effect from June 1, 2015 to incorporate the reference of "specified sum" in section 271D and "specified advance" in section 271E consequent to the modification in sections 269SS and 269T. "Specified advance" means any sum of money in the nature of an advance, by whatever name called, in relation to transfer of an immovable property whether or not the transfer takes place.

82. Penalty for failure to furnish statement by an eligible investment fund [Sec. 271 FAB]

Section 271FAB has been inserted with effect from the assessment year 2016-17. It provides that if any eligible investment fund which is required to furnish a statement or any information and document under section 9A(5) fails to furnish such statement or information and the document within 90 days from the end of the previous year, the concerned income-tax authority may direct that such fund shall pay, by way of penalty, a sum equal to ₹ 5 lakh.

83. Penalty for failure to furnish information or documents under section 285A [Sec. 271GA]

Section 271GA has been inserted with effect from the assessment year 2016-17. It provides that if any Indian concern which is required to furnish any information or document under section 285A, fails to do so, the Income-tax authority, as may be prescribed in the said section 285A, may direct that such Indian concern shall pay, by way of penalty -

a. a sum equal to 2 per cent of the value of the transaction, in respect of which such failure has taken place, if such transaction had the effect of directly or indirectly transferring the right of management or control in relation to the Indian concern;

b. a sum of ₹ 5 lakh in any other case.

84. Penalty for failure to furnish information or furnishing inaccurate information under section 195(6) [Sec. 271-I]

Section 271-I has been inserted with effect from June 1, 2015. It provides that if a person, who is required to furnish information under section 195(6), fails to furnish such information; or furnishes inaccurate information, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of ₹ 1 lakh.

85. Amendment to section 272A

Section 272A has been amended with effect from June 1, 2015 on the following lines -

1. If any person fails to deliver (or cause to be delivered) a statement within the time as may be prescribed under section 200(2A) or section 206C(3A), then such person shall pay, by way of penalty, a sum of ₹ 100 for every day of such default.
2. The above penalty shall not exceed the amount of tax deductible or tax collectible, as the case may be.

86. Amendment to section 273B

Section 273B provides for non-levy of penalty under various sections enumerated in the said section, if the assessee is able to show existence of reasonable cause for the failure for which penalty is leviable.

- This section has been amended with effect from the assessment year 2016-17 so as to include the reference of new section 271FAB relating to penalty for failure to furnish statement or information or document by an eligible investment fund and new section 271GA relating to penalty for failure to furnish information or document under section 285A.
- Further, section 273B has been amended with effect from June 1, 2015 so as to include the reference of new section 271-I.

87. Furnishing of information or document by an Indian concern [Sec. 285A]

Section 285A has been inserted with effect from the assessment year 2016-17. It provides that where any share or interest in a company or entity registered or incorporated outside India derives, directly or indirectly, its value substantially from the assets located in India as referred to in the Explanation 5 to section 9(1)(i), and such company or, as the case may be, entity holds such assets in India through or in an Indian concern, then, any such Indian concern shall, for the purposes of determination of income accruing or arising in India, under section 9(1)(i), furnish within the prescribed period to the prescribed income-tax authority the relevant information or document, in such manner and form as is prescribed in this behalf.

88. Amendment to section 288

Section 288 has been amended (with effect from June 1, 2015).

Certain chartered accountants not to give reports/certificates - The following chartered accountants will not be eligible to furnish audit reports and certificates under different provisions of the Income-tax Act. However, these persons can attend income-tax proceeding before income-tax authorities and ITAT as authorised representative on behalf of the assessee.

In the case of a corporate-assessee - In the case of a company, the person [who is not eligible for appointment as an auditor of the said company in accordance with the provisions of section 141(3) of the Companies Act, 2013], will not be eligible to furnish audit reports and different certificates under different provisions of the Income-tax Act. Under section 141(3) of the Companies Act, the following persons are eligible for appointment as an auditor of a company, namely—

1. A body corporate other than a LLP.
2. An officer or employee of the company.
3. A person who is a partner, or who is in the employment, of an officer or employee of the company.
4. A person who, or his relative or partner—
   i. is holding any security of or interest in the company or its subsidiary, or of its holding or associate company or a subsidiary of such holding company (the relative may hold security or interest in the company of fa« value not exceeding ₹ 1 lakh),
   ii. is indebted to the company, or its subsidiary, or its holding or associate company or a subsidiary of suclholding company, in excess of ₹ 5 lakh,
   iii. has given a guarantee or provided any security in connection with the indebtedness of any third person to the company, or its subsidiary, or its holding or associate company or a subsidiary of such holding company, for exceeding ₹ 1 lakh.

5. A person or a firm who, whether directly or indirectly, has business relationship with the company, or its subsidiary, or its holding or associate company or subsidiary of such holding company or associate company of such nature as may be prescribed [i. e., any commercial purpose not being (a) professional services permitted to be rendered by an auditor under Chartered Accountants Act or under Companies Act, (b) commercial transactions under ordinary course of business at arm's length price like sale of products/ services to the Chartered Accountant as customer].
6. A person whose relative is a director or is in the employment of the company as a director or key managerial personnel.
7. A person who is in full time employment elsewhere or a person or a partner of a firm holding appointment as its auditor, if such persons or partner is at the date of such appointment or reappointment holding appointment as auditor of more than 20 companies.
8. A person who has been convicted by a court of an offence involving fraud and a period of 10 years has not elapsed from the date of such conviction.
9. Any person whose subsidiary or associate company or any other form of entity, is engaged as on the date of appointment in consulting and specialised services as provided in section 144 of the Companies Act.

In the case of a non-corporate assessee - In the case of an assessee (not being a company) the following chartered accountants will not be eligible to furnish audit reports and different certificates under different provisions of the Income-tax Act -

1. The assessee himself or in case of the assessee, being a firm or association of persons or Hindu undivided family, any partner of the firm, or member of the association or the family.
2. In case of the assessee, being a trust or institution, any person referred to in section 13(3)(a)/(b)/(c) and (cc).
3. In case of any person [other than persons referred to in (1) and (2) above], the person who is competent to verify the return under section 139 in accordance with the provisions of section 140.
4. Any relative of any of the persons referred to in (1), (2) and (3) above.
5. An officer or employee of the assessee.
6. An individual who is a partner, or who is in the employment, of an officer or employee of the assessee.
7. An individual who, or his relative or partner—
   i. is holding any security of, or interest in, the assessee (the relative may hold security or interest in the company of face value not exceeding ₹ 1 lakh),
   ii. ii is indebted to the assessee in excess of ₹ 1 lakh,
   iii. Hi has given a guarantee or provided any security in connection with the indebtedness of any third person to the assessee (the relative may give guarantee or provide any security in connection with the indebtedness of any third person to the assessee for an amount not exceeding ₹ 1 lakh).
8. A person who, whether directly or indirectly, has business relationship with the assessee of such nature as may be prescribed.
9. A person who has been convicted by a court of an offence involving fraud and a period of 10 years has not elapsed from the date of such conviction.

Meaning of relative - For the purpose of section 288, relative in relation to an individual means -

a. spouse of the individual;

b. brother or sister of the individual;

c. brother or sister of the spouse of the individual;

d. any lineal ascendant or descendant of the individual;

e. any lineal ascendant or descendant of the spouse of the individual;

f. spouse of a person referred to in (b), (c), (d) or (e) (supra);

g. any lineal descendant of a brother or sister of either the individual or of the spouse of the individual.

Example:

X is a chartered accountant in practice in Mumbai. On June 5, 2015, he holds appointments as a statutory auditor of 21 companies. On June 6, 2015, he wants to sign and upload the following reports/certificates –

1. Tax audit report in Form Nos. 3CA and 3CD pertaining to A Ltd. for the assessment year 2015-16 (professional fees: ₹ 1,80,000).
2. Report in Form No. 3CEA under section 50B(3) relating to computation of capital gain in the case of slump sale made by B & Co. (a partnership firm) during the previous year 2014-15 (professional fees : ₹ 30,000).
3. Audit report section 80-IA(7) for C Ltd. for the assessment year 2015-16 (professional fees : ₹ 5,000).
4. Tax audit under section 44AB for D (D is a sole proprietor having turnover of ₹ 5.5 crore) for the assessment year 2015-16 (professional fees : ₹ 1,05,000).

Solution:

X holds appointment as a statutory auditor of more than 20 companies on June 6, 2015. He will have to vacate the office of the statutory auditor of one of the companies. Till he vacates the office of the statutory auditor of one of the companies, he cannot sign and upload any report/certificate pertaining to a company. However, there is no such limitation for report/certificate pertaining to a person other than a company. Consequently, X is not competent to sign and upload audit reports pertaining to A Ltd. and C Ltd. on June 6, 2015. Slump sale report for B & Co. and tax audit report of D can be signed and uploaded on June 6, 2015.

Convicted person not eligible to act as authorised representative - Any person convicted by a court of an offence involving fraud shall not be eligible to act as authorised representative for a period of 10 years from the date of such conviction.

89. Board to notify rules for giving foreign tax credit [Sec. 295]

Section 91 provides for relief in respect of income-tax on the income which is taxed in India as well as in the country with which there is no Double Taxation Avoidance Agreement (DTAA). It provides that an Indian resident is entitled to a deduction from the Indian income-tax of a sum calculated on such doubly taxed income, at the Indian rate of tax or the rate of tax of said country, whichever is lower. In cases of countries with which India has entered into an agreement for the purposes of avoidance of double taxation under section 90 or section 90A, a relief in respect of income-tax on doubly taxed income is available as per the respective DTAAs.

The Income-tax Act does not provide the manner for granting credit of taxes paid in any country outside India. To provide this, section 295(2) has been amended with effect from June 1, 2015. The amended version provides that CBDT may make rules to provide the procedure for granting relief or deduction, as the case may be, of any income-tax paid in any country or specified territory outside India, under section 90, or under section 90A, or under section 91, against the income-tax payable under the Act.

90. Abolition of levy of wealth-tax under Wealth-tax Act, 1957

Levy of wealth tax under the Wealth-tax Act has been abolished with effect from the assessment year 2016-17.

91. Amendment to the Finance (No. 2) Act, 2004 pertaining to securities transaction tax

The Finance (No. 2) Act, 2004 has been amended with effect from June 1, 2015 to provide that securities transaction tax (STT) shall be levied on sale of such units of business trust which are acquired in lieu of shares of SPV, under an initial offer at the time of listing of units of business trust on similar lines as in the case of sale of unlisted equity shares under an IPO.

It shall be payable by seller at the rate of 0.2 per cent and collected by the lead merchant banker appointed by the business trust in respect of an initial offer.

AMENDMENTS BROUGHT IN BY THE FINANCE ACT, 2015

AMENDMENTS MADE IN INDIRECT TAX ACT

Amendments relating to Central Excise

1. Amendment to section 3A

In the Central Excise Act, 1944 (1 of 1944) (hereinafter referred to as the Central Excise Act), in section 3A, after *Explanation* 2, the following *Explanation* shall be inserted, namely :-

'*Explanation 3.*— For the purposes of sub-sections (2) and (3), the word "factor" includes "factors".'.

2. Amendment of section 11A

In the Central Excise Act, in section 11A,-

(i) sub-sections (5), (6) and (7) shall be omitted;

(ii) in sub-sections (7A), (8) and clause (b) of sub-section (11), the words, brackets and figure "or sub-section (5)", wherever they occur, shall be omitted;

(iii) in *Explanation* 1, -

(A) in clause (b), in sub-clause (ii), the words "on due date" shall be omitted;

(B) after sub-clause (v), the following sub-clause shall be inserted, namely :-

"**(vi)** in the case where only interest is to be recovered, the date of payment of duty to which such interest relates.";

(C) clause (c) shall be omitted;

(iv) after sub-section (15), the following sub-section shall be inserted, namely :-

"**(16)** The provisions of this section shall not apply to a case where the liability of duty not paid or short-paid is self-assessed and declared as duty, payable by the assessee in the periodic returns filed by him, and in such case, recovery of non-payment or short-payment of duty shall be made in such manner as may be prescribed.".

(v) for *Explanation* 2, the following *Explanation* shall be substituted, namely :-

"Explanation 2. — For the removal of doubts, it is hereby declared that any non-levy, short-levy, non-payment, short-payment or erroneous refund where no show cause notice has been issued before the date on which the Finance Bill, 2015 receives the assent of the President, shall be governed by the provisions of section 11A as amended by the Finance Act, 2015.";

3. Substitution of new section for section 11AC

In the Central Excise Act, for section 11AC, the following section shall be substituted, namely :-

"11AC. Penalty for short-levy or non-levy of duty in certain cases. — (1) The amount of penalty for non-levy or short-levy or non-payment or short-payment or erroneous refund shall be as follows :-

(a) where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, for any reason other than the reason of fraud or collusion or any wilful mis-statement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay a penalty not exceeding ten per cent. of the duty so determined or rupees five thousand, whichever is higher :

Provided that where such duty and interest payable under section 11AA is paid either before the issue of show cause notice or within thirty days of issue of show cause notice, no penalty shall be payable by the person liable to pay duty or the person who has paid the duty and all proceedings in respect of said duty and interest shall be deemed to be concluded;

(b) where any duty as determined under sub-section (10) of section 11A and the interest payable thereon under section 11AA in respect of transactions referred to in clause (a) is paid within thirty days of the date of communication of the order of the Central Excise Officer who has determined such duty, the amount of penalty liable to be paid by such person shall be twenty-five per cent. of the penalty imposed, subject to the condition that such reduced penalty is also paid within the period so specified;

(c) where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, by reason of fraud or collusion or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay a penalty equal to the duty so determined :

Provided that in respect of the cases where the details relating to such transactions are recorded in the specified record for the period beginning with the 8th April, 2011 up to the date on which the Finance Bill, 2015 receives the assent of the President (both days inclusive), the penalty shall be fifty per cent. of the duty so determined;

(d) where any duty demanded in a show cause notice and the interest payable thereon under section 11AA, issued in respect of transactions referred to in clause (c), is paid within thirty days of the communication of show cause notice, the amount of penalty liable to be paid by such person shall be fifteen per cent. of the duty demanded, subject to the condition that such reduced penalty is also paid within the period so specified and all proceedings in respect of the said duty, interest and penalty shall be deemed to be concluded;

(e) where any duty as determined under sub-section (10) of section 11A and the interest payable thereon under section 11AA in respect of transactions referred to in clause (c) is paid within thirty days of the date of communication of the order of the Central Excise Officer who has determined such duty, the amount of penalty liable to be paid by such person shall be twenty-five per cent. of the duty so determined, subject to the condition that such reduced penalty is also paid within the period so specified.

(2) Where the appellate authority or tribunal or court modifies the amount of duty of excise determined by the Central Excise Officer under sub-section (10) of section 11A, then, the amount of penalty payable under clause (c) of sub-section (1) and the interest payable under section 11AA shall stand modified accordingly and after taking into account the amount of duty of excise so modified, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay such amount of penalty and interest so modified.

(3) Where the amount of duty or penalty is increased by the appellate authority or tribunal or court over the amount determined under sub-section (10) of section 11A by the Central Excise Officer, the time within which the interest and the reduced penalty is payable under clause (b) or clause (e) of sub-section (1) in relation to such increased amount of duty shall be counted from the date of the order of the appellate authority or tribunal or court.

Explanation 1. — For the removal of doubts, it is hereby declared that–

(i) any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where no show cause notice has been issued before the date on which the Finance Bill, 2015 receives the assent of the President shall be governed by the provisions of section 11AC as amended by the Finance Act, 2015;

(ii) any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where show cause notice has been issued but an order determining duty under sub-section (10) of section 11A has not been passed before the date on which the Finance Bill, 2015 receives the assent of the President, shall be eligible to closure of proceedings on payment of duty and interest under the proviso to clause (a) of sub-section (1) or on payment of duty, interest and penalty under clause (d) of sub-section (1), subject to the condition that the payment of duty, interest and penalty, as the case may be, is made within thirty days from the date on which the Finance Bill, 2015 receives the assent of the President;

(iii) any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where an order determining duty under sub-section (10) of section 11A is passed after the date on which the Finance Bill, 2015 receives the assent of the President shall be eligible to payment of reduced penalty under clause (b) or clause (e) of sub-section (1), subject to the condition that the payment of duty, interest and penalty is made within thirty days of the communication of the order.

***Explanation 2.* –** For the purposes of this section, the expression "specified records" means records maintained by the person chargeable with the duty in accordance with any law for the time being in force and includes computerised records.".

4. Amendment of section 31

In the Central Excise Act, in section 31, in clause (c), in the proviso, the words "in any appeal or revision, as the case may be," shall be omitted.

5. Amendment of section 32

In the Central Excise Act, in section 32, in sub-section (3), the proviso shall be omitted.

6. Amendment of section 32B

In the Central Excise Act, in section 32B, for the words ", as the case may be, such one of the Vice-Chairmen", at both the places where they occur, the words "the Member" shall be substituted.

7. Amendment of section 32E

In the Central Excise Act, in section 32E, sub-section (1A) shall be omitted.

8. Amendment of section 32F

In the Central Excise Act, in section 32F, in sub-section (6), for the words, figures and letters "on or before the 31st day of May, 2007, later than the 29th day of February, 2008 and in respect of an application made on or after the 1st day of June, 2007," shall be omitted.

9. Omission of section 32H

In the Central Excise Act, section 32H shall be omitted.

10. Amendment of section 32K

In the Central Excise Act, in section 32K, in sub-section (1), the *Explanation* shall be omitted.

11. Amendment of section 32-O

In the Central Excise Act, in section 32-O, in sub-section (1),-

(a) in clause (i), the words, brackets, figures and letters "passed under sub-section (7) of section 32F, as it stood immediately before the commencement of section 122 of the Finance Act, 2007 (22 of 2007) or sub-section (5) of section 32F" shall be omitted;

(b) in clause (ii), the words, brackets, figures and letter "under the said sub-section (7), as it stood immediately before the commencement of section 122 of the Finance Act, 2007 (22 of 2007) or sub-section (5) of section 32F" shall be omitted.

12. Amendment of section 37

In the Central Excise Act, in section 37, in sub-sections (4) and (5), for the words "two thousand rupees", the words "five thousand rupees" shall be substituted.

13. Amendment of notification issued under section 5A of the Central Excise Act

(1) The notification of the Government of India in the Ministry of Finance (Department of Revenue) number G.S.R. 163 (E), dated the 17th March, 2012, issued under sub-section (1) of section 5A of the Central Excise Act, 1944 (1 of 1944) (hereinafter referred to as the Central Excise Act), shall stand amended and shall be deemed to have been amended, retrospectively, in the manner specified in column (2) of the Third Schedule, on and from and up to the date specified in column (3) of that Schedule.

(2) For the purposes of sub-section (1), the Central Government shall have and shall be deemed to have the power to amend the notification with retrospective effect as if the Central Government had the power to amend the said notification under sub-section (1) of section 5A of the Central Excise Act, retrospectively, at all material times.

(3) Refund shall be made of all such duty of excise which has been collected but which would not have been so collected, had the notification referred to in sub-section (1), been in force at all material times, subject to the provisions of section 11B of the Central Excise Act.

(4) Notwithstanding anything contained in section 11B of the Central Excise Act, an application for the claim of refund of duty of excise under sub-section (3) shall be made within a period of six months from the date on which the Finance Bill, 2015 receives the assent of the President.

14. Amendment of Third Schedule

In the Central Excise Act, the Third Schedule shall be amended in the manner specified in the Fourth Schedule.

Amendments relating to Central Excise Tariff

15. Amendment of First Schedule

In the Central Excise Tariff Act, 1985 (hereinafter referred to as Central Excise Tariff Act), the First Schedule shall be amended in the manner specified in the Fifth Schedule.

Amendments relating to CENVAT Credit Rules

[Notification No. 6/2015-C.E.(N.T.) dated 01.03.2015]

Amendments w.e.f. 1.3.2015

1. Education Cess and Secondary & Higher Education Cess leviable on all excisable goods are fully exempted. Simultaneously the standard advalorem rate of duty of Excise, i.e. CENVAT is being increased from 12 to 12.5% w.e.f. 1.3.2015.

2. As per earlier provisions of sub-rule (1) of Rule 4, if inputs were directly delivered from supplier to job worker, the credit can be availed by the manufacturer only on receipt of the processed goods from the job worker. The said rule has now been amended to provide that even if the inputs are directly sent to the job worker on the directions of the manufacturer, credit can be availed immediately and the manufacturer need not wait for the processed goods to be received from the job worker.

Similarly, if the capital goods are sent directly to a job worker on the directions of a manufacturer or the service provider, the credit can be taken immediately to the extent of the 50% of the total duty paid on such capital goods in the same financial year.

3. As per the earlier provisions, CENVAT Credit was allowed to be availed on inputs and input services within six months from the date of invoice. This restriction have been extended to one year from the date of invoice.

4. The earlier provisions of Rule 4(5)(a), were applicable to both inputs and capital goods. As per the new provisions, separate provisions are made applicable for inputs and capital goods as under:

5. Provisions applicable for inputs - 4(5)(a)(i)

The credit shall be allowed on inputs if the inputs are sent to a job worker or even from one job worker to another job worker and likewise and the time limit for receiving the processed goods back by the manufacturer is within 180 days from the date of sending the inputs from the factory. Similarly, inputs can also be directly sent to a job worker without being first brought to the premises of a manufacturer subject to the condition that the processed goods should come back within 180 days from the date of receipt of the inputs by the job worker.

6. Provisions applicable for capital goods - 4(5)(a)(ii)

The credit on capital goods shall be allowed even if they are sent as such to a job worker for further processing subject to the condition that the same is received back within two years from the date of sending the capital goods from the factory. Similarly, capital goods can also be directly sent to a job worker without being first brought to the premises of a manufacturer subject to the condition that the capital goods should come back within two years from the date of receipt of the capital goods by the job worker.

In view of the above, as per the amended provisions, the time limit for receiving back the processed inputs from the job worker will continue to remain 180 days, while in case of capital goods the time limit has been increased to two years. Further, if the inputs/capital goods are not received back within the prescribed time limit, attributable credit on it needs to be reversed. However, as and when the same are received back from the job worker, the credit originally reversed can be restored by the manufacturer/service provider on their own.

7. For claiming refund of CENVAT credit under Rule 5 of CENVAT Credit Rules, 2004, the term "Export Goods" has been defined as any goods which are to be taken out of India to a place of out of India.

8. As per sub-rule (1) of Rule 6, CENVAT credit shall not be allowed on inputs used in relation to the manufacture of exempted goods. Explanation-I has been added to this sub-rule to provide that exempted goods shall include non-excisable goods cleared for a consideration from the factory. Further, as per Explanation-II of this sub-rule, value to be considered for such non-excisable goods for reversal of CENVAT credit to be made shall be the invoice value and where such value is not available, it will be determined by a reasonable means consistent with the principles of valuation contained in the Central Excise Act, and Rules.

9. Sub-rule (4) of Rule 9 provides for maintenance of records by the First Stage Dealer or the Second Stage Dealer. Now the said provisions are made applicable to an importer also who issues an invoice on which CENVAT credit can be taken.

10. As per Rule 12AAA, certain restrictions are imposed in order to avoid misuse of CENVAT credit by the manufacturer, first and second stage dealer, provider of taxable service or an exporter. The said restrictions are now applicable to a registered importer also.

11. Rule 14 has been amended to provide that where the credit has been taken wrongly and even if not utilized, the same can be recovered from manufacturer/service provider and the provisions of Section 11A of the Central Excise Act, 1944 or Section 73 of the Finance Act, 1994 shall be applicable for effecting such recoveries.

Amendments w.e.f. 1.4.2015

12. Earlier, as per sub-rule (7) of Rule 4, in case of service tax paid by the service receiver under full reverse charge mechanism, CENVAT credit was allowed to be availed on making of service tax payment even if value of the service is not paid to the service provider. Similarly, in case of service tax paid under partial reverse charge mechanism, CENVAT credit was allowed to be availed on making payment of value of service as well as portion of the service tax payable by the service receiver.

Now as per the amended provisions, the service tax paid both under partial and full reverse charge by the service receiver, credit of service tax payable by the service recipient is allowed to be availed after making payment of service tax and even if value of the service is not paid. However, if the payment of value of input service and the service tax paid as indicated in the invoice of the manufacturer/ service provider is not made within three months of the date of the invoice, the manufacturer/service provider has to reverse the credit availed, and as and when the payment of the value and service tax thereon as indicated in the invoice is made to the service provider, the credit can be restored on their own, by the manufacturer/service provider.

13. Payment to be made by the manufacturer/service provider by debiting the CENVAT credit account or otherwise, on or before 5th/6th of the following month except in March where payment shall be made on or before 31st March, the same was earlier applicable only for sub-rule (7) of Rule 4, which has now been made applicable to entire Rule 4. Therefore all the debits/CENVAT credit reversals to be made under this Rule are to be made only at the month-end along with duty paid on normal finished goods clearances.

Amendments w.e.f. enactment of Finance Act.

14. As per rule 15, in case of CENVAT credit wrongly taken or utilized on inputs, capital goods or input services, earlier the penal provisions under Section 11AC of the Central Excise Act was not applicable, if the credit wrongly availed is not by a reason of fraud, collusion or any willful mis-statement or suppression of fact, etc. However, as per the amended provisions of Rule 15, even if merely by availing or utilizing the credit wrongly without by reason of fraud or collusion, etc., the provisions of Section 11 AC of Central Excise Act, 1944 or Section 76 of the Finance Act, 1944, will now get attracted.

15. **Restrictions on utilization of CENVAT Credit [Notification No. 25/2014-CE(NT) dated 25.08.2014]**

In case of misuse of CENVAT credit, certain restrictions are provided on the assessees, such as utilization of CENVAT credit, suspension of registration, etc. These restrictions were earlier applicable only to manufacturer, first stage/ second stage dealers and exporters. By amending Rule 12AAA of CENVAT Credit Rules, 2004, these restrictions are made applicable to a provider of taxable services also.

16. **Documents for availing CENVAT Credit [Notification No.26/2014-CE(NT) dated 27.08.2014]**

Services provided in relation to transport of goods by rail became a taxable service w.e.f. 1.10.2012, accordingly a new clause (fa) has been inserted in Rule 9(1) of CENVAT Credit Rules, 2004, to allow certificate issued by Railways to be a valid a duty paying document for availing credit.

17. **Place of Removal [Circular No. 988/12/2014-CX dated 20.10.2014]**

With effect from 11.7.2014, the definition of "Place of removal" has been added in the CENVAT Credit Rules, 2004. Accordingly, CBEC has clarified the place where sale has token place or when the property in goods passes from the seller to the buyer is the relevant consideration to determine the place of removal.

18. **CENVAT Credit for Cellular Service Provider [F. No. 267/60/2014-CX.8 dated 11.11.2014]**

Cellular Mobile Service Provider is not entitled to avail CENVAT credit on Tower Parts & Pre-fabricated buildings. This is based on Judgement of Hon'ble Bombay High Court in the case of M/s Bharti Airtel Ltd. vs. CCE, Pune III (2014-TIOL-1452-HC-MUM-ST).

19. **Recredit of CENVAT credit reversed earlier [Circular No. 990/14/2014-CX-8 dated 19.11.2014]**

Clarification issued by CBEC regarding non-applicability of six months' time limit for availing recredit of the CENVAT credit reversed earlier under three different situations.

20. **Utilisation of Education Cess and Secondary and Higher Education Cess [Notification No. 12/2015-C.E. (N.T.), dated 30-4-2015]**

In rule 3, in sub-rule (7), in clause (b), after the second proviso, the following shall be substituted, namely :-

"Provided also that the credit of Education Cess and Secondary and Higher Education Cess paid on inputs or capital goods received in the factory of manufacture of final product on or after the 1st day of March, 2015 can be utilized for payment of the duty of excise leviable under the First Schedule to the Excise Tariff Act :

Provided also that the credit of balance fifty per cent. Education Cess and Secondary and Higher Education Cess paid on capital goods received in the factory of manufacture of final product in the financial year 2014-15 can be utilized for payment of the duty of excise specified in the First Schedule to the Excise Tariff Act :

Provided also that the credit of Education Cess and Secondary and Higher Education Cess paid on input services received by the manufacturer of final product on or after the 1st day of March, 2015 can be utilized for payment of the duty of excise specified in the First Schedule to the Excise Tariff Act.".

21. **Revision of rate of Central Excise duty for assessee opting not to maintain separate accounts [Notification No. 14/2015-C.E. (N.T.), dated 19-5-2015, w.e.f. 01-06-15]**

In the CENVAT Credit Rules, 2004, in rule 6, in sub-rule (3), -

(a) in clause (i), after the words "goods and", the words "seven per cent. of value of the" shall be inserted.

(b) in the second proviso, for the word "six", the word "seven" shall be substituted.

22. Refund of Cenvat credit to service provider providing services taxed on reverse charge basis [Notification No. 15/2015-C.E. (N.T.), dated 19-5-2015]

In exercise of the powers conferred by rule 5B of the CENVAT Credit Rules, 2004, the Central Board of Excise and Customs hereby makes the following amendments in the notification No. 12/2014-C.E (N.T.), dated 3rd March, 2014, published in the Gazette of India, Extraordinary, Part II, Section 3, Sub-section (i) vide number G.S.R. 139(E), dated the 3rd March, 2014, except as thing done or omitted to be done with respect to supply of manpower for any purpose or security services upto and including 31st March, 2015, namely :-

In the said notification,

(i) In paragraph 1, relating to safeguards, conditions and limitations, in sub-paragraph (a), clause (ii) shall be omitted;

(ii) In Form A, in paragraph (a), in the table, Sl. No. 2 and the entries relating thereto shall be omitted.

Amendments relating to Customs Act

1. Amendment of section 28

In the Customs Act, 1962 (52 of 1962) (hereinafter referred to as the Customs Act), in section 28,—

(a) in sub-section (2), the following proviso shall be inserted, namely :—

"Provided that where notice under clause (a) of sub-section (1) has been served and the proper officer is of the opinion that the amount of duty along with interest payable thereon under section 28AA or the amount of interest, as the case may be, as specified in the notice, has been paid in full within thirty days from the date of receipt of the notice, no penalty shall be levied and the proceedings against such person or other persons to whom the said notice is served under clause (a) of sub-section (1) shall be deemed to be concluded.";

(b) in sub-section (5), for the words "twenty-five per cent.", the words "fifteen per cent." shall be substituted;

(c) after *Explanation 2*, the following *Explanation* shall be inserted, namely :—

"Explanation 3.— For the removal of doubts, it is hereby declared that the proceedings in respect of any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where show cause notice has been issued under sub-section (1) or sub-section (4), as the case may be, but an order determining duty under sub-section (8) has not been passed before the date on which the Finance Bill, 2015 receives the assent of the President, shall, without prejudice to the provisions of sections 135, 135A and 140, as may be applicable, be deemed to be concluded, if the payment of duty, interest and penalty under the proviso to sub-section (2) or under sub-section (5), as the case may be, is made in full within thirty days from the date on which such assent is received.".

2. Amendment of section 112

In the Customs Act, in section 112, in clause (b), for sub-clause (ii), the following sub-clause shall be substituted, namely:-

"**(ii)** in the case of dutiable goods, other than prohibited goods, subject to the provisions of section

114A, to a penalty not exceeding ten per cent. of the duty sought to be evaded or five thousand rupees, whichever is higher :

Provided that where such duty as determined under sub-section (8) of section 28 and the interest payable thereon under section 28AA is paid within thirty days from the date of communication of the order of the proper officer determining such duty, the amount of penalty liable to be paid by such person under this section shall be twenty-five per cent. of the penalty so determined;".

3. Amendment of section 114

In the Customs Act, in section 114, for clause (ii), the following clause shall be substituted, namely:—

"**(ii)** in the case of dutiable goods, other than prohibited goods, subject to the provisions of section 114A, to a penalty not exceeding ten per cent. of the duty sought to be evaded or five thousand rupees, whichever is higher :

Provided that where such duty as determined under sub-section (8) of section 28 and the interest payable thereon under section 28AA is paid within thirty days from the date of communication of the order of the proper officer determining such duty, the amount of penalty liable to be paid by such person under this section shall be twenty-five per cent. of the penalty so determined;".

4. Amendment of section 127A

In the Customs Act, in section 127A, in clause (b), in the proviso, the words "in any appeal or revision, as the case may be," shall be omitted.

5. Amendment of section 127B

In the Customs Act, in section 127B, sub-section (1A) shall be omitted.

6. Amendment of section 127C

In the Customs Act, in section 127C, sub-section (6) shall be omitted.

7. Omission of section 127E

In the Customs Act, section 127E shall be omitted.

8. Amendment of section 127H

In the Customs Act, in section 127H, in sub-section (1), the *Explanation* shall be omitted.

9. Amendment of section 127L

In the Customs Act, in section 127L, in sub-section (1),—

(a) in clause (i), the words, brackets, figures and letters "passed under sub-section (7) of section 127C, as it stood immediately before the commencement of section 102 of the Finance Act, 2007 (22 of 2007) or sub-section (5) of section 127C" shall be omitted;

(b) in clause (ii), the words, brackets, figures and letter "under said sub-section (7), as it stood immediately before the commencement of section 102 of the Finance Act, 2007 (22 of 2007) or sub-section (5) of section 127C" shall be omitted.

Amendments relating to Customs Tariff

10. Amendment of First Schedule

In the Customs Tariff Act, 1975 (51 of 1975) (hereinafter referred to as the Customs Tariff Act), the First Schedule shall be amended in the manner specified in the Second Schedule.

Amendments relating to Service Tax

1. Amendment of section 65B

In the Finance Act, 1994 (32 of 1994.) (hereinafter referred to as the 1994 Act), save as otherwise provided, in section 65B, —

(a) clause (9) shall be omitted with effect from such date as the Central Government may, by notification in the Official Gazette, appoint;

(b) after clause (23), the following clause shall be inserted, namely :—

'**(23A)** "foreman of chit fund" shall have the same meaning as is assigned to the term "foreman" in clause (j) of section 2 of the Chit Funds Act, 1982 (40 of 1982);';

(c) clause (24) shall be omitted with effect from such date as the Central Government may, by notification in the Official Gazette, appoint;

(d) after clause (26), the following clause shall be inserted, namely :—

'**(26A)** "Government" means the Departments of the Central Government, a State Government and its Departments and a Union territory and its Departments, but shall not include any entity, whether created by a statute or otherwise, the accounts of which are not required to be kept in accordance with article 150 of the Constitution or the rules made thereunder;';

(e) after clause (31), the following clause shall be inserted, namely :—

'**(31A)** "lottery distributor or selling agent" means a person appointed or authorised by a State for the purposes of promoting, marketing, selling or facilitating in organising lottery of any kind, in any manner, organised by such State in accordance with the provisions of the Lotteries (Regulation) Act, 1998 (17 of 1998);'

(f) in clause (40), the words "alcoholic liquors for human consumption," shall be omitted with effect from such date as the Central Government may, by notification in the Official Gazette, appoint;

(g) in clause (44), for *Explanation 2,* the following *Explanation* shall be substituted, namely :—

'***Explanation 2.*** - For the purposes of this clause, the expression "transaction in money or actionable claim" shall not include —

(i) any activity relating to use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a separate consideration is charged;

(ii) any activity carried out, for a consideration, in relation to, or for facilitation of, a transaction in money or actionable claim, including the activity carried out —

(a) by a lottery distributor or selling agent in relation to promotion, marketing, organising, selling of lottery or facilitating in organising lottery of any kind, in any other manner;

(b) by a foreman of chit fund for conducting or organising a chit in any manner.';

(h) clause (49) shall be omitted with effect from such date as the Central Government may, by notification in the Official Gazette, appoint.

2. Amendment of section 66B

In section 66B of the 1994 Act, with effect from such date as the Central Government may, by notification in the Official Gazette, appoint, for the words "twelve per cent.", the words "fourteen percent." shall be substituted.

3. Amendment of section 66D

In section 66D of the 1994 Act, with effect from such date as the Central Government may, by notification in the Official Gazette, appoint, —

(1) in clause (a), in sub-clause (iv), for the words "support services", the words "any service" shall be substituted;

(2) for clause (f), the following clause shall be substituted, namely :—

"**(f)** services by way of carrying out any process amounting to manufacture or production of goods excluding alcoholic liquor for human consumption;";

(3) in clause (i), the following *Explanation* shall be inserted, namely :—

'***Explanation.*** - For the purposes of this clause, the expression "betting, gambling or lottery" shall not include the activity specified in *Explanation 2* to clause (44) of section 65B;';

(4) clause (j) shall be omitted.

4. Amendment of section 66F

In section 66F of the 1994 Act, in sub-section (1), the following *Illustration* shall be inserted, namely :—

Illustration:

The services by the Reserve Bank of India, being the main service within the meaning of clause (b) of section 66D, does not include any agency service provided or agreed to be provided by any bank to the Reserve Bank of India. Such agency service, being input service, used by the Reserve Bank of India for providing the main service, for which the consideration by way of fee or commission or any other amount is received by the agent bank, does not get excluded from the levy of service tax by virtue of inclusion of the main service in clause (b) of the negative list in section 66D and hence, such service is leviable to service tax.'.

5. Amendment of section 67

In section 67 of the 1994 Act, in the *Explanation*, for clause (a), the following clause shall be substituted, namely :—

'**(a)** "consideration" includes —

(i) any amount that is payable for the taxable services provided or to be provided;

(ii) any reimbursable expenditure or cost incurred by the service provider and charged, in the course of providing or agreeing to provide a taxable service, except in such circumstances, and subject to such conditions, as may be prescribed;

(iii) any amount retained by the lottery distributor or selling agent from gross sale amount of lottery ticket in addition to the fee or commission, if any, or, as the case may be, the discount received, that is to say, the difference in the face value of lottery ticket and the price at which the distributor or selling agent gets such ticket.'.

6. Amendment of section 73

In section 73 of the 1994 Act, —

(i) after sub-section (1A), the following sub-section shall be inserted, namely :—

"**(1B)** Notwithstanding anything contained in sub-section (1), in a case where the amount of service tax payable has been self-assessed in the return furnished under sub-section (1) of section 70, but not paid either in full or in part, the same shall be recovered along with interest thereon in any of the modes specified in section 87, without service of notice under sub-section (1).";

(ii) sub-section (4A) shall be omitted.

7. Substitution of new section for section 76

For section 76 of the 1994 Act, the following section shall be substituted, namely :—

"76. Penalty for failure to pay service tax. —

(1) Where service tax has not been levied or paid, or has been short-levied or short-paid, or erroneously refunded, for any reason, other than the reason of fraud or collusion or wilful mis-statement or suppression of facts or contravention of any of the provisions of this Chapter or of the rules made thereunder with the intent to evade payment of service tax, the person who has been served notice under sub-section (1) of section 73 shall, in addition to the service tax and interest specified in the notice, be also liable to pay a penalty not exceeding ten per cent. of the amount of such service tax:

Provided that where service tax and interest is paid within a period of thirty days of —

(i) the date of service of notice under sub-section (1) of section 73, no penalty shall be payable and proceedings in respect of such service tax and interest shall be deemed to be concluded;

(ii) the date of receipt of the order of the Central Excise Officer determining the amount of service tax under sub-section (2) of section 73, the penalty payable shall be twenty-five per cent. of the penalty imposed in that order, only if such reduced penalty is also paid within such period.

(2) Where the amount of penalty is increased by the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be, over the above the amount as determined under sub-section (2) of section 73, the time within which the reduced penalty is payable under clause (ii) of the proviso to sub-section (1) in relation to such increased amount of penalty shall be counted from the date of the order of the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be.".

8. Substitution of new section for section 78

For section 78 of the 1994 Act, the following section shall be substituted, namely :—

"78. Penalty for failure to pay service tax for reasons of fraud, etc. —

(1) Where any service tax has not been levied or paid, or has been short-levied or short-paid, or erroneously refunded, by reason of fraud or collusion or wilful mis-statement or suppression of facts or contravention of any of the provisions of this Chapter or of the rules made thereunder with the intent to evade payment of service tax, the person who has been served notice under the proviso to sub-section (1) of section 73 shall, in addition to the service tax and interest specified in the notice, be also liable to pay a penalty which shall be equal to hundred per cent. of the amount of such service tax.

Provided that in respect of the cases where the details relating to such transactions are recorded in the specified records for the period beginning with the 8th April, 2011 upto the date on which the Finance Bill, 2015 receives the assent of the President (both days inclusive), the penalty shall be fifty per cent. of the service tax so determined :

Provided further that where service tax and interest is paid within a period of thirty days of —

(i) the date of service of notice under the proviso to sub-section (1) of section 73, the penalty payable shall be fifteen per cent. of such service tax and proceedings in respect of such service tax, interest and penalty shall be deemed to be concluded;

(ii) the date of receipt of the order of the Central Excise Officer determining the amount of service tax under sub-section (2) of section 73, the penalty payable shall be twenty-five per cent. of the service tax so determined :

Provided also that the benefit of reduced penalty under the second proviso shall be available only if the amount of such reduced penalty is also paid within such period :

***Explanation*. —** For the purposes of this sub-section, "specified records" means records including computerised data as are required to be maintained by an assessee in accordance with any law for the time being in force or where there is no such requirement, the invoices recorded by the assessee in the books of accounts shall be considered as the specified records.

(2) Where the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be, modifies the amount of service tax determined under sub-section (2) of section 73, then, the amount of penalty payable under sub-section (1) and the interest payable thereon under section 75 shall stand modified accordingly, and after taking into account the amount of service tax so modified, the person who is liable to pay such amount of service tax, shall also be liable to pay the amount of penalty and interest so modified.

(3) Where the amount of service tax or penalty is increased by the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be, over and above the amount as determined under sub-section (2) of section 73, the time within which the interest and the reduced penalty is payable under clause (ii) of the second proviso to sub-section (1) in relation to such increased amount of service tax shall be counted from the date of the order of the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be.

9. Insertion of new section 78B

After section 78A of the 1994 Act, the following section shall be inserted, namely :—

"78B. Transitory provisions. — **(1)** Where, in any case,—

(a) service tax has not been levied or paid or has been short-levied or short-paid or erroneously refunded and no notice has been served under sub-section (1) of section 73 or under the proviso thereto, before the date on which the Finance Bill, 2015 receives the assent of the President; or

(b) service tax has not been levied or paid or has been short-levied or short-paid or erroneously refunded and a notice has been served under sub-section (1) of section 73 or under the proviso thereto, but no order has been passed under sub-section (2) of section 73, before the date on which the Finance Bill, 2015 receives the assent of the President, then, in respect of such cases, the provisions of section 76 or section 78, as the case may be, as amended by the Finance Act, 2015 shall be applicable.

(2) In cases where show cause notice has been issued under sub-section (1) of section 73 or under the proviso thereto, but no order has been passed under sub-section (2) of section 73 before the date on which the Finance Bill, 2015 receives the assent of the President, the period of thirty days for the purpose of closure of proceedings on the payment of service tax and interest under clause (i) of the proviso to sub-section (1) of section 76 or on the payment of service tax, interest and penalty under clause (i) of the second proviso to sub-section (1) of section 78, shall be counted from the date on which the Finance Bill, 2015 receives the assent of the President."

10. Omission of section 80

Section 80 of the 1994 Act (1 of 1994) shall be omitted.

11. Amendment of section 86

In section 86 of the 1994 Act, in sub-section (1), —

(a) for the words "Any assessee", the words "Save as otherwise provided herein, an assessee" shall be substituted;

(b) the following provisos shall be inserted, namely :-

"Provided that where an order, relating to a service which is exported, has been passed under section 85 and the matter relates to grant of rebate of service tax on input services, or rebate of duty paid on inputs, used in providing such service, such order shall be dealt with in accordance with the provisions of section 35EE of the Central Excise Act, 1944 (1 of 1944) :

Provided further that all appeals filed before the Appellate Tribunal in respect of matters covered under the first proviso, after the coming into force of the Finance Act, 2012 (23 of 2012), and pending before it up to the date on which the Finance Bill, 2015 receives the assent of the President, shall be transferred and dealt with in accordance with the provisions of section 35EE of the Central Excise Act, 1944 (1 of 1944).".

12. Amendment of section 94

In section 94 of the 1994 Act, in sub-section (2), for clause (aa), the following clause shall be substituted, namely :—

"**(aa)** determination of the amount and value of taxable service, the manner thereof, and the circumstances and conditions under which an amount shall not be a consideration, under section 67;".

Study Note - 1

CANONS OF TAXATION

This Study Note includes

1.1 Basis for Taxation

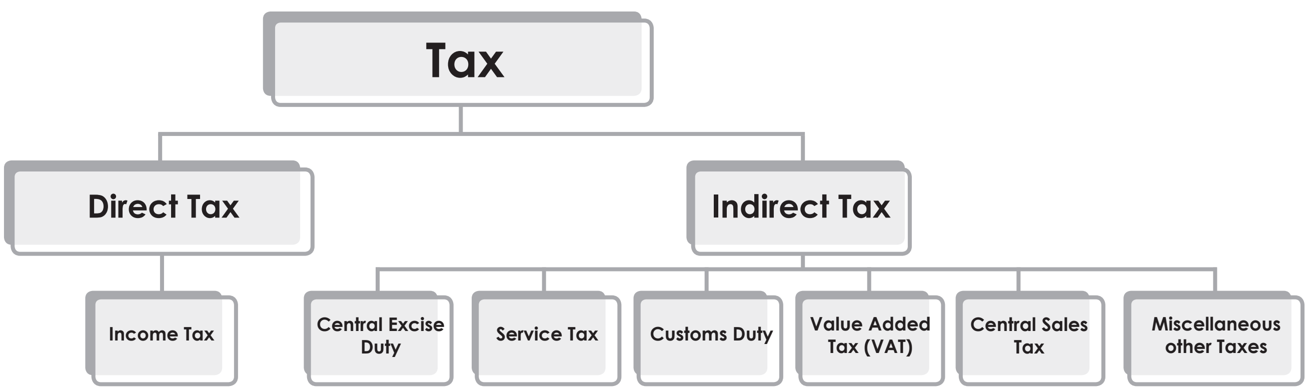
1.2 Direct Taxes and Indirect Taxes

1.3 Constitutional Validity

1.4 Administration and Relevant Procedures

1.1 BASIS FOR TAXATION

India is a socialist, democratic and republic country. Constitution of India is supreme law of land. All other laws, including the Income Tax Act, are subordinate to the Constitution of India. The Constitution provides that 'no tax shall be levied or collected except by Authority of Law'. The Constitution includes three lists in the Seventh Schedule providing authority to the Central Government and the State Governments to levy and collect taxes on subjects stated in the lists.



1.2 DIRECT TAXES AND INDIRECT TAXES

(A) Direct Taxes: They are imposed on a person's income, wealth, expenditure, etc. Direct Taxes charge is on person concern and burden is borne by person on whom it is imposed.

Example- Income Tax.

(B) Indirect Taxes: They are imposed on goods/ services. The Immediate liability to pay is of the manufacturer/ service provider/ seller but its burden is transferred to the ultimate consumers of such goods/ services. The burden is transferred not in form of taxes, but, as a part of the price of goods/ services.

Example- Excise Duty, Customs Duty, Service Tax, Value-Added Tax (VAT), Central Sales Tax (CST).

Government need funds for various purposes like maintenance of law and order, defence, social/ health services, etc. Government obtains funds from various sources, out of which one main source is taxation. Justice Holmes of US Supreme Court, has, long ago, rightly said that tax is the price which we pay for a civilized Society.

Difference between Direct Taxes & Indirect Taxes :

Particulars	Direct Taxes	Indirect Taxes
Meaning	Direct Taxes are those taxes where the incidence and impact falls on the same person.	Indirect Tax is a tax where incidence and impact fall on two different person.
Nature of tax	Direct Tax progressive in nature.	Indirect Taxes is regressive in nature.
Taxable Event	Taxable Income of the Assessees.	Purchase / Sale / Manufacture of goods and provision of services.
Levy & Collection	Levied and collected from the Assessee.	Levied & collected from the consumer but paid / deposited to the Exchequer by the Assessee / Dealer.
Shifting of Burden	Directly borne by the Assessee. Hence, cannot be shifted.	Tax burden is shifted or the subsequent / ultimate user.
Collected	After the income for a year is earned or valuation of assets is determined on the valuation date.	At the time of sale or purchases or rendering of services.
Disadvantages of Direct taxes / Advantages of Indirect Taxes	It is psychologically very difficult for a person to pay some amount after it is received in his hands. Hence, there is psychological resistance [This is the reason why even Income Tax Act is widening the scope of "Tax Deduction at Source'' (TDS) and TCS. Thus, a direct tax is converted to an indirect tax].	Since the price of commodity or service is already inclusive of indirect taxes, the customer i.e. the ultimate tax payer does not feel a direct pinch while paying indirect taxes and hence, resistance to indirect taxes is much less compared to resistance to direct taxes. ***Manufacturer's/ Dealer's Psychology favours indirect taxes***- The manufacturer/ trader who collects the taxes in his Invoice and pays it to Government, has a psychological feeling that he is only collecting the taxes and is not paying out of his own pocket (though this feeling may not be always correct).
	Direct taxes are mainly on income of individuals, firms or corporate bodies, where millions of transactions are carried out in lakhs of places and keeping an eye over all such transactions is virtually impossible.	Indirect taxes are easier to collect as indirect taxes are mainly on goods/ commodities/ services, for which record keeping, verification and control is relatively easy (at least in organized sector). Manufacturing activities are carried out mainly in organized sector, where records and controls are better.

Particulars	Direct Taxes	Indirect Taxes
	Tax evasion is comparatively more in direct taxes where it is on unorganized sector, since control is difficult.	Tax evasion is comparatively less in indirect taxes in organized sector due to convenience of control.
	Collection cost as percentage of tax collected are higher in direct taxes compared to indirect taxes.	Collection costs as percentage of tax collected are lower in indirect taxes compared to direct taxes.
	Direct taxes can control such wasteful expenditure only indirectly by taxing higher income group people.	Government can levy higher taxes on luxury goods, which reduces the wasteful expenditure.
	Government can judiciously use the direct taxes to support development in desirable areas, while discouraging in backward areas, infrastructure development etc.	Government can judiciously use the indirect taxes to support development in desirable areas, while discouraging it in others, e.g. reducing taxes on goods manufactured in tiny or small scale units; lowering taxes in backward areas etc.
Advantages of Direct taxes/ Disadvantages of Indirect taxes	Direct taxes are 'progressive', as they depend on paying capacity. Rich person is taxed more compared to poor person.	Indirect taxes do not depend on paying capacity. Since the indirect tax is uniform, the tax payable on commodity is same, whether it is purchased by a poor man or a rich person. Hence, the indirect taxes are termed as 'regressive'. (This argument is only partially correct; as it is possible to levy lower taxes on goods of daily consumption while levying higher taxes on luxury goods and the regressive effect can be reduced in many circumstances.)
	Direct taxes do not affect prices of goods and service.	Tax on goods and services increases its prices, which reduces demand of goods and services. Lesser demand means lower growth of industrialization.
	High income tax rates increase tax evasion and hawala transactions.	High customs/ excise duty increases smuggling, hawala trade and mafia gangs, which is harmful in many ways. Similarly, high excise duty leads to evasion.
	Direct taxes do not have such effect.	Higher customs duty and excise duty increases cost of modern machinery and technology.
	Direct taxes are not inflationary.	Indirect taxes increase the prices of products and hence are often perceived as inflationary.

Recovery from buyer is not essential condition for levy of indirect taxes- In general, indirect taxes are recovered from buyer, it is not an essential feature of indirect taxes. Tax on goods or services will be valid even if it is not recovered or recoverable from buyer.

1.3 CONSTITUTIONAL VALIDITY

Power of Taxation under Constitution of India is as follows :

(a) The Central Government gets tax revenue from Income Tax (except on Agricultural Income), Excise (except on alcoholic drinks) and Customs.

(b) The State Governments get tax revenue from sales tax, excise from liquor and alcoholic drinks, tax on agricultural income.

(c) The Local Self Governments e.g. municipalities, etc. get tax revenue from entry tax and house property tax.

Article 265 provides that no tax shall be levied or collected except by Authority of Law. The authority for levy of various taxes, as discussed above, has been provided for under Article 246 and the subject matters enumerated under the three lists set out in the Schedule-VII to the Constitution.

1.4 ADMINISTRATION AND RELEVANT PROCEDURES

In India, Constitution which came into effect on 26th January, 1950 is supreme and all laws and Government actions are subordinate to our Constitution. Clear understanding of concepts is vital for any discussion on taxation matters as power to levy and collect tax is derived from Constitution. If it is found that any Act, Rule, Notification or Government order is not according to the Constitution, it is illegal and void and it is called ultra vires the Constitution.

India is Union of States – The structure of Government is federal in nature. Article 1(1) of Constitution of India reads, 'India, that is Bharat, shall be a Union of States'.

Government of India (Central Government) has certain powers in respect of whole country. India is divided into various States and Union Territories and each State and Union Territory has certain powers in respect of that particular State. Thus, there are States like Gujarat, Maharashtra, Tamilnadu, Kerala, Uttar Pradesh, Punjab etc. and Union Territories like Pondicherry, Chandigarh etc.

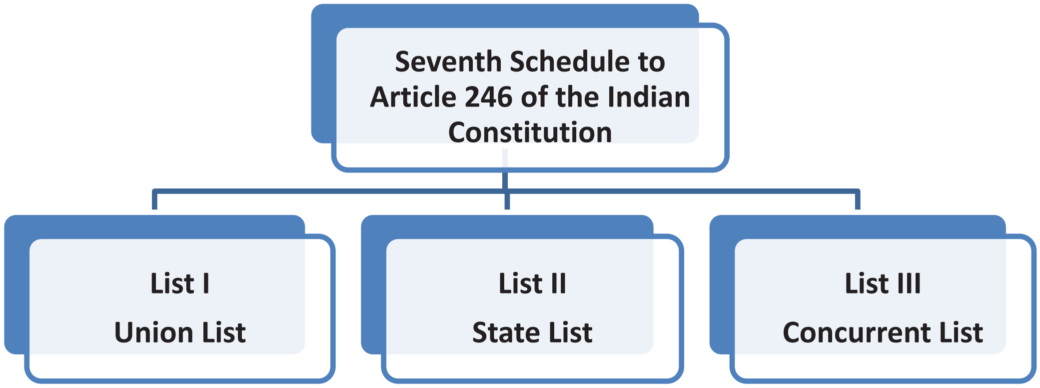
Sources and Authority of Taxes in India

Powers of Central or State Government to levy tax		
Article	**Empowers**	**For**
246(1)	Central Government	Levy taxes in List I of the Seventh Schedule of the Constitution.
246(2)	Central or State Government	Levy taxes in List III of the Seventh Schedule
246(3)	State Government	Levy taxes in List II of the Seventh Schedule of the Constitution.

Bifurcation of powers between Union and States – Article 246(1) of Constitution of India states that Parliament has exclusive powers to make laws with respect to any of matters enumerated in List I in the Seventh Schedule to Constitution (called 'Union List'). As per Article 246(3), State Government has exclusive powers to make laws for State with respect to any matter enumerated in List II of Seventh Schedule to the Constitution.

Seventh Schedule to Constitution consists of following three lists:

- List I (Union List) contains entries under exclusive jurisdiction of Union Government.
- List II (State List) contains entries under exclusive jurisdiction of States.
- List III (Concurrent List) contains entries where both Union and State Governments can exercise power. [In case of Union Territories, Union Government can make laws in respect of all the entries in all three lists].



Taxation under Constitution

Union List (List I)	State List (List II)
Only Union Government can make laws.	Only State Government can make laws.
Given in Schedule Seven of Constitution	Given in Schedule Seven of Constitution.
Important taxes in Union List	**Important taxes in State List**
Entry No. 82 – Tax on income other than agricultural income. **Entry No. 83** – Duties of customs including export duties. **Entry No. 84** – Duties of excise on tobacco and other goods manufactured or produced in India except alcoholic liquors for human consumption, opium, narcotic drugs, but including medicinal and toilet preparations containing alcoholic liquor, opium or narcotics. **Entry No. 85** – Corporation Tax. **Entry No. 86** – Taxes on the capital value of assets, exclusive of agricultural land of individuals and companies; taxes on capital of companies. **Entry No. 92A** – Taxes on the sale or purchase of goods other than newspapers, where such sale or purchase takes place in the course of interstate trade or commerce. **Entry No. 92B** – Taxes on consignment of goods where such consignment takes place during interstate trade or commerce. **Entry No. 92C** – Tax on services [Amendment passed by Parliament on 15-1-2004, but not yet made effective]. **Entry No. 97** – Any other matter not included in List II, List III and any tax not mentioned in list II or list III. (These are called 'Residual Powers'.)	**Entry No. 46** – Taxes on agricultural income. **Entry No. 51** – Excise duty on alcoholic liquors, opium and narcotics. **Entry No. 52** – Tax on entry of goods into a local area for consumption, use or sale therein (usually called Entry Tax or Octroi). **Entry No. 54** – Tax on sale or purchase of goods other than newspapers except tax on interstate sale or purchase. **Entry No. 55** – Tax on advertisements other than advertisements in newspapers. **Entry No. 56** – Tax on goods and passengers carried by road or inland waterways. **Entry No. 59** – Tax on professions, trades, callings and employment.

List III : Concurrent List
Both union and State Government can exercise power
Given in Schedule Seven of constitution
Entry No.17A – Forest Income
Entry No. 25 – Education Income

Study Note - 2

CENTRAL EXCISE ACT, 1944

This Study Note includes

2.1 CONSTITUTIONAL BACKGROUND

Central Excise is a duty on excisable goods manufactured or produced in India, other than alcoholic liquor. Duty liability is principally on 'manufacturer' of excisable goods in India, except in a few cases. In majority of cases, the general rate of excise duty has been increased from 12.36% (including education cess and secondary and higher education cess) to 12.50% (excluding education cess and secondary and higher education cess) [notification no. 01/2015-M&TP dated 01.03.2015]. The education cess which was levied on all excisable goods as a duty of excise has been fully exempted vide notification no. 14/2015 CE dated 01.03.2015 and secondary and higher education cess which was levied on all excisable goods as a duty of excise has also been fully exempted vide notification no. 15/2015 CE dated 01.03.2015.

To solve the practical problems regarding the calculation of excise duty, the general rate of 12.50% is considered here irrespective of the name and nature of the product. However, the product specific rates of excise duty are mentioned in CETA.

2.2 LAWS RELATING TO CENTRAL EXCISE

Central Excise Act,1944(CEA) : The basic act which provides the constitutional power for charging of duty, valuation, powers of officers, provisions of arrests, penalty, etc.

Central Excise Tariff Act, 1985 (CETA): This classifies the goods under 96 chapters with specific codes assigned.

Central Excise Rules, 2002: The procedural aspects are laid herein. The rules are implemented after issue of notification.

Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000: The provisions regarding the valuation of excisable goods are laid down in this rule.

Cenvat Credit Rules, 2004: The provisions relating to Cenvat Credit available and its utilization are mentioned.

Central Excise law extended to ''designated areas'' in continental shelf and exclusive Economic Zone of India i.e., upto 200 nautical miles from the base line of India and represents the limit till which India can be engaged in economic exploitation.

2.3 CENTRAL EXCISE ACT, 1944

The duty of Central Excise is levied if the following conditions are satisfied:

(1) The duty is on goods.

(2) The goods must be excisable.

(3) The goods must be manufactured or produced.

(4) Such manufacture or production must be in India.

In other words, unless all of these conditions are satisfied, Central Excise Duty cannot be levied. Ownership of raw material is not relevant for duty liability - Hindustan General Industries v. CCE 2003 (155) ELT 65 (CEGAT)

Example 1:

In the case of ***CCE v M M Khambhatwala* (1996) SC,** Mr. Khambhatwala was the owner of raw material. He supplied the raw material to the household ladies who were manufacturing the 'dhoop, agarbatti; etc. in their houses. There was no control or supervision over their work and payment to the ladies was on the basis of number of pieces manufactured. It was held that the household ladies, and not Mr. Khambhatwala, were the manufacturers.

2.4 DUTIES LEVIABLE

- **Basic Excise Duty (BED)** is levied u/s 3(1) of Central Excise Act. The section is termed as 'charging section'. In majority of cases, the standard rate of basic excise duty has been increased from 12% to 12.50% (notification no. 01/2015-M&TP dated 01.03.2015). It should be mentioned here that the BED will vary productwise according to the rate mentioned in CETA.
- **Education Cess** which was earlier 2% of excise duty has been fully exempted w.e.f. 01.03.2015.
- **Secondary and Higher Education Cess** (S&H Education Cess) which was earlier 1% of the total duties of excise has also been fully exempted w.e.f. 01.03.2015.

Example 2:

Basic Excise Duty	12.50%
Add: Education Cess	—
Add: S & H Education Cess	—
Total effective rate of duty	12.50%

National Calamity Contingent Duty – A 'National Calamity Contingent Duty' (NCCD) has been imposed vide section 136 of Finance Act, 2001 on some products. NCCD of 1% has been imposed on mobile phones w.e.f. 1-3-2008.

In addition, cesses and duties have been imposed on some specified products.

2.5 LEVY, COLLECTION & EXEMPTIONS FROM EXCISE DUTY

2.5.1 What is the Taxable Event?

The taxable event is of great significance in levy of any tax or duty. Excise duty is leviable on all excisable goods, which are produced or manufactured in India. Thus, 'manufacture or production in India' of an excisable goods is a 'taxable event' for Central Excise. It becomes immaterial that duty is collected at a later stage i.e. at the time of removal of goods. Therefore, removal from factory is not the 'taxable event'.

In UOI v Bombay Tyre International Ltd. (1983) 14 ELT 1896 (SC), the Supreme Court of India had held that while the levy of duty of excise is on manufacture or production of the goods, taxable event is with reference to manufacture.

Example 3:

Product X is produced on 1st February 2016 by X Ltd. On that date X is an excisable commodity with a tariff rate of 12.50%. Subsequently on 31st March, 2016 Product X was removed from the factory. Hence, the taxable event is on 1st February 2016 and not on 31st March 2016.

2.5.2 Who is Liable to Pay Duty?

Rule 4(1) of the Central Excise Rules, 2002 provides that every person who produces or manufactures any excisable goods, or who stores such goods in a warehouse, shall pay the duty leviable on such goods in the manner provided in Rule 8 or under any other law, and no excisable goods, on which any duty is payable, shall be removed without payment of duty from any place, where they are produced or manufactured or from a warehouse, unless otherwise provided.

Rule 4(1A) provides that notwithstanding anything contained in sub-rule (1), every person who gets the goods, falling under Chapter 61 or 62 or 63 of the First Schedule to the Tariff Act, produced or manufactured on his account on job work, shall pay the duty leviable on such goods, at such time and in such manner as is provided under these rules, asa if such goods have been manufactured by such person.

Provided that where any person had, instead of paying duty, quthorised job worker to pay the duty leviable on goods manufactured in his behalf under the provisions of sub-rule (1A) as it stood prior to the publication of this notification, he shall be allowed to obtain registration and comply with the provisions of these rules within a period of thirty days from the date of publication of this notification in the Official Gazatte.

Rule 4(2) provides that notwithstanding anything contained in sub-rule (1), where molasses are produced in a khandsari sugar factory, the person who procures such molasses, whether directly from such factory or otherwise, for use in the manufacture of any commodity, whether or not excisable, shall pay the duty leviable on such molasses, in the same manner as if such molasses have been produced by the procurer.

Rule 4(4) provides that notwithstanding anything contained in sub-rule (1), Commissioner may, in exceptional circumstances having regard to the nature of the goods and shortage of storage space at the premises of the manufacturer where the goods are made, permit a manufacturer to store his goods in any other place outside such premises, without payment of duty subject to such conditions as he may specified.

From the above discussion it can be concluded that the following persons shall be liable to pay excise duty :

(I) Every person, who produces or manufactures any excisable goods,

(II) Every person, who stores excisable goods in a warehouse,

(III) In case of molasses, the person who procures such molasses,

(IV) In case goods are produced or manufactured on job work,

  (a) the person on whose account goods are produced or manufactured by the job work, or

  (b) the job worker, where such person authorizes the job worker to pay the duty leviable on such goods.

2.5.3 Liability to Excise Duty

Section 3(1) of Central Excise Act provides that there shall be levied and collected in such manner, as may be prescribed:

(a) a duty of excise to be called the Central Value Added Tax (CENVAT), on all excisable goods which are produced or manufactured in India as, and at the rates, set forth in the First Schedule to the Central Excise Tariff Act, 1985;

(b) a special duty of excise, in addition to the duty of excise specified in clause (a) above, on excisable goods specified in the Second Schedule to the Central Excise Tariff Act, 1985, which are produced or manufactured in India, as, and at the rates, set forth in the said Second Schedule :

Provided that the duties of excise which shall be levied and collected on any excisable goods which are produced or manufactured:

> by a hundred per cent Export Oriented Undertaking and brought to any other place in India, shall be an amount equal to the aggregate of the duties of customs which would be leviable under the Customs Act, 1962 or any other law for the time being in force on like goods produced or manufactured outside India if imported into India, and where the said duties of customs are chargeable by reference to their value.

The value of such excisable goods shall, notwithstanding anything contained in any other provision of this Act, be determined in accordance with the provisions of the Customs Act, 1962 and the Customs Tariff Act, 1975.

Explanation.- where in respect of any such like goods, any duty of customs leviable for the time being in force is leviable at different rate, then, such duty shall, for the purposes of this proviso, be deemed to be leviable at the highest of these rates.

Section 3(1A) provides that the provisions of sub-section (1) shall apply in respect of all excisable goods other than salt which are produced or manufactured in India, by or on behalf of Government as they apply in respect of goods which are not produced or manufactured by Government.

Section 3(2) provides that Central Government may, by notification in the Official Gazette, fix for the purpose of levying the said duties, tariff values of any articles enumerated, either specifically or under general headings, in First Schedule and the Second Schedule to the Central Excise Tariff Act, 1985 as chargeable with duty ad valorem and may alter tariff values for the time being in force.

2.5.4 Exemption on DTA Clearance by 100% EOU [Notification no. 23/2003-C.E., Dated 31.3.2003]

DTA clearances by 100% EOU are exempt from-

(a) 50% of the basic duties leviable thereon ;

(b) Additional duty of customs u/s 3(5) of Customs Tariff Act, 1975. Exemption from additional duty is available only if the goods so removed are not exempt from payment of Sales Tax/VAT in India.

2.5.5 Collection of Excise Duty

For collection of Central Excise Duty, the following two procedures are followed by the Central Excise Department:

(i) **Physical Control Procedure:** Applicable to cigarettes only. In this case, assessment is done by Central Excise Officer and therafter goods are removed under his supervision under cover of an invoice countersigned by him.

(ii) **Self-Removal Procedure:** Applicable to all other goods produced or manufactured within the country. Under this system, the assesee himself determines the duty liability on the goods and clears the goods.

2.5.6 Exemptions from Levy of Excise Duty

Section 5A of the Central Excise Act, 1944 empowers the Central Government to grant Exemption from levy of excise duty and lays down the provisions relating thereto:

(1) Power to Notify Exemptions in Public Interest

Section 5A(1) provides that the Central Government is empowered to exempt in the public interest, any excisable goods from the levy of whole or any part of excise duty. Such exemption may be granted either absolutely or subject to such conditions, as may be specified in the Notification.

Exceptions — However, unless specifically provided in such notification, no exemption shall apply to excisable goods, which are produced or manufactured :

(i) in a Free Trade Zone or a Special Economic Zone and brought to any other place in India; or

(ii) by a hundred per cent Export Oriented Undertaking and brought to any place in India.

(2) Exemption in public interest

Section 5A(2) provides that if the Central Government is satisfied that it is necessary in the public interest so to do, it may, by special order in each case, exempt from payment of duty of excise, under circumstances of an exceptional nature to be stated in such order, any excisable goods on which duty of excise is leviable.

(3) Notification may provide for different method of levy of duty as well

Section 5A(3) provides that an exemption in respect of any excisable goods from any part of the duty of excise leviable thereon may be granted by providing for the levy of a duty on such goods at a rate expressed in a form or method different from the form or method in which the statutory duty is leviable and any exemption granted in relation to any excisable goods in the manner provided in this sub-section shall have effect subject to the condition that the duty of excise chargeable on such goods shall in no case exceed the duty statutorily payable.

Section 5A(2A) provides that the Central Government may, if it considers it necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification issued or order issued, insert an Explanation in such notification or order, as the case may be, by notification in the Official Gazette at any time within one year of issue of the notification or order, and every such Explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.

2.6 GOODS

"Goods" has not been defined in the central Excise Act, 1944.

As per Article 366(12) of the Constitution of India, ''Goods'' means all articles, materials and commodities.

Section 2(7) of Sale of Goods Act, 1930 defines 'Goods' to mean every kind of movable property other than actionable claims and money and includes stocks and shares, growing crops, grass and things attached to and forming part of the land, which are agreed to be served before sale or under the contract of sale.

These articles, materials and commodities must be movable and marketable. [Decision of the Supreme Court of India in the case of Union of India vs Delhi Cloth and General Mills Ltd (1977)].

Those movable and marketable goods must be excisable goods as per section 2(d) of the Central Excise Act, 1944. Those excisable goods must be manufactured in India as per section 2(f) of the Central Excise Act,1944 which includes any process incidental or ancillary to the completion of the manufactured product. [Decision of the Supreme Court in the case of Wallace Flour Mills Ltd Vs Commissioner of Central Excise (1989)].

Basic conditions for levy of Duty Under Section 3

It is obvious from section 3(1) that, to attract excise duty, the following conditions must be fulfilled:

- There should be movable goods;
- The goods must be excisable;
- The goods must be manufactured or produced; and
- The manufacture or production must be in India.

Goods manufactured or produced in SEZ are "excluded excisable goods". This means, that the goods manufactured or produced in SEZ are "excisable goods" but no duty is leviable, as charging section 3(1) excludes these goods. Thus, the goods manufactured in SEZ are not "exempted goods". They can be termed as "excluded excisable goods".

As per explanation to section 2(d), 'goods' includes any article, material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable'.

Basic Ingredients

From the above definitions of 'goods', the two essential elements of goods are emanated:

(i) They should be movable, and

(ii) They should be marketable.

2.6.1 Goods must be Movable

In order to be movable, an article must fulfill two conditions:

(i) It should come into existence (as a result of manufacture); and

(ii) It should be capable of being moved to market to be bought and sold.

Thus, goods must exist. Where goods have not come into existence, they cannot be moved as well. So long as the goods have not come into existence, no question of levy of excise duty would arise. It has been observed that the word 'manufacture' or 'production' are associated with movables.

In *Municipal Corporation of Greater Mumbai v. Union of India,* a petrol pump of huge storage capacity which was not embedded to earth but which could not be removed without dismantling was held to be immovable in nature.

In *Sirpur Papers Mills Ltd. V. CCE* the machinery embedded to a concrete base to ensure its wobble free operation was held to be a movable property.

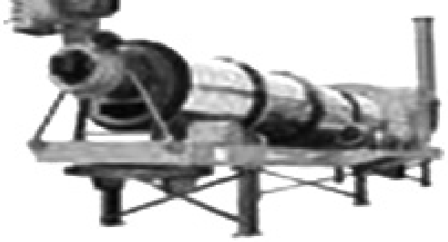
CBEC has clarified that whatever is attached to earth, unless it is like a tree/building/similar thing, shall not necessarily be regarded as immovable property if the whole purpose behind such attaching to the concrete base is to secure maximum operational efficiency and safety.

Thus, excise duty cannot be levied on immovable property.

Example 4: A Ltd. was engaged in fabrication, assembly and erection of waste treatment plant. The plant could not function as such until it was wholly built including civil construction. A Ltd. purchased duty paid parts of water treatment plant in unassembled form and assembled to the ground with civil work. Hence, excise duty is not required to pay. Because, the product emerges as immovable in nature. Larsen & Toubro Limited v UOI 2009 (243) ELT 662 (Bom).

Waste Water Treatment Plant is an immovable property

Example 5: M/s X Ltd., engaged in the manufacture of drums mix/hot mix plant by assembling and installing its parts and components. The machine is fixed by nuts and bolts to a foundation not because the intention was to permanently attach it to the earth, but because a foundation was necessary to provide a wobble free operation to the machine. Hence, the Supreme Court held that the plants in question were not immovable property. Consequently, duty would be levied on them *[CCE v Solid & Correct Engineering Works and Ors 2010 (252) ELT 48 1 (SC)]*.



Drum Mix Plant

Hot Mix Plant

2.6.2 Goods must be Marketable

Marketability denotes the capability of a product, of being put into the market for sale. Where goods are not marketable, excise duty cannot be charged on them. Marketability is the decisive test for durability. The article must be capable of being sold to consumer without any additional thing.

The test of marketability will depend on the facts and circumstances of each case. It is a question of fact. The vendibility or marketability test includes the following three essential components: -

(a) the goods should be capable of being sold in the market,

(b) the goods should be capable of being sold ordinarily, and

(c) the goods should be capable of being sold as such.

The following points can be noted –

i. Marketability is to be decided on the basis of condition in which goods are manufactured or produced.

ii. Everything that is sold is not necessarily 'marketable'.

iii. Waste and Scrap can be 'goods' but dutiable only if 'manufactured' and are mentioned in Tariff.

iv. The marketability test requires that the goods as such should be in a position to be taken to market and sold. If they have to be separated, the test is not satisfied. Thus, if machinery has to be dismantled before removal, it will not be goods - Triveni Engineering v. CCE AIR 2000 SC 2896 = 2000 AIR SCW 3144 = 40 RLT 1 = 120 ELT 273 (SC).

v. Branded Software is goods. However, service tax will be payable on tailor made software (w.e.f. Finance Act, 2008).

Shelf-life of 2 to 3 days sufficient for Marketability

The Apex Court namely the Supreme Court ruled that short shelf-life could not be equated with no shelf-life. A shelf-life of 2 to 3 days was sufficiently long enough for a product to be commercially marketed. Shelf-life of a product would not be a relevant factor to test the marketability of a product unless it was shown that the product had absolutely no shelf-life or the shelf-life of the product was such that it was not capable of being brought or sold during that shelf-life.

Hence, product with the shelf life of 2 to 3 days was marketable and hence, excisable *[Nicholas Piramal India Ltd v CCEx., Mumbai 2010* (260) ELT 338 (SC)].

Theoretical possibility of product being sold is not sufficient to establish the marketability of a product:

It means to say that a product known in the market with a nomenclature is not sufficient for marketability unless for the said product there is a buyer to buy it.

Example 6: M/s X Ltd. manufactured Double Textured Rubberized Fabric (i.e. upper lace of the shoe) and removed from the factory for job work, it has no marketability, because the said product known in the market with no buyer ***[Bata India Ltd.* v** *CCE* 2010 (252) ELT 492 (SC)].

Case Laws

(a) *In Cipla Ltd. V Union of India,* it was held by the Karnataka High Court that for dutiability, a product must pass the test of marketability, even if it is a transient item captively consumed in the manufacture of other finished goods and that the onus is on the Department to produce evidence of marketability.

(b) *In UOI v Indian Aluminium Co. Ltd. v CCE,* the Supreme Court held that marketability of a product must be for its dutiability. Mere manufacture or specification of an article in Tarrif is not enough.

(c) *In Bhor Industries Ltd. v CCE,* the Supreme Court held that the mere inclusion of a particular article in the Tariff Schedule will not render it liable to excise duty. The marketability of that article is of primary importance. The decision given in this case was a turning point because prior to this decision, it was normal to treat all goods in the Tariff Schedule, as chargeable to duty regardless of the test of marketability.

(d) *In Union Carbide India Ltd. v UOI & Geep Industrial Syndicate Ltd. v Central Government,* the Supreme Court held that intermediate products, which were in a crude form, would not constitute goods. In this case, aluminium cans produced by the extrusion process were not to be goods, as they were neither capable of being sold nor were marketable.

Example 7: concept of immovability and marketability has been explained in the following lines:

Bags are movable and marketable, Excise Duty can be levied on bags

Commercial buildings are immovable even though marketable, Excise Duty cannot be levied on commercial buildings

2.6.3 Excisable Goods

Section 2(*d*) of Central Excise Act, defines Excisable Goods means 'Goods specified in the First Schedule and the Second Schedule to Central Excise Tariff Act, 1985 as being subject to a duty of excise and includes salt. As per explanation to section 2(d), 'goods' includes any article, material or substance which is capable of being bought and sold for a consideration and such goods shall be deemed to be marketable'. Thus, unless the item is specified in the Central Excise Tariff Act as subject to duty, no duty is leviable.

In terms of the above definition of 'Excisable Goods, it may be held that all those goods, which are specified in the Tariff Schedule are 'Excisable Goods'. However, question arises as to whether those goods, which are exempted from duty by a notification, but find a place in the tariff schedule, are excisable goods. To answer this question we should know two terms namely dutiable goods and non-dutiable goods.

i. Dutiable goods mean excisable goods which has rate of duty greater than 2% per cent.

ii. Non-dutiable goods or exempted goods mean excisable goods which has rate of duty nil or 0% or 1% or 2%.

Therefore, both dutiable and non-dutiable goods are called as excisable goods.

Impact: Manufacturers paying excise duty @1% or 2% as the case may be are not eligible for claiming CENVAT Credit. Since, these goods are called as exempted goods.

By analyzing the definition, the following two important ingredients of excisable goods are found :

(a) Goods must be specified in the Schedule to the Central Excise Tariff Act, 1985;

(b) The goods so specified must be subject to duty.

(c) "Non-Excisable goods" are that goods which has not been very clearly mentioned in the Central Excise Tariff Act before they are manufactured.

2.6.4. The goods must be Manufactured or Produced in India

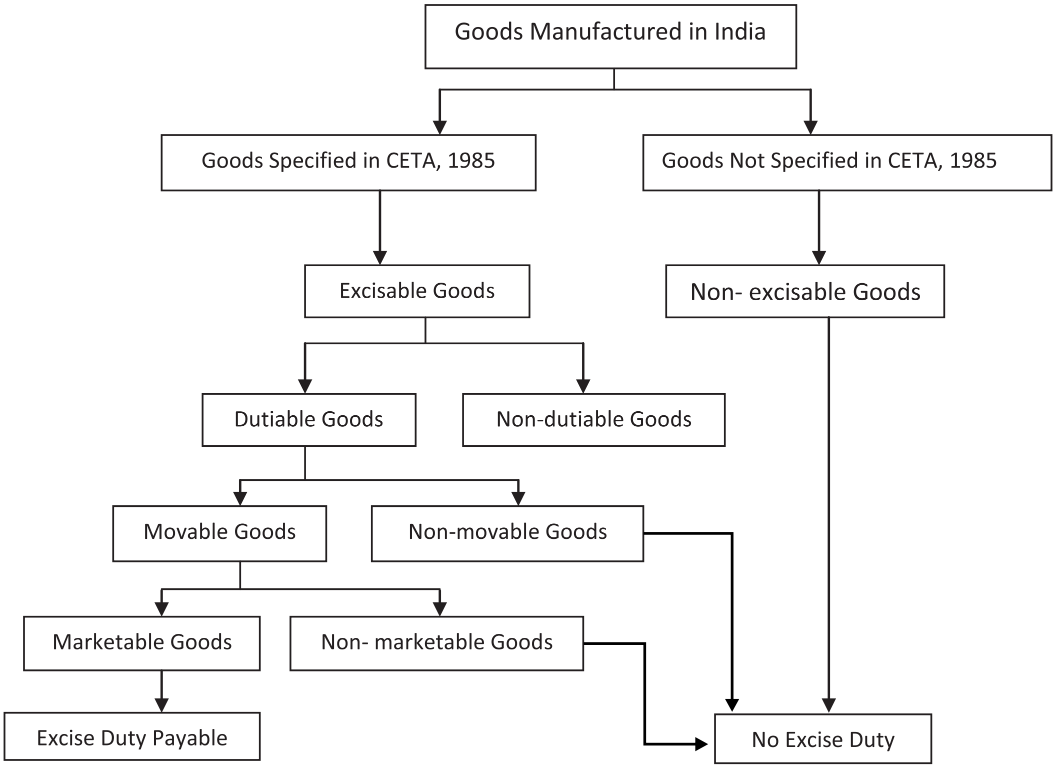
The term manufacture as understood under Excise Law refers to a process involving the conversion of an input into a completely different output. Goods manufactured in special economic zone are not exigible to excise duty as they are excluded from the scope of charging provisions of section 3 of Central Excise Act, 1944. However the goods manufactured by 100% EOU will be attracted if goods are cleared for domestic tariff area.

Excisable Goods manufactured in the state of Jammu and Kashmir attracts the excise duty since, the Central Excise Act, 1944 extended to the whole of India.

The Central Excise Act, 1944 has been extended to the designated areas in the Continental Shelf and Exclusive Economic Zone (EEZ) of India (vide Notification No. 166/87-CE, dated 11.6.1987).

Exclusive Economic Zone extends to 200 nautical miles from the base line of the coast. It means goods manufactured outside EEZ excise duty does not attract.

The entire concept of goods manufactured in India has been explained in the following diagram:



Summary

Goods = Movable + Marketable **Excisable Goods = Movable + Marketable + Listed in Tariff Schedule**

2.7 EXCISABILITY OF PLANT & MACHINERY, WASTE AND SCRAP

2.7.1 Excisability of Plant & Machinery

In view of Entry No. 84 of List-I Seventh Schedule to the Constitution of India, duty of excise could be levied only on goods and not on immovable property. The goods are classified and charged to duty according to the state and condition in which they are removed from the factory.

Assembly of Plant & Machinery at Site:

Mere bringing together of parts of a plant and machinery at site cannot be termed to be manufacture and hence, assembled plant cannot be treated to be goods.

Where assembly of parts and components brings out a different recognizable marketable product, before its installation or erection or attachment to the earth, it would be goods and hence chargeable to duty.

In *Sirpur Paper Mills Ltd. v CCE,* the Supreme Court held that machinery assembled and erected at site from bought out component was held to be goods and hence chargeable to duty, as it was attached to earth for operational efficiency and could be removed and sold.

However, in Triveni Engineering v CCE the Supreme Court overruled its decision given in Sirpur case and held that the marketability test, essentially, requires that goods should be in such condition, as could be brought as such to the market and sold, but if machinery requires dismantling before removal, it cannot be goods and hence, not chargeable to duty.

2.7.2 Excisability of Waste & Scrap

Section 3 imposes duty on manufacture of goods. Waste and scrap are not manufactured, but arise as a result of manufacture of the final product. Therefore, generally, there should not be levied any tax on the waste and scrap. Thus, waste and scrap can be 'goods' but dutiable only if 'manufactured' and are mentioned in Tariff.

In view of the amendment made by the Finance Act, 2008 in the definition of excisable goods under Section 2(d) of the Central Excise Act, 1944, which include bagasse, aluminium/zinc dross and other such products termed as waste, residue or refuse which arise during the course of manufacture and are capable of being sold for consideration would be excisable goods and chargeable to payment of excise duty [Circular No. 904/24/09-CX, dated 28.10.2009].

Case Laws

In 1987 in the case of Modi Rubber Ltd., it was held that even though the waste was capable of fetching some amount of sale, it would not be chargeable to excise duty. Similar decision was given in the case of Captainganj Distilleries.

Later in 1989, the criteria for determining, whether waste generated would be excisable or not was laid down in the case of Asiatic Oxygen Limited v CCE. The Tribunal held that the question as to whether waste would be charged to duty or not would depend on:

(a) whether a process of manufacture has taken place,

(b) whether the waste generated is marketable, and

(c) whether the product named in the Tariff.

2.8 MANUFACTURE

Any taxable event for central excise duty is manufacture or production in India. The word 'produced' is broader than 'manufacture' and covers articles produced naturally, live products, waste, scrap etc. Manufacture means to make, to inset, to fabricate, or to produce an article by hand, by machinery or by other agency. To manufacture is to produce something new, out of existing materials.

i. 'Manufacture' means :

   (a) Manufacture as specified in various Court decisions i.e. new and identifiable product having a *distinctive name, character or use must emerge or*

   (b) Deemed Manufacture.

ii. Deemed Manufacture is of two types –

   (a) CETA specifies some processes as 'amounting to manufacture'. If any of these processes are carried out, goods will be said to be manufactured, even if as per Court decisions, the process may not amount to 'manufacture', [Section 2(f)(ii)].

   (b) In respect of goods specified in Third Schedule to Central Excise Act, repacking, re-labelling, putting or altering retail sale price etc. will be 'manufacture'. The goods included in Third Schedule of Central Excise Act are same as those on which excise duty is payable u/s 4A on basis of MRP printed on the package. [Section 2(f)(iii) w.e.f. 14-5-2003].

2.8.1 Definition

Section 2(f) defines the term 'Manufacture' to include any process:

(i) incidental or ancillary to the completion of a manufactured product; and

(ii) which is specified in relation to any goods in the Section or Chapter Notes of the Schedule to the Central Excise Tariff Act, 1985, as amounting to manufacture or,

(iii) which, in relation to the goods specified in the Third Schedule, involves packing or repacking of such goods in a unit container or labeling or re-labelling of containers including the declaration or alteration of retail sale price on it or adoption of any other treatment on the goods to render the product marketable to the consumer. And the word "manufacturer" shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also any person who engages in their production or manufacture on his own account.

[Clauses (ii) and (iii) are called Deemed Manufacture]

And the word "manufacturer" shall be construed accordingly and shall include not only a person who employs hired labour in the production or manufacture of excisable goods, but also any person who engages in their production or manufacture on his own account".

Thus, according to the above definition, the manufacturer is a person:

(a) who manufactures or produces any excisable goods, or

(b) carries on any process incidental or ancillary to the completion of the manufactured products.

Case Laws

It was decided in the case of "Union of India v Delhi Cloth & General Mills Ltd" *that,* the manufacturer of vanaspati used to purchase oil from market and vanaspati was manufactured after subjecting the oil with various processes. The excise was paid on vanaspati. The Excise Department contended that during the process of manufacture of vanaspati, vegetable non-essential oil was produced, which is a separate dutiable product. The court decided that :

Manufacture implies a change, but every change is not manufacture and yet every change of an article is the result of treatment, labour and manipulations. But something more is necessary and there must be transformation; a new and different article must emerge having a distinctive name and character or use."

Based on the above definition, the Court held that mere processing of basic oils did not amount to manufacture, because it is not marketable product. The refined oil requires deodorization before marketing.

In *South Bihar Sugar Mills Ltd. v UOI* the Supreme Court held that there must be such a transformation that a new and different article must emerge having a distinctive name.

In *Ujagar Prints v UOI,* the Supreme Court held that the generally accepted test to ascertain whether there was a manufacture, is whether the change or the series of changes brought about by the application of processes should take the commodity to the point, where commercially can no longer be regarded as the original commodity, but instead is recognized as a distinct and new article that has emerged out of and because of the result of processes.

Example 8: X Ltd is engaged in the activity of conversion of gray cloth into embroidered dyed cloth. In the course of the various activities it gets the sizing done by S and dyeing by D. The cost of gray cloth is ₹50 per meter. S charges ₹ 10 per meter for sizing and D charges ₹ 30 per meter. The finished product is sold by X Ltd for ₹ 100 per meter. In the context of Central Excise Act, 1944, is there any manufacture involved? Who will be regarded as the manufacturer in this situation?

Answer:

As per the decided case law of the Supreme Court in Ujagar Paints v Union of India (1998), the end product should be one which is distinctive in name, usage and commercial character. In the given case, consequent to the value addition made to the grey cloth which is the input, the end product which emerges is commercially different with its own price structure, customs and commercial incidents. Hence, there is manufacture within the meaning of section 2(f) of the Central Excise Act, 1944.

It is not necessary that manufacturer should be the owner of the end product. Hence, in the given case, S and D will be regarded as manufacturers.

2.8.2 Assembly or Repair or Production- Whether the same is Manufacture

Assembly involves use of certain duty paid components to bring into existence an operational or functional product. As per the cardinal list laid down by the Supreme Court in Emperor Industries case, "any process would amount to manufacture if as a result of the said process the object has been transferred into a commercially known new and different product".

Thus, where assembly brings into existence of a new commercially known different product, however minor the consequent change, it would amount to manufacture.

Example 9: M/s Antony India Ltd. imported various components of TV (i.e T.V parts) in different consignments separately. They assembled these parts to bring into existence TV, it is a complicated procedure. Therefore, components cannot be considered as if they were finished goods. Hence, assembling of TV parts called as manufacture.

However, in Enfield India Ltd. case the tribunal held that an assembly, repair or reconditioning only improves the quality of performance of something which is not otherwise useful or fit to use, it would be manufacture.

Explanation as to what is not Manufacture

Any activity shall not be deemed to be manufacture, only because it has been so written in the licence granted. The following are not manufacture :

(a) Natural activity, even if carried otherwise, e.g. drying yarn in natural sun;

(b) Processing of duty paid goods;

(c) Purchasing various item and putting into a container and selling them;

(d) Obtaining of natural products;

(e) Testing/quality control of items manufactured by others;

(f) Cutting and polishing of diamond;

(g) Upgradation of computer system;

(h) Printing on glass bottles;

(i) Affixing brand name;

(j) Crushing of boulders into smaller stones.

Example 10: Cigarettes were wrapped in it with the help of roll of Aluminum Foil. It did not change the nature and substance of foil. The said process did not render any marketable value, only made it usable for packing. *CCE v. GTC Industries Ltd. 2011 (266) E.L.T. 160 (Bom.)]*.

2.8.3 Explanation about Incidental & Ancillary Process

'Incidental' means anything that occurs incidentally. It refers to occasional or casual process.

'Ancillary' means auxiliary process, which unless pursued, shall not result into manufacture of the product. The definition of 'manufacture' under section 2(f), includes the processes which are 'incidental or ancillary to the completion of a manufactured product'. A process can be regarded as incidental or ancillary to the completion of the manufactured product, if it comes in relation to the finished product. It is immaterial whether the process is significant or inessential. On the other hand, where a process is not connected to the manufacture of the final product, it cannot be termed as incidental or ancillary.

Example 11: Mr. Ram use to purchase duty paid MS tubes from its manufacturers and cut the same into requisite length. Thereafter, put it in the swaging machine for undertaking swaging process whereby dies fitted in the machine imparted "folds" to the flat surface of the MS tube/pipe. The Department took the plea that swaging process amounted to manufacture and hence duty was payable on the goods manufactured by Mr. Ram.

Answer:

As per Section 2(f) of the Central Excise Act, 1944, Manufacture includes 'any process incidental or ancillary to the completion of a manufactured product'. However, input and output must be different with each other. Therefore, the process of swaging amounts to manufacture. Mr. Ram was liable to pay the duty. *[Prachi Industries v CCEx., Chandigarh* 2008 (225) ELT 16 (SC)]

Intermediate Products & Captive Consumption

The definition of manufacture under section 2(f) implies that manufacture would take place even at an intermediate stage, so long as the intermediate product is commercially and distinctly identifiable.

Intermediate products are such products, which are produced in a process naturally in the course of manufacture of a finished product, which involves more than one process. Thus, such products are output of one process and input for the subsequent process. Captive consumption means consumption of such output of one process in the subsequent process. Generally, the intermediate products do not have any marketable identity and can hardly be sold in the market.

In the case of JK Spinning &Weaving Mills v UOI the Supreme Court held that the captive consumption would amount to removal, hence chargeable to duty. However, in Union Carbide v UOI, the Supreme Court held that an intermediate product would be chargeable to excise duty, only if it is a complete product and can be sold in the market to a consumer. This decision was affirmed in Bhor Industries v UOI.

2.9 MANUFACTURER

Manufacturer is the person who actually brings new and identifiable product into existence.

(i) Duty liability is on manufacturer in most of the cases.

(ii) Mere supplier of raw material or brand name owner is not 'manufacturer'.

(iii) Loan licensee is not 'manufacturer'.

Loan licensee can be treated as manufacturer only if the manufacture is carried out by use of his own raw material under his own supervision by hiring the premises and equipment shift-wise or otherwise.

Exception:

2.9.1 Brand owners Liable to pay Excise Duty (w.e.f. 1-3-2011)

In case of ready-made garments and made-up articles of textiles manufactured on job-work basis, liability to pay excise duty and comply with the provisions of the Central Excise Rules, 2002 is on the merchant manufacturer (i.e. person on whose behalf the goods are manufactured by job workers, namely owner of raw materials), as per rule 4(1A) of the Central Excise Rules, 2002 (vide Notification No. 4/2011 C.E. dt. 1-3-2011).

Example 12: X Pvt. Ltd is job worker located at Tambaram South, Chennai, received raw material for manufacture of articles of apparels, clothing accessories, knitted or crocheted and worn clothing from Peter England a brand owner. Hence, the liability to pay excise duty is on brand owner namely Peter England.

2.9.2 Manufacturer as per Statute

The following are held to be manufacturer:

(a) Person manufacturing for own consumption,

(b) Person hiring labour or employees for manufacturing,

(c) A job-order worker,

(d) A contractor.

2.9.3 Person not considered as Manufacturer

The following have been held as not to be a manufacturer :

(a) Where an activity is not a manufacture;

(b) Brand Owners, if their relation with the manufaturer is 'Principal to Principal' basis.

(c) Labour Contractors, who supply labor;

(d) Loan licensee.

(e) Raw material supplier is not manufacturer

Example 13: Assessee repairs his worn out machineries /parts with the help of welding electrodes, mild steel, cutting tools, M.S. Channel, M.S. Beam etc, in this process M.S. Scrap and Iron Scrap generated. Repairing activity in any possible manner cannot be called as a part of manufacturing activity in relation to production of end product. The generation of metal scrap or waste during the repair of worn out machineries/parts of cement manufacturing plant does not amount to manufacture. *GRASIM INDUSTRIES LTD v UOI 2011 (273) E.L.T 10 (S.C.)*

2.9.4 Dutiability of Packing, Labelling and Repacking Activities

Section 2(*f*), defines 'Manufacture' to include any process, which is specified in relation to any goods in the Section or Chapter notes of the Schedule to the Central Excise Tariff Act, 1985 (CETA) as amounting to manufacture. Thus, the process may not amount to manufacture as per principles evolved by Courts, but the same may be liable to excise duty, if it is defined as amounting to manufacture under CETA.

This provision seemingly includes the process like packing, labeling, re-labelling, re-packing into manufacture, though otherwise these processes are not 'manufacture' as no new product emerges. In fact, these processes are adjunct to manufacture. The manufacture shall be complete only when the product is rendered marketable and movable and for this purpose packing is an inevitable process. Therefore, packing and associated with that the labeling is a part of the manufacturing process.

In *CCE v Prabhat Packging Ltd.,* the Tribunal has held that repacking of an already manufactured product would not amount to manufacture in excise law, since repacking does not result into a new commercially distinct product.

Labelling on packaged products is also not manufacture, since in the common market parlance a labeled and unlabelled product is treated as the same product and the distinction as such is made. The principle was affirmed in the case of *Pioneer Tools and Appliances Ltd. v UOI* by the Bombay High Court.

2.10 CLASSIFICATION OF GOODS

Central Excise Duty is chargeable on the goods, which are manufactured in India and are subject to excise duty. However, all goods cannot be charged with the same rate of duty. Therefore, the goods need to be grouped into separate categories and sub-categories, for which the rate of excise duty may be determined. This identification of goods through groups and sub-groups is called classification of goods.

The rate of duty is found out by classifying the product in its appropriate heading under Central Excise Tariff. The Central Excise Tariff Act, 1985 (CETA) classifies all the goods under 96 chapters and specific code is assigned to each item. CETA is based on International Convention of Harmonised System of Nomenclature (HSN), which is developed by World Customs Organisation (WCO) (That time called as Customs Cooperation Council). This is an International Nomenclature standard adopted by most of the Countries to ensure uniformity in classification in International Trade. HSN is a multi purpose 6 digit nomenclature classifying goods in various groups. Central Excise Tariff is divided in 20 broad sections. Section Notes are given at the beginning of each Section, which govern entries in that Section. Each of the sections is divided into various Chapters and each Chapter contains goods of one class. Chapter Notes are given at the beginning of each Chapter, which govern entries in that Chapter. There are 96 chapters in Central Excise Tariff. Each chapter and sub-chapter is further divided into various headings and sub-headings depending on different types of goods belonging to same class of products.

The Central Excise Tariff Act, 1985 (CETA) came into force w.e.f. 28th February, 1986.

The main features of the Excise Tariff are:

- The Central Excise Tariff has been made very detailed and comprehensive as all the technical and legal aspects in relation to goods have been incorporated in it.
- The Excise Tariff is based on the Harmonised System of Nomenclature, which is an internationally accepted product coding system formulated under the GATT.
- The goods of the same class have been grouped together to bring about parity in treatment and restrict the dispute in classification matter.
- The Central Excise Tariff provided detailed clarificatory notes under each section/chapter.

- The interpretation of the Tariff have been provided for at the beginning of the Schedule. All the section notes, chapter notes and rules for interpretation are legal notes and/therefore serve as statutory guidelines in classification of goods.
- The Tariff is designed to group all the goods relating to one industry under one chapter from one raw material in a progressive manner.

2.10.1 Harmonised System of Nomenclature (HSN)

Goods are classified under Central Excise Tariff Act based on the "Harmonized System of Nomenclature" having eight digit classifications. All goods are classified using 4 digit system. These are called 'headings'. Further 2 digits are added for sub-classification, which are termed as 'sub-headings'. Further 2 digits are added for sub-sub-classification, which is termed as 'tariff item'. Rate of duty is indicated against each 'tariff item' and not against heading or sub-heading.

Harmonised System of Nomenclature (HSN) is an internationally accepted product coding system, formulated to facilitate trade flow and analysis of trade statistics. The system was developed by World Customs Organisation (WCO), which was earlier known as Customs Cooperative Council. HSN was adopted by International Convention of Harmonised System of Nomenclature.

The CETA is also based on the HSN pattern, of course, with some deviation. HSN has got commercial as well as judicial recognition.

Example 14:

Chapter	XXXX
Sub Chapter	XXXX
Heading	- - -- - - - (Four digits)
Sub-heading	----------- (Six digits)
Tariff Item	----------- (Eight digits)
Rate	%

2.10.2 Trade Parlance Theory/ Commercial Parlance

If a product is not defined in the Schedules and Section Notes and Chapter Notes of the Central Excise Tariff Act, 1985, then it should be classified according to its popular meaning attached to it by those dealing with it i.e., in its commercial sense.

2.10.3 Interpretative Rules of CETA

The Central Excise Tariff Act, 1985 incorporates SIX Rules of interpretation, which together provide necessary guidelines for classification of various products under the schedule. Rules for Interpretation of Schedule to Tariff are given in the Tariff itself. These are termed as 'General Interpretative Rules' (GIR). GIR (General Interpretative Rules) are to be applied for interpretation of Tariff, if classification is not possible on the basis of tariff entry and relevant chapter notes and section notes. Following are the steps of classification of a product.

(1) Rule 1 provides that the titles of sections, chapters and sub-chapters are provided for ease of reference and headings along cannot be used for classification. The determination as to where the goods fall would be dependent on the relevant section and chapter notes contained in the tariff.

Rules for interpretation are not invokable if the section and chapter notes clearly determine the classification.

Example 15: Mr. A manufactured wooden table. There is no ambiguity or confusion while classifying the said product. Hence, the said product can be classified as wooden table.

(2) If meaning of word is not clear, refer to trade practice. If trade understanding of a product cannot be established, find technical or dictionary meaning of the term used in the tariff. We may also refer to BIS or other standards, but trade parlance is most important.

Example 16: Glass mirror cannot be classified as Glass and Glassware because glass loses its basic character after it is converted into mirror. It means that mirror has the reflective function [Atul Glass Industries Ltd v CCE (SC) (1986)]

Example 17: M/s. Baidyanath Ayurved Bhawan Limited manufacturing a product called "Dant Manjan Lal" (DML). The assessee contended that the product DML was a medicament under Chapter sub-heading 3003.31 of the Central Excise Tariff Act, 1985. However, the stand of the Department was that the said product was a cosmetic/toiletry preparation/tooth powder classifiable under Chapter heading 33.06, by considering common parlance test.

As long as product has popular meaning and understanding which is attached to such products by those using the product and not to the scientific and technical meaning of the terms and expressions used. Hence, it is important to note how the consumer looks at a product and his perception in respect of such product.

Moreover, merely because there is some change in the tariff entries, the product may not change its character. Therefore, it has to be classified as a tooth powder and falls under cosmetics.

Hence, the Department stand is correct. *CCEx., Nagpur v Shree Baidyanath Ayurved Bhawan Ltd. 2009 (237) ELT 225 (SC)*

(3) Principle for classification of incomplete or unfinished goods – Rule 2(a):

Rule 2(a) specifies that if the incomplete or unfinished goods have the essential characteristics of the complete or finished goods, then such goods would be classified in the same heading as the complete goods. Complete or finished goods would cover goods removed in unassembled or disassembled form.

Example 18: Motor Car not fitted with wheels or tyres will be classified under the heading of Motor Vehicle.

(4) Mixture or Combinations of goods falls under different classifications –Rule 2(b):

Any reference in a heading to a material or substance shall be taken to include a reference to mixtures or combinations of that material or substance with other materials or substances. Any reference to goods of a given material or substance shall be taken to include a reference to goods consisting wholly or partly of such material or substance. The classification of goods consisting of more than one material or substance shall be according to the principles of rule 3.

Example 19: The Motor Car contains the stereo (music system), here two different products namely Motor Vehicle and Electronic System, hence we have to refer the Rule 3 for solution. It means to say that if Rule 2(b) is applied, or for any other reason, goods are prima facie classifiable with two or more headings then classification shall be under Rule 3.

(5) If ambiguity persists, find out which heading is specific and which heading is more general. Prefer specific heading:- Rule 3(a).

Example 20: Electrical lighting used for motor vehicles is more specifically classified as part of motor vehicle.

(6) If problem is not resolved by Rule 3(a), find which material or component is giving 'essential character' to the goods in question - Rule 3(b).

Example 21: Cell phone which consist a calculator will be called as Cell phone and not a Calculator. It means to say that the classification should be done according to its main function and additional function may be ignored.

(7) If both are equally specific, find which comes last in the numerical order in the Tariff and take it - Rule 3(c).

Example 22: If a product by virtue of its essential character comes under two headings namely 8512 and 8513 equally then the said product can be classified under the heading 8513 (i.e. Latter the better)

(8) In case where the goods cannot be classified based on the above principles, they would be classified under the head appropriate to the goods to which they are most akin – Rule 4.

Example 23: Manufacturer manufacturing the following products can be understood as most akin products:

(a) Window mirror of the car

(b) Front mirror of the car

(9) Packing material is to be classified in the heading in which the goods packed are classified – Rule 5.

Example 24: packing material used as cases for camera classifiable as camera product.

(10) Goods compared at the same level of sub-headings- Rule 6: The classification of goods in the sub-headings of a heading shall be determined according to the terms of those sub-headings and any related sub-heading Notes and, mutatis mutandis, to the above rules, on the understanding that only sub-headings at the same level are comparable. For the purposes of this rule the relative Section and Chapter Notes also apply, unless the context otherwise requires.

It means that if one heading contains 4-5 sub-headings, these sub-headings can be compared with each other. However, sub-heading under one heading should not be compared with the sub-heading of another heading.

As regards the Interpretative Rules, the classification is to be first tested in the light of Rule 1. Only when it is not possible to resolve the issue by applying this Rule, recourse is taken to rules 2,3 and 4 in seriatim.

2.10.4 Steps in Classification

The following steps are involved in classification:

(i) First reference is made to the heading and sub-heading, together with corresponding section notes and chapter notes. In case of no ambiguity, as per Rule 1, the classification would be final.

(ii) Where the product name is not clear, reference is made to the common trade practice, further reference may be made to dictionary meaning or technical terminology, if the product name is not understood in common trade practice or, it is a new product.

(iii) In case of incomplete or un-finished goods, the essential characteristics of the product must be matched with the known finished product. In case of similarity, it should be classified, as per Rule 2, under the same heading.

(iv) In case of ambiguity Rule 3(a) should be applied and specific heading should be preferred over general heading.

(v) If Rule 3(a) does not apply, goods should be classified, as per rule 3(b) as if they consist of material or components which give them their essential character.

(vi) When goods cannot be classified with reference to rules 3(a) and 3(b), they should be classified, as per Rule 3(c) under the heading, which occurs last in numerical order.

(vii) In case of residuary items classification should be made as per Rule 4 under heading, which is most akin to the goods in question.

2.10.5 Tariff Commission and other Tariff Authorities

Tariff Commission

The Tariff Commission aims to be a premier knowledge based organisation, and a centre of excellence in the field of domestic and global market research and in tax, tariff, trade related matters, and realistic cost/price determination.

Mission of Tariff Commission

To advise the Government, Public Sector Undertakings(PSUs) and other client organisations, in a relevant, fair, and unbiased manner to enable and sharpen their decision making capabilities with practical recommendations.

Objectives

To complete the designated studies in a time bound manner, using technoeconomic-costing skills, scientific and analytical/costing techniques to examine relevant primary data obtained from reliable sources.

Background of Predecessor Bodies

(i) In the pre independence period, the tariff board under the Ministry of Commerce was in existence "to advise the Government on measures required for the protection of domestic industry".

(ii) The Tariff Commission was set up in 1951 under the Tariff Commission Act 1951 by merging tariff board with statutory powers and functions to recommend protection to Indian industries, change in duties of any goods, action in relation to dumping of goods and to undertake suo moto studies.

(iii) Bureau of Industrial Costs and Prices (BICP) was set up in 1970 on the recommendation of administrative reforms commission with statutory powers under IDR Act to call for information and to advice on various issues pertaining to determination of industrial costs, on cost reduction and improvement in industrial efficiency and pricing in relation to various industries.

(iv) The old Tariff Commission was wound up under the TC(REPEAL) Act 1976 due to stringent import and foreign exchange regulation, the necessity of protection of domestic industry through tariff regulation had lost significance and the observation of the second fiscal commission that the functions of the TC were largely similar to those of BICP.

(v) Out of BICP, National Pharmaceutical Pricing Authority(NPPA) was carved out with the functions of pricing of bulk drugs and formulation and placed under the Ministry of Chemicals and Fertilizers.

Present Tariff Commission

(i) The Tariff Commission was established on 2nd September, 1997, under the Department of Industrial Policy and Promotion, as an independent expert body to tender advice to the Government on tariffs and tariff related issues concerning trade in goods and services, that have an impact on India's larger economic interests and international commitments.

(ii) The Bureau of Industrial Costs & Prices(BICP) was merged with Tariff Commission in April, 1999. The BICP role was to advise the Government on a continuous basis on issues relevant to cost reduction, improvement in industrial efficiency, energy audit and pricing of public and private sector industrial products and services.

Constitution of Tariff Commission

The Commission is headed by a Chairman in the rank of Secretary to the Government of India and assisted by a Member Secretary in the rank of Additional Secretary to the Government of India.

Tariff Commission is the only organization in the Public domain having multi-disciplinary teams of :-

- Engineers from the field of Science and Technology belonging to Tariff Commission

- Cost Accountants/Charted accountants from Indian Costs & Account Service (IC&AS)
- Economists from Indian Economic Service (IES); and
- Statisticians from Indian Statistical Service (ISS).

Status of Tariff Commission

(i) Commenced functioning in April 1999 as a focal and catalyst organization with vision and objectives outlined above.

(ii) The Commission is an independent status, and functions as an expert body.

(iii) The Commission is headed by a Chairman of the level of Secretary to Government of India, and assisted by a Member Secretary in the rank of Additional Secretary to Government of India.

(iv) Unfettered access to outside expertise.

(v) Unique independent and expert organization with multidisciplinary professionals in the fields of Finance, Costing, Economics, Science & Technology.

(v) Functions as an advisory body to the Government of India in formulating policies to promote competitiveness in indigenous industry, and enhance consumer welfare.

(vi) Advise Government on tariff related matters, impact analysis, cost/price analysis in a scientific and analytical manner, taking into account forward and backward linkages.

Functions of Tariff commission

A: On a reference from Government Tariff Commission undertakes

(i) Fixation of tariffs and all tariff related issues for goods and services.

(ii) Examination of transition period for select industries for gradual phasing out of tariffs.

(iii) Identification of tariffication process for select economic activities.

(iv) To evolve an overall tariff structure and look into tariff rationalization issues.

(v) To examine market access offers from trading partners within WTO framework (including antidumping and safe guards).

(vi) To advise on classification of goods and applicable tariffs on such goods and products.

(vii) Such other tasks as may be assigned by the Government from time to time.

B. On suo-moto basis

(i) To conduct –

Detailed impact analysis in select sectors like textiles, agriculture, automobiles, steel, information technology, chemicals and engineering goods.

(ii) To maintain & monitor –

Tariff changes of competing and trade partner countries and inventorize tariff rates.

(iii) To carry out studies –

On cost of production of different goods and services and its competitiveness in relation to other countries.

(iv) To discharge –

Core functions of the merged Bureau of Industrial Costs & Prices.

Capabilities

The use of inter-disciplinary professional expertise developed over the last three decades has made the Tariff Commission into a cohesive, comprehensive and analytical organization with demonstrable synergies, unique in its ability to

(i) Collect and analyse data from government, public and private sector;

(ii) Advise on costs, prices, efficiencies and competitiveness of industrial ventures;

(iii) Interact with transparency and confidence with the captains of industry/technology leaders to look into issues relating to industrial production;

(iv) Advise on policy issues related to specialized fields keeping in view the overall government policies;

(v) Calculate price, based on normative costing of the product using prudent accounting methods and provide a better way of determining the protection level for domestic industries so that they can survive competition from foreign manufacturers and products and intervention;

(vi) Develop technological input/output norms which are also appropriate to international cost calculations in so far as they are anchored on efficiency and realism;

(vii) Suggest improvements in industrial efficiency, cost reduction and pricing issues in relation to normative industrial cost and realistic/reasonable fair price;

(viii) Suggest systemic improvements conducive to cost rationalization and optimal efficiency of the operating units of the industry.

Study Areas

The Commission undertakes studies suo-moto or on reference from various Ministries/Departments. Area covered are :

(i) Industrial Policy Issues

(ii) Resource Efficiency Studies – Energy, Water, Materials, R & D and Environment

(iii) Tariff studies for streamlining/ rationalizing/ harmonizing the tariff structure

(iv) Studies in International Competitiveness

(v) Pricing studies of industries including utility and service sector

(vi) Developmental studies

(vii) Consumer oriented studies

(viii) Techno economic & cost studies of industries with reference to cost of inputs, possibilities of technological improvements and effective utilization of capital & other material resources, cost reduction measures.

Achievements

The Tariff Commission, and the erstwhile BICP, has always advocated a regime of industrial/economic liberalization, and made recommendations which have been accepted for implementation, including phased/full decontrol of price and distribution of cement, aluminium, steel, coal, and newsprint.

The Tariff Commission has always advocated move towards the regime of open general license with suitable tariffs on intermediates and final products, so that the industrial sector becomes internationally competitive.

Industry specific studies include :

(i) Pricing zones for sugar

(ii) Realistic cost/price of cement, salt and healthcare products

(iii) Two part power tariff structures

(iv) Taking measures for improving the energy efficiency for various industries like cement, caustic soda, fertilizer, steel, water conservation, paper, petrochemicals, etc.

(v) Determining methodology for fixation of service charges of polishing, lacquering, powder coating, electroplating etc. for handicraft service centres

(vi) Water conservation in steel, pulp and paper industry

(vii) Fixation of normative milling charges for raw rice and par boiled rice

(viii) Pricing of levy sugar

(ix) Study on the transportation tariff of gas and regasiffication charges of Liquified Natural Gas(LNG)

(x) Study on evaluation of methodology and procedures adopted by Madhya Pradesh Electricity Board(MPSEB) for accounting & computation of capital related charges

(xi) India's need for critical raw materials and identification of sources of raw materials in Asia, Africa & Latin America

(xii) Transportation tariff for KG Basin Gas supply network

(xiii) Study on Fee Structure of Medical Education in Central Government run Institutions

The Tariff Commission's recommendations on prices, rationalization of tariff structure, and cost reduction measures (e.g. efficient use of materials, appropriate scales of production, reduction in capital costs, availability of raw materials and intermediates at international prices) have played an important role in encouraging :

(i) Development of industry

(ii) Stimulating demand and directing channelisation of investments

(iii) Directing production to meet the requirements of the priority sectors at economic prices

(iv) Helping industry to achieve international competitiveness

(v) Determining the reasonable/realistic prices of individual products

This has been achieved by close interaction with units, industry associations, researchers in the field, and the concerned administrative ministries/departments of the Government of India.

Tariff Commission's Strengths

(i) Independent and expert organization carrying out the vital role of detailed analytical studies with long term national interest and facilitating real time policy making.

(ii) Recommendations have been appreciated by client Ministries/Departments.

(iii) Mature and reputed organization on industry and trade matters.

(iv) Reservoir of qualified and enlightened professionals, Engineers / Scientists, Chartered Accountants and Economists.

(v) Use of transparent procedure and objective decision-making.

(vi) Inbuilt flexibility and creativity to adapt with the fast, changing business environment.

(vii) Rich repository of Data/Information (973 study reports – upto September 2011).

(viii) Equipped with validated and tested diagnostic tools/methodologies for holistic analysis and assessment of industry and trade issues (such as Normation of Inputs/Long Run Marginal Cost(LRMC), Escalation Formulae, Domestic Resource Cost (DRC), Effective Rate of Protection (ERP) and Project Appraisal & Financial Viability.

(ix) Has inhouse expertise on fixation of tariffs, impact analysis, cost-price studies, regulatory issues, international competitiveness, resource efficiency evaluation, benchmarking and investigation of consumer grievances and unique core competence within GOI in determining normative and fair price/cost-price of goods and services.

(x) Currently assisting in a series of studies on energy pricing issues.

(xi) Several recommendations of Tariff Commission have been commended/ recognized by the Supreme Court, Prime Minister's Office, World Bank, and various Ministries and Associations.

Opportunities

(i) Ministry of Finance has observed that "TC (as an expert body) is necessary fordealing with critical issues of India, which is emerging as major trading power."

(ii) In the emerging complex global economy vis-à-vis complicated issues, the need for an independent and expert TC is becoming increasingly essential to critically analyse the issues and prescribe remedies for evolving national policies.

(iii) The Tariff Commission has the ability to advise Ministries/Departments on industry & trade related issues as an umbrella organization for referral.

(iv) Provide complementary/supplementary knowledge-based support to all Regulatory Bodies.

(v) Undertake alleged injury study and investigation in Anti-Dumping and Duty Safeguard measures.

(vi) Determine cost-price of Government regulated and consumer sensitive goods and services like fertilizers, natural gas, sugar, coal, public utilities, rice-milling, etc.

(vii) Data source for the Competition Commission in investigations of abuse of predatory pricing, limiting of production/supply, cases where claimed benefits are to be passed on to consumers, assess sunk cost/investment, which is often a barrier for entry/exit, and the reasonability of license fees.

(viii) Assist the National Manufacturing Competitive Council (NMCC) to examine competitiveness, gaps of indigenous products & sectoral benchmarking studies.

(ix) Undertake resource efficiency, assessment of energy, water, and material intensive products, and also address (ecology linkage and industrial waste management) issues of industry.

(x) Provide assistance in tariff-related problems of agriculture commodities to the Commission on Agriculture Costs & Prices (CACP).

Confidentiality of Tariff Commission Reports

The Reports of the Tariff Commission are confidential between the Commission and Client Ministries/ Departments.

Methodology of Tariff Commission Study – Procedural Aspects

Receipt of Reference

The Administrative Ministries of the Government of India normally requests Tariff Commission (TC) to take up studies on specified aspects. Besides the Administrative Ministries studies are also taken up based on requests received from State Governments, Industry Associations, etc. The Commission also initiates studies on its own (suo-moto), if there are important issues regarding a particular sector which merits such studies.

Once a reference is received or the Commission decides to take up a study on suo-moto basis, the Commission communicates the acceptance of studies to the client Ministries/Departments with a request to nominate the nodal officer and terms of reference (ToR) of the study. This is followed by nomination of a Study Coordinator(SC) (who is normally at the level Adviser/Director) and one member to assist the SC from each division provided the study requires input from S&T, Cost or Economic Division. The Study Coordinator is an inter-face between the team members and the Commission and plays a vital role in drawing up ToRs, study tours if any, data collection and analysis associated with conducting and completion of the study. The study team members are selected by Secretariat Division of the Commission with the approval of Member Secretary/Chairman depending on the work load of the officers associated with the studies taken up by the Commission. The various activities carried out by a Study Coordinator and its role is detailed below.

Role of Study Coordinator

The Study Coordinator plays a crucial role and has the following responsibilities to discharge from the time the reference is received till the Report is submitted to the client.

(i) On receipt of a reference or in the event of a suo-motu study, a file, which would contain a copy of the reference, background note, names of study team, PERT chart is opened. During the course of the study, minutes of various meetings, questionnaire, draft report and final report, if it is not a secret one, etc. will be added. This would be useful not only for referencing but also to ensure continuity in case, the divisional officer proceeds on leave/tour or alternatively where there is a change of team coordinator or member.

(ii) Preparation of ToRs and finalization of scope of the Study.

(iii) Preparation of a status note wherever required particularly when a study is held up for want of information, non approval of ToRs by concerned Department/Ministry, assistance in data entry etc.

(iv) Preparation of detailed time schedule in the form of PERT charts and mandays required for the completion of the study.

(v) Drawing up of a comprehensive questionnaire covering Economic, Technical and Costing aspects.

(vi) Consolidation of identified data gaps/clarification received from different divisions and onward transmission to Secretary, TC for calling data from the concerned units.

(vii) Preparation of an approach paper detailing the methodology to be adopted, issues requiring focus and data collection report, structure/chapter profile etc.

(viii) Planning and submission of tour programme in consultation with team members of each division through Secretary (TC) to Member Secretary/Chairman. Secretary (TC) will examine the tour programme from expenditure point of view.

(ix) Fortnightly/monthly review of the progress of the study by Study Coordinator and Member Secretary respectively. The Study Coordinator is primarily responsible for monitoring as well as initiating action as on various aspects of the study as and when required, till the study is completed and the report approved by the Commission.

(x) Consolidation of Chapters of different Divisions, ensuring that repetitions are avoided. The draft report is to be put up to Member Secretary/Chairman for comments and review.

(xi) Presentation of salient features/highlights/focal issues/important recommendation in the internal meeting fixed prior to the Commission meeting. This will include brain storming on the subject with selected officers of the Commission, industry leaders, industry representatives, officers of the nodal Ministry associated with the study and any experts who are associated with the subject.

(xii) After submission of a Commission Report, the Study Coordinator is required to identify the areas/ data which requires editing/camouflaging before sending the same to the Editorial Board for further action on actual editing, presentation, layout, etc.

Manpower Planning

The Commission at the beginning of financial year draws out a detailed Annual Action Plan (AAP) now known as Results Framework Document (RFD) indicating therein the various studies to be done during the year (on-going + new references), studies taken up suo-motu, along with their target date of completion. The Study Coordinator in consultation with the members of each Division draws out a detailed time schedule in the form of a PERT Chart of various activities proposed for the study which is synchronised with the time schedule of the Commission's RFD. The likely date of completion of the study is finalized keeping in view the need of the client Ministry, viz-a-viz existing references received by the Commission. A systematic review of the existing manpower both with regard to numbers as well as expertise would reveal the need for engaging consultants, if any, with relevant experience keeping in view the objective of the study. Young Professionals/DEOs are also employed to supplement the efforts of the Commission's officials in compilation of information from secondary and primary sources, data analysis, etc. The Division-wise mandays proposed to be assigned in a study for each activity is tabulated and consolidated in order to get the total number of mandays expected to be utilized. The number of mandays will in no case exceed 90 days from the date of receipt of information/data required for the study.

Preparation of Questionnaire

Keeping in view the objective/scope of the study the probable issues involved and ToR of the study, a questionnaire consisting of economic, technical and costing aspects, is designed by all the three divisions. At times, in case of new area of study, before the data requirement can be crystallized there exists a need for a preliminary visit to the manufacturing units to have an understanding of the manufacturing process and various forward and backward linkages. This visit helps in understanding the manufacture, process, technology involved, other related issues, which in turn facilitate the preparation of questionnaire. The requirement of data from the industry (associations/units) are put in a formal, concise, crisp and cogent questionnaire by each Division. The questions should be formulated in a manner that the respondents (manufacturers) can easily understand, compile and respond promptly. The calling of unrelated or unrequired data should be avoided in order to avoid unnecessarily burdening the parties involved in the study.

Further the questionnaire to the extent feasible be structured in a manner that information can be provided by the manufacturers in soft copy with minimum effort. The draft computer and respondent friendly questionnaire is consolidated by the Study Coordinator and is put up to the Commission for approval. Further, the Questionnaire covering of Economic, Technical and Costing aspects as Sections (A), (B) and (C) respectively be issued to the selected units by Secretary, Tariff Commission. The normal time frame for response from the units is 4 to 8 weeks, depending on the scope of the study. Full assistance be provided by the Study Coordinator to the respondents I order to understand and furnish replies to the questionnaire in the manner required.

Data Compilation

Till the response is received from the units, secondary source data be compiled. The secondary sources normally comprises of concerned Industry Association/Administrative Ministry/Consultants/Academic Institutions, particularly in the area of applied research/statistical organizations/various technical, economic and costing journals as well as Cost Audit Reports, past study reports etc. The scanning of data from secondary sources is an on-going process which helps in culling data/information and is a continues process till the report is submitted.

Primary Sources

Once the replies are received, the data gaps/clarification be identified by the team members of respective division and the same be sent to the Coordinator for consolidation. The consolidated data gap/clarification sought from the units are further sent to the units by the Study Coordinator through Secretary, TC. In some cases, data gaps/clarification can be collected during the field visits. Any additional data assessed on a scrutiny of replies to questionnaire can also be collected during the field visits. The field visit tour program is to be put up by the study coordinator 15 days prior to commencement of tour to Member Secretary. Secretariat will examine the tour programme before approval of MS keeping in view the economy in expenditure / economy instructions, availability of TA funds etc.

Discussions/meetings with officials of companies/units in order to seek clarification are to be organized with concurrence of the Member Secretary, if required.

The Commission study teams comprising of one officer(s) from each division, if necessary (if full replies are received the particular division can assess if visit is necessary) visit the units to verify the data already collected, hold discussions, understand plant and processes, seek clarification and collect additional detailed information/data wherever necessary. The field visit tour programme is to be put up by the study coordinator for the approval of the Member Secretary/Chairman through Secretary, TC. The study units are informed about the visit in order to enable them to render required assistance and wanting / additional data/information to the visiting teams by the Secretary, TC. All officers proceeding on tour are required to endorse copies of the approved tour programme to all HoDs, Secretary and PPS to Member Secretary/Chairman. A check list of points should also prepared for obtaining clarification from various functionaries at the unit/plant level by the study team before proceeding on field visit.

After completion of tour, officers are required to submit tour reports brining out the benefits of the tour to Chairman through Member Secretary. The tour report is to be kept by the Secretariat section in the concern study file after being seen by the Member Secretary/Chairman.

Detailed Analysis

After collection of primary and secondary data, the same is analysed and evaluated and study lines drawn up. At this stage an approach paper detailing the important issues to be focused, methodology to be adopted, alongwith the structure/chapter profile of the report should be prepared by the Study Coordinator which is discussed in a meeting convened by Study Coordinator with the study team and concerned Chief Adviser. Following this, detailed chapter composition should commence.

Chapter Writing and Consolidation of Report

Chapters in accordance with the approved structure of the Report are composed and drafted by the nominated study team members from each division after consultation/approval with/of their HoD. General guidelines for preparing various Chapters of the TC Reports are detailed below. These are then consolidated/integrated by the Study Coordinator which is then circulated directly to Member Secretary/Chairman for perusal/comments recording their observation.

General Guidelines while preparing the Chapters of Commission Report

(i) An index covering the following : Dates or period relating to : (a) Prices of major inputs (domestic and imported) ; (b) Production data ; (c) Import data ; (d) Export Data ; and (e) Pricing period of the study, wherever relevant should normally be prepared. Another index listing all the abbreviations used in the Report should also to be prepared.

(ii) Executive Summary at the beginning of the report should be self-contained, focused and crisp and different from conclusion and recommendation chapter which appears at the end of the report.

(iii) The Introduction should cover background, scope and ToR of the study along with the approach & methodology adopted in the study.

(iv) Chapter profile sub-themes should have sub-para numbers.

(v) Units should be uniformly used throughout the Report.

(vi) Maps/Bar Charts/Pie Diagrams etc. should be given in the Report and should be also numbered.

(vii) All tables should have corresponding Chapter numbers. The percentages should be built in the tables themselves.

(viii) Contents of tables should be explained if some inference/analysis is being drawn.

(ix) Company/unit data should not be repeated in every chapter provided by different divisions. Such data should be reflected at one place only. Thus, it is important that chapters from different divisions are presented in a cohesive and integrated manner by the Study Coordinator.

(x) The main inferences/conclusions should be given at the end of every chapter.

(xi) The Commission's recommendations/suggestions should form a part of the last chapter and the gist of the main recommendations should be given in the executive summary.

Monitoring the progress of the work - Monthly Review Meetings and Other Meetings

The progress of each study is periodically reviewed normally every week by Study Coordinator and once a month by Member Secretary/Chairman. HODs undertake a systematic review of all cases under their charge, at least once a fortnight, in order to ensure that study is progressing on schedule, study direction is being appropriately addressed and important issues related to the study are not left unattended either by oversight or by default. Member Secretary presides over the Review Meetings which are normally held once in a month and attended by all HOD's and Secretary(TC). Specific problems being experienced by the Study Coordinator or other officers are brought out in such meeting for suitable attention and action. In such review meetings, the need for rescheduling various steps for completing the study in time are also discussed for suitable action in various cases. These meetings be minuted and circulated by Secretary, TC. Follow-up action on studies is taken by Secretary, TC, by ascertaining the progress of different studies and the action taken on various decisions during the meeting. This should be done by sending 'Action Due' statement to all Study Coordinators and consolidating the 'Action Taken' received from them which is put up to Member Secretary/Chairman on a fortnightly basis. If it is felt that a study requires an in-depth discussion on its progress, issues involved, methodology, meetings will be taken by Member Secretary in smaller groups with Members and concerned officers only, in order to expedite the study data collection, analysis and report writing and adherence to the time schedule.

A record of the time spent by officers on various studies is required to be kept in order to find out the cost of each study, and also to work out the mandays required and reschedule activities, whenever required.

PERT Charts in respect of each study showing the progress of study are prepared by the Study Co-ordinator and loaded on the computer, updated and delivered before the Monthly Review meeting.

Internal Meeting

Internal meeting is the mechanism used for discussing draft reports circulated in which Study Coordinator presents the salient features/highlights/focal issues of the report. Such presentations are made before the Commission in which other concerned officers from all Divisions are also normally present. The suggestions made during this internal meeting are incorporated by the Study Coordinator/Study team members and a modified draft report is circulated by the Study Coordinator to the Commission. The draft report after incorporation of the comments of the Member Secretary is put up to Chairman for kind perusal by the Study Coordinator through Member Secretary and incorporate the comments of Chairman. The study report can also be circulated by Study Coordinator to the Chief Advisers or HoDs for their comments. The comments can be incorporated after discussion with Member Secretary. The final report is to be put up by Secretary, TC for signature of Member Secretary /Chairman with the forwarding letter for onward transmission to the client Ministries/Departments.

Commission Meeting

The formal Commission meeting, which is normally held to consider draft reports is chaired by Member Secretary. The others present during this meeting are Study Coordinator, Study team members and Secretary, TC. The views of the industry association are also heard by the Member Secretary and to be incorporated in the report, along with observations of the Commission.

The report is approved with or without modifications in the meeting of the Commission. In case of major changes, the report is redrafted and submitted again for the consideration of Commission. The approved report is sent to the EDP division for formatting etc. The EDP division will send the report to the Secretariat division with soft copies.

Publication of Reports

After taking into account various factors like the objective of the study, the sensitivity of data, etc., the Commission decides on whether a particular Report should be published or not. Once a decision is taken to publish a Report, editing of the same is required, which involves camouflaging of sensitive data, ensuring consistency across Chapters, avoiding repetition/verbosity of any kind, improving presentation and layout. This should normally be done within one month of submission of Report. Generally this work is done in-house by the Study Coordinator with the help of his study team members. If required, outside editor may also appointed for this purpose. The Report, as edited, by the Study Coordinator/editor, is given final shape by the Editorial Board, constituted for the purpose. The Editorial Board among other things takes care of formatting, spelling, presentation, layout, content of the Report in terms of sensitivity of data, avoiding overlapping, if any, across Chapters. The edited Report is thereafter put up for approval of the Commission (Chairman & Member Secretary). This is then sent to systems division of TC for in-house publishing. After the final print out by system division, proof reading by the Study Coordinator and Secretary, TC, the same is sent to the Government of India Press for printing the required number of copies. Published Report is made available at a cost to Government Departments, Industry Associations, etc. if a request for the same is received. The cost of report will be decided from time to time by the Commission.

(1) Pleasantime Products (243) E.L.T 641 (S.C.) 2009

The assessee is of the view that "Scrabble' was a puzzle or in the alternative it was an educational toy' falling under sub-heading 9503.00, whereas the Department argued that "Scrabble" was not a puzzle, it was not a toy but a game therefore it was classifiable under sub-heading 9504.90.

The difference between a "game" and a "puzzle" is brought out by three distinct features, viz., outcome, clue-chance and skill. In a puzzle, the outcome is fixed or pre-determined which is not there in "Scrabble". In a "Scrabble" there are no clues whereas in crossword puzzle, as stated above, words are written according to clues. Hence, the essential characteristic of crossword to lay down clues and having a solution is absent from "Scrabble". Thus, "Scrabble" would not fall in the category or class mentioned in sub-heading 9503.00, namely, "puzzles of all kinds". As per the dictionary meaning, "Scrabble" is a board game in which players use lettered tiles to create words in a crossword fashion. Applying the dictionary meaning, the Apex Court held that "Scrabble" was a board game. It was not a puzzle. In the circumstances, it would fall under heading 95.04 and not under sub-heading 9503.00 of the CETA.

(2) Vicco Laboratories 254 ELT A44 (SC) (2010):

As per the ingredients tests and common parlance test Vicco Vajardanti Paste, powder and vicco Turmeric cream classified as "medicaments/Ayurvedic medicine and not as 'cosmetic' as contended by the department.

The fact that the products were re-labelled for export to other countries in advertising/ attractive packing, by itself cannot result in the product being classified as cosmetic. Advertisements, packing materials etc., cannot be taken into consideration for determining the real nature and character of the product.

(3) Bhushan Steels & Strips Ltd. 257 ELT 5 (SC) 2010:

Side offcuts of HR coils made of iron and steel are classified as "angles, shapes and sections of iron or non-alloy steel" under heading 7216, and not under "slitting, end cutting, roughly shaped pieces and trimmings" under heading 7204 of the tariff as "Waste and scrap" as contended by the assessee and not as "Flat rolled products" as contended by the department.

(4) Tikitar Industries [2010] 253 ELT 513 (SC):

Assessee engaged in the Process of making blown grade bitumen from straight grade bitumen through oxidation known as blowing process. It was held that said process doesn't amount to manufacture.

Further, it was also held that Bituminous coated/ covered hessian fabric which is "Rot proof, water proof and fire resistant" is classifiable under Heading 59.09 and not under heading 68.07 even though Bitumen is used in the process of manufacture of such Hessian fabric since the expression "similar materials" in Heading 68.07 has to be read in the light of other articles specifically mentioned thereunder i.e., stone, plaster, cement, asbestos and mica.

Notes:

Heading 59.09: All other textiles products and articles of a kind suitable for industrial use (for example, textile fabrics, combined with one or more layers of rubber, leather or other material, bolting cloth, endless felts of textile fabrics, straining cloth).

Heading 68.07: All other articles of stone, plaster, cement, asbestos, mica or of similar materials not elsewhere specified or included.

(5) L.M.L. Ltd. v. CC [2010 258 ELT 321 (SC)

It was held by the Apex court that, drawings and designs contained in a CD ROMs are not classifiable as "printed matter" nor "Information and Technology Software" not either `"Bare CD ROM". It is Classifiable as "Recorded CD ROM".

(6) N.I. Systems (India) P. Ltd. [2010] 256 ELT 173(SC)

It was held that based on functional test PXI Controllers, Input/output Modules/Adaptor units and Signal Converters are classified under Chapter 90 as 'Measuring and Checking Instruments' and not classifiable as 'computers/data processing machines' under Chapter 84.

2.11 VALUATION OF GOODS

Excise duty is payable on any one of the following basis:

i. **Duty based on production capacity -** Some products (e.g. pan masala, rolled steel products) are perceived to be prone to duty evasion. In case of such products, Central Government, by notification, can issue notification specifying that duty on such notified products will be levied and collected on the basis of production capacity of the factory [section 3A(1) of Central Act inserted w.e.f. 10th May 2008]. When such notification is issued, annual capacity will be determined by Assistant Commissioner [section 3A(2)(a) of CEA]. Factors relevant to determine production capacity will be specified by rules issued by Central Government [section 3A(2)(b)(i)].

ii. Specific Duty - It is the duty payable on the basis of certain unit like weight, length, volume, thickness etc. For example, duty on Cigarette is payable on the basis of length of the Cigarette, duty on sugar is based on per Kg basis etc.

Example 25:

(a) Excise Duty payable on cigarette is based on the length of the Cigarette. If the length of cigarette is 5 mm the rate of duty is say ₹ 2 flat irrespective of the price at which it is sold.

(b) Excise duty payable on sugar is based on quintals of sugar. The excise duty is say ₹ 100 per Kg of sugar produce irrespective of the price at which it is sold.

iii. Tariff value - In some cases, tariff value is fixed by Government from time to time. This is a " Notional Value " for purpose of calculating the duty payable. Once 'tariff value' for a commodity is fixed, duty is payable as percentage of this 'tariff value' and not the Assessable Value fixed u/s 4.

Products covered under the tariff basis of valuation:

(a) Pan masala packed in retail packs of upto 10 gm per pack

(b) Readymade garments

Example 26: The price of readymade garment is ₹ 500 per unit. Suppose the government fixes a rate of 60% for computing tariff value. In this case, the tariff value is 60% of ₹ 500 i.e. ₹ 300. If the duty rate is 12.50%, the excise duty payable will be ₹ 300 x 12.50% = ₹ 37.50 per unit

iv. Duty based on basis of Maximum Retail Price printed on carton after allowing deductions - section 4A of CEA.

As per section 4A of the Central Excise Act 1944, MRP provisions will be covered only when the following two conditions are satisfied:

(a) Goods must be specified under Legal Metrology Act, 2009, w.e.f. 1-8-2011 (earlier Standards of Weights and Measures Act, 1976).

(b) Those Goods must be mentioned in the notification issued by the Government of India along with rate of abatement.

Example 27: The MRP of an Air-condition Machine is ₹ 40,000 and the abatement per cent is 40%. The Excise duty is the BED rate is 12.50% will be as under:

Maximum Retail Price	=	₹	40,000
Less: abatement (40%)	=	₹	16,000
Assessable Value	=	₹	24,000
Central Excise Duty (12.50%) = ₹ 24,000 x 12.50/100	=	₹	3,000
Total Excise Duty Payable	=	₹	3,000

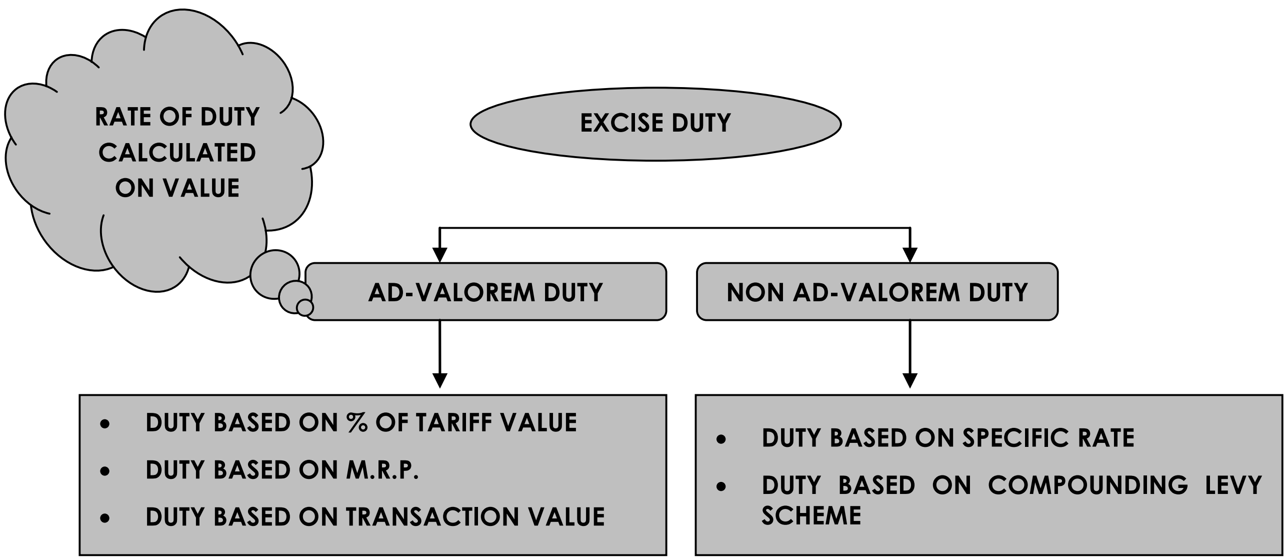
v. Compounded Levy Scheme - Normal excise procedures and controls are not practicable when there are numerous small manufacturers. Rule 15 of Central Excise Rules provides that Central Government may, by notification, specify the goods in respect of which an assessee shall have option to pay duty of excise on the basis of specified factors relevant to production of such goods and at specified rates. The scheme is presently applicable only to stainless steel pattas/pattis and aluminium circles. These articles are not eligible for SSI exemption.

Example 28: (i) The rate of compounded levy in case of cold rolled Stainless Steel patties/pattas, the manufacturer has to pay ₹ 30,000 per cold rolling machine per month plus cess as applicable.

(ii) The rate of compounded levy on aluminum circles is ₹ 12,000 per machine per month plus cess as applicable.

(iii) Duty as % based on Assessable Value (i.e. Transaction Value) fixed under section 4 (ad valorem duty) (If not covered in any of above)

It means, that payment of excise duties are depends upon value of goods (i.e. ad-valorem duty) or volume of goods (including production capacity) as the case may be. This concept explained hereunder:



2.11.1 Methods & Techniques of Valuation

Proper valuation of goods manufactured is an integral part towards levy of Excise Duty accurately. Accordingly, goods manufactured should be valued strictly in the manner as prescribed in the Central Excise Act, 1944 and rules framed there-under.

2.11.2 Value Under the Central Excise Act, 1944

Value of the excisable goods has to be necessarily determined when the rate of duty is on ad-valorem basis. Accordingly, under the Central Excise Act, 1944 the following values are relevant for assessment of duty. Transaction value is the most commonly adopted method.

(i) Transaction value under Section 4 of the Central Excise Act.

(ii) Value determined on basis of Maximum Retail Sale Price as per Section 4A of the Act, if applicable to a given commodity.

(iii) Tariff value under Section 3, if applicable.

Details of all the methods of valuation are discussed below :

1. Transaction Value

Section 4(3) (d) of the Central Excise Act, as substituted by section 94 of the Finance Act, 2000, came into force from the 1st day of July, 2000. This section contains the provision for determining the Transaction Value of the goods for purpose of assessment of duty.

For applicability of transaction value in a given case, for assessment purposes, certain essential requirements should be satisfied. If anyone of the said requirements is not satisfied, then the transaction value shall not be the assessable value and value in such case has to be arrived at under the valuation rules notified for the purpose. The essential conditions for application of a transaction value are :

(a) The excisable goods must be sold by the assessee.

(b) The transaction is between unrelated parties, i.e, the assessee and the buyer are not related parties

(c) The price is the sole consideration for the sale.

(d) The goods are sold by an assessee for delivery at the time of place of removal. The term "place of removal" has been defined basically to mean a factory or a warehouse, and will include a depot, premises of a consignment agent or any other place or premises from where the excisable goods are to be sold after their clearances from the factory.

Transaction value would include any amount which is paid or payable by the buyer to or on behalf of the assessee, on account of the factum of sale of goods. In other words, if, for example, an assessee recovers advertising charges or publicity charges from his buyers, either at the time of sale of goods or even subsequently, the assessee cannot claim that such charges are not to be included in the transaction value. The law recognizes such payment to be part of the transaction value, that is assessable value for those particular transactions.

(1) As per the Sec.4, transaction value shall include the following receipts/recoveries or charges, incurred or provided for in connection with the manufacturing, marketing, selling of the excisable goods :

   I. Advertising or publicity;

   II. Marketing and selling organization expenses;

   III. Storage;

   IV. Outward handling;

   V. Servicing, warranty;

   VI. Commission or

   VII. Any other matter.

The above list is not exhaustive and whatever elements which enrich the value of the goods before their marketing and were held by Hon'ble Supreme Court to be includible in "value" under the erstwhile section 4 would continue to form part of section 4 value even under new section 4 definition.

(2) Thus if in addition to the amount charged as price from the buyer, the assessee recovers any other amount by reason of sale or in connection with sale, then such amount shall also form part of the transaction value. Where the assessee includes all their costs incurred in relation to manufacture and marketing while fixing price payable for the goods and bills and collects an all inclusive price -as happens in most cases where sales are to independent customers on commercial consideration - the transaction price will generally be the assessable value.

    However, where the amount charged by an assessee does not reflect the true intrinsic value of goods marketed and total value split up into various elements like special packing charges, warranty charges, service charges etc. it has to be ensured that duty is paid on correct value.

2.11.3 Inclusions in Assessable Value

(i) Packing Charges: Packing charges shall form part of the assessable value as it is a charge in connection with production and sale of the goods, recovered from the buyer. Under the erstwhile Sec. 4, inclusion of cost of packing in the value was related to the nature of packing such as preliminary or secondary ete. Such issues are not relevant in the Sec. 4 and any charges recovered for packing, whether ordinary or special is includible in the transaction value if the same is not included in the price of the goods.

In the case of reusable containers (glass bottles, crates etc.), normally the cost is amortized and included in the cost of the product itself. Therefore, the same is not required to be included in the value or the product unless it is found that the cost of reusable container has not been amortised and included in the value of the product.

However, rental charges or cost of maintenance of reusable metal containers like gas cylinders etc. are to be included in the value since the amount has been charged by reason of, or in connection with the sale of goods.

Similarly, cost or containers supplied by the buyer will be included in the transaction value of the goods, as the price will not be the sole consideration of the sale and the valuation would be governed by Rule 6 of the Valuation Rules, 2000.

Durable and Returnable Packing : In case of durable/returnable containers, all that would be necessary, as per the Board's Circular No. 643/34/2002-CX dated 1-7-2002 [2002 (143) E.L.T. T39], is to include the amortised cost of the container in the price of the product itself; the returnable deposit taken from the buyer or deposit of the empty container by him would not then be treated as additional consideration.

(ii) Design and Engineering Charges being an essential process/activity for the purpose of manufacture shall be included in the Assessable value.

(iii) Consultancy Charges relating to manufacturing/production is included as such payment is 'by reason of sale".

(iv) Loading and Handling charges within the factory are included in Assessable Value.

(v) Royalty Charged in Franchise Agreement for permission to use the brand name is included in Assessable value as such payment is 'by reason of sale' or 'in connection with sale'.

(vi) Advance Authorisation Surrendered in favour of seller is additional consideration and includible. It is considered as an Additional consideration. It shall be included if it is paid by or on behalf of buyer to manufacturer-assessee and not when it is given by third party.

(vii) Price Increase, Variation, Escalation subsequent to removal of goods cleared from the factory is not relevant, provided the price is final at the time of removal.

(viii) Free After Sales Service/Warranty charges will form part of the transaction value irrespective of whether the warranty is optional or mandatory.

(ix) Advertisement and Sales Promotion Expenses Incurred by the Buyer: Manufacturer incurs advertisement expenditure. These are obviously built in the selling & distribution cost for determining the selling price. In addition, often dealers also advertise for the product at their own cost.

Definition of "Transaction Value" includes charges for "advertisement, publicity and marketing expenses". However, these are includible only if the buyer is liable to pay the amount to assessee or on behalf of the assessee.

Thus, advertisement and sales promotion expenses incurred by dealer/distributor, if done on his own, are not to be included, if transaction between buyer and seller is on principle to principle basis. This is because the buyer is not incurring these expenses "on behalf of the assessee".

(x) After Sales Service and Pre Delivery Inspection (PDI) Charges: After sales service and pre delivery inspection (PDI) are services provided free by the dealer on behalf of the assessee and the cost towards this is included in the dealer's margin (or reimbursed to him).

The value of goods which are consumed by the assessee or on his behalf in the manufacture of other articles will be on cost construction method only (Rule 8). The assessable value of captivity consumed goods will be taken at 110% (substituted by 60/2003 (NT.) 5-10-2003) of the cost of manufacture of goods even if identical or comparable goods are manufactured and sold by the same assessee as there have been disputes in adopting values of comparable goods. The concept of deemed profit for notional purposes has also been done away with and a margin of 10% by way of profit etc. is prescribed in the rule itself for ease of assessment of goods used for captive consumption. The cost of production of captively consumed goods will be done strictly in accordance with CAS- 4.

(xi) "Transaction Value" includes receipts/recoveries or charges incurred or expenses provided for in connection with the manufacturing, marketing, selling of the excisable goods to be part of the price payable for the goods sold. In other words, whatever elements which enrich the value of the goods before their marketing and were held by Hon'ble Supreme Court to be includible in "value" under the erstwhile Section 4 would continue to form part of Section 4 value even under new Section 4 definition. Where the assessee charges an amount as price for his goods, the amount so charged and paid or payable for the goods will form the assessable value. If however, in addition to the amount charged as price from the buyer, the assessee also recovers any other amount "by reason of sale" or "in connection with sale", then such amount shall also form part of the transaction value for valuation and assessment purposes. Thus if assessee splits up his pricing system and charges a price for the goods and separately charges for packaging, the packaging charges will also form part of assessable value as it is a charge in connection with production and sale of the goods recovered from the buyer.

(xii) Dharmada Charges: As per CBE&C Circular No. 763/79/2003-CX dt. 21-11-2003 has clarified that dharmada is includible in Assessable Value and the same view expressed by the Apex Court namely Supreme Court of India in the case of CCE v. Panchmukhi Engg. Works 2003 (158) E L T 550 (SC).

(xiii) Dealers Margin: Dealer's margin contained provision for rendering pre-delivery inspection and there after sale services, then amount collected by the dealers towards pre-delivery inspection or after sale services from the buyer of the goods during the warranty period it would form part of the assessable value of such goods. Therefore, pre-delivery inspection charges and after sale service recovered from the buyers of vehicles would be included in the assessable value of vehicles. The same view confirmed by the Tribunal in the case of Maruti Suzuki India Ltd. v. CCE (2010).

2.11.4 Exclusions from Transaction Value

(i) Taxes and Duties: The definition of transaction value mentions that whatever amount is actually paid or actually payable to the Government or the relevant statutory authority by way of excise, sales tax and other taxes, such amount shall be excluded from the transaction value. If any excise duty or other tax is paid at a concessional rate for a particular transaction, the amount of excise duty or tax actually paid at the concessional rate shall only be allowed to be deducted from price.

(ii) Erection, Installation and Commissioning Charges: If the final product is not excisable, the question of including these charges in the assessable value of the product does not arise. As for example, since a thermal power, as a whole, is an immovable property and therefore not excisable, no duty would be payable on the cost of erection, instigations and commissioning of the steel plant. Similarly, if a machine is cleared from a factory on payment of appropriate duty and later on taken to the premises of the buyer for installation/erection and commissioning into an immovable property, no further duty would be payable. On the other hand if parts/ components of a generator are brought to a site and the generator erected/installed and commissioned at the site then, the generator being an excisable commodity, the cost of erection, installation and commissioning charges would be included in its assessable value. In other words if the expenditure on erection, installation and commissioning has been incurred to bring into existence any excisable goods, these charges would be included in the Assessable Value of the goods. If these costs are incurred to bring into existence some immovable property, they will not be included in the assessable value of such resultant property.

However, 'time of removal' in case of excisable goods removed from the place of removal is deemed to be the time of clearance of such goods from the 'factory'. Therefore, the assessable value is with reference to delivery at the 'time and place of removal, transaction value will be the assessable value.

(iii) Freight : It follows from the Valuation Rules that in such categories of cases also if the price charged is with reference to delivery at a place other than the depot, etc. then the actual or average cost of transportation (average freight being calculated according to Generally Accepted Principles of Costing - CAS - 5) beyond the depot/place of sale will not be taken to be a part of the transaction value and exclusion of such cost allowed on similar lines as discussed earlier, when sales are effected from factory gate/warehouse. There is no question of including the freight etc. right upto the buyer's premises even though delivery may be effected at that place. Delivery to the carrier at factory gate/depot is delivery to the buyer and element of freight and transit insurance are not includible in assessable value. Moreover, the ownership of the goods has no relevance so far as their transit insurance is concerned. - Escorts JCB Ltd. v. CCE., Delhi-II - 2002 (146) E.L.T. 31 (S.C) and Prabhat Zarda Factory Ltd. v. CCE. -2002 (146) E.L.T. 497 (S.C). Freight (actual or average) upto the point of depot etc. will, however, continue to be included.

(iv) Advertising/Publicity Expenditure by Brand Name/Copyright Owner: The expenditure incurred by brand name/copyright owner on advertisement and publicity charges, in respect of goods will not be added to assessable value, as such expenditure is not incurred on behalf of the manufacturer-assessee.

(v) Notional Interest on Security Deposit/Advances: The notional interest on advances may not be includible if relation between advance and selling price is only casual. There is 'relation' but 'no connection in relation to manufacture'.

(vi) Interest on Receivables: As regards interest for delayed payments it is the normal practice in industry to allow the buyers some credit period for which no interest is charged. That is to say, the assessee allows the buyers some time (normally 30 days, which could be less or even more depending upon industry) to make the payment for the goods supplied. Interest is charged by him from the buyer only if the payments are made beyond this period. A question has been raised whether such interest on receivables (for delayed payments) should form part of the transaction value or not. As per the earlier practice under Section 4 such amount of interest is not included in "value". Also, similar is the practice followed in this regard on the Customs side, where duties are collected on transaction value basis, and the importers are given certain "free" period for payment or to pay up interest for delayed payments. As the intention is not to disturb the existing trade practice in this regard, charges for interest under a financing arrangement entered between the assessee and the buyer relating to the purchase of excisable goods shall not be regarded as part of the assessable value provided that :

(a) the interest charges are clearly distinguished from the price actually paid or payable for the goods;

(b) the financing arrangement is made in writing; and

(c) where required, assessee demonstrates that such goods are actually sold at the price declared as the price actually paid or payable.

(vii) Discounts : As regards discounts, the definition of transaction value does not make any direct reference. In fact, it is not needed by virtue of the fact that the duty is chargeable on the net price paid or payable. Thus if in any transaction a discount is allowed on declared price of any goods and actually passed on to the buyer of goods as per common practice, the question of including the amount of discount in the transaction value does not arise. Discount of any type or description given on any normal price payable for any transaction will, therefore, not form part of the transaction value for the goods, e.g. quantity discount for goods purchased or cash discount for the prompt payment etc. will therefore not form part of the transaction value.

(i) cash discount for prompt payment and

(ii) interest or cost of finance for delayed payment, when not exorbitant, is to be granted abatement whether availed or not even under Section 4 - 2006 (204) E.L.T. 570 (Tri - L.B.) - CCE v. Arvind Mills Ltd.

The differential discounts extended as per commercial considerations on different transactions to unrelated buyers if extended can't be objected to and different actual prices paid or payable for various transactions are to be accepted for working assessable value. Where the assessee claims that the discount of any description for a transaction is not readily known but would be known only subsequently - as for example, year end discount - the assessment for such transactions may be made on a provisional basis. However, the assessee has to disclose the intention of allowing such discount to the department and make a request for provisional assessment. Trade discount not paid to dealers at the time of invoice preparation but paid later on net sale value was held as deductable for valuation purpose by Hon'ble Supreme Court in the case of *Commissioner v. DCM Textiles* - 2006 (195) E.L.T. 129 (S.C). Liquidated damages (as for example price reduction for delay in delivery of goods) is acceptable - 2006 (204) E.L.T. 626 (Tri.) - *United Telecom Ltd. v. CCE.*

(viii) Deemed Export Incentives Earned on Goods Supplied: Duty drawback cannot be added to assessable value, especially if there is no evidence of drawback with depression of prices.

(ix) Subsidy/Rebate Obtained by Assessee: A general subsidy/rebate is not to be included as it has no connection with individual clearances of goods. In case of rebate/subsidy which is directly relatable to individual clerances, it should not be includible.

(x) Price of Accessories and Optional Bought-out items is not includible in Assessable Value.

2.11.5 Valuation Rules to Determine Assessable Value

As per Section 4(1)(b) of the Central Excise Act, if 'Assessable Value' cannot be determined u/s 4(1)(a), it shall be determined in such manner as may be prescribed by rules. Under these powers, Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 have been made effective from 1-7-2000.

In Ispat Industries Ltd. v CCE 2006, it was observed that Excise Valuation Rules should be applied serially. The rules are as below :

(i) Value nearest to time of removal if goods not sold: If goods are not sold at the time of removal, then value will be based on the value of such goods sold by assessee at any other time nearest to the time of removal, subject to reasonable adjustments. **[Rule 4]**

The rule applies when price at the time of removal is not available as the goods are not sold by the assessee at the time of removal. Thus, this rule should apply in case of removal of free samples or supply under warranty claims.

In case of new or improved products or new variety of products, price of similar goods may not be available. In such case, valuation should be on basis of cost of production plus 10%, in absence of any other mode available for valuation.

(ii) Goods sold at different place: Sometimes, goods may be sold at place other than the place of removal e.g. Buyer's place. In such cases, actual cost of transportation from place of removal upto place of delivery of the excisable goods will be allowable as deduction. Cost of transportation can be either on actual basis or on equalized basis. **[Rule 5]**

Explanation:

(1) "Cost of transportation" includes – (i) the actual cost of transportation; and (ii) in case where freight is averaged, the cost of transportation calculated in accordance with Generally Accepted Cost Accounting Principle.

(2) For removal of doubts, it is clarified that the cost of transportation from the factory to the place of removal, where the factory is not the place of removal, shall not be excluded for the purpose of determining the value of the excisable goods.

(iii) Valuation when the price is not the sole consideration : Where the price is not the sole consideration for sale, the value of such goods shall be deemed to be the aggregate of —

(a) such transaction value, and

(b) the amount of money value of any additional consideration flowing directly or indirectly from the buyer to the assessee. **[Rule 6]**

In case any of the goods and services *(listed below)* is provided by the buyer free of change or at reduced cost in connection with production and sale of such goods, then, the value of such goods and services, apportioned as appropriate, shall be deemed to be the money value of the additional consideration.

Only the value of the following goods and services are to be added in the transaction value:

(a) materials, components, parts and similar items relatable to such goods;

(b) tools, dies, moulds, drawings, blue prints, technical maps and charts and similar items used in the production of such goods;

(c) material consumed, including packaging materials, in the production of such goods;

(d) engineering, development, artwork, design work and plans and sketches undertaken elsewhere than in the factory of production and necessary for the production of such goods.

Provided that where price is not the sole consideration for sale of such excisable goods and they are sold by the assessee at a price less than manufacturing cost and profit, and no additional consideration is flowing directly or indirectly from the buyer to such assessee, the value of such goods shall be deemed to be the transaction value.

(iv) Sale at Depot/Consignment Agent: Section 4(3)(c)(iii) provides that in case of sale at depot/consignment agent, the depot/place of consignment agent will be the 'place of removal'. As per section 4(3) (cc), in case of sale from depot/place of consignment agent, 'time of removal' shall be deemed to be the time at which the goods are cleared from factory.

In other words, in case of sale from depot/place of consignment agent, duty will be payable on the price prevailing at the depot as on date of removal from factory. Price at which such goods are subsequently sold from the depot is not relevant for purpose of excise valuation.

When goods are sold through depot, there is no 'sale' at the time of removal from factory. In such cases, price prevailing at depot (but at the time of removal from factory) shall be the basis of Assessable Value. The value should be 'normal transaction value' of such goods sold from the depot at the time of removal or at the nearest time of removal from factory. **[Rule 7 of Valuation Rules]**

As per Valuation Rule 2(b), "normal transaction value" means the transaction value at which the greatest aggregate quantity of goods are sold.

For example, if an assessee transfers a consignment of paper to his depot from Delhi to Agra on 5-7-2015, and that variety and quality of paper is normally being sold at the Agra depot on 5-7-2015 at transaction value of ₹ 15,000 per tonne to unrelated buyers, where price is the sole consideration for sale, the consignment cleared from the factory at Delhi on 5-7-2015 shall be assessed to duty on the basis of ₹ 15,000 per tonne as the assessable value. If assuming that on 5-7-2015 there were no sales of that variety from Agra depot but the sales were effected on 1-7-2015, then the normal transaction value on 1-7-2015 from the Agra depot to unrealated buyers, where price is the sole consideration shall be the basis of assessment.

(v) Captive Consumption (Rule 8): Where whole or part of the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value of such goods that are consumed shall be one hundred and ten per cent of the cost of production or manufacture of such goods.

Duty payable on intermediated products: In A S Processors v. CCE 1999(112) ELT 706 (CEGAT), it was held that once a new marketable intermediate product comes into existence, it is to be charged to duty if not exempted by a notification – same view in CCE v. Citric India 2001(127) ELT 539 (CEGAT).

Captive consumption for dutiable final products: The intermediate product manufactured within the factory is exempt from duty, if it is consumed captively for manufacture of (a) Capital goods as defined in Cenvat Credit Rules i.e. those which are eligible for Cenvat credit or (b) Used for is or in relation to manufacture of final products eligible for Cenvat, made from inputs which are eligible for Cenvat. [Notification No. 67/1995 dated 16-3-1995].

Duty payable on captive consumption if intermediate product under Compounded Levy scheme: In Gaya Aluminium Industries v. CCE (2004) 170 ELT 98 (CESTAT), it was held that even if Aluminium Circles are captively consumed, duty will be payable under compounded levy scheme [However, assessee claimed that compounded levy scheme is optional and assessee can opt to pay normal duty. Hence, the matter was remanded to adjudicating authority for consideration].

In Gouri Shankar Industries v. CCE 2004 (1 73) ELT 247 (CESTAT) also, it was held that duty is payable if Aluminium circles are consumed captively.

Valuation in case of captive consumption: In case of captive consumption, valuation shall be done on basis of cost of production plus 10% [The percentage was 15% upto 5-8-2003]. (Rule 8 of Valuation Rules). Cost of production is required to be calculated as per CAS – 4.

Captive consumption means goods are not sold but consumed within the same factory or another factory of same manufacturer (i.e. inter-unit transfers).

The rule may also be helpful if goods are to be transferred to job worker for job work and then brought back for further processing. If job worker is utilizing some of his own material, it may be advisable to clear processed inputs on payment of duty to job worker. The job worker can avail Cenvat credit and then send back the goods manufactured by him on payment of duty.

Rule 8. Where the excisable goods are not sold by the assessee but are used for consumption by him or on his behalf in the production or manufacture of other articles, the value shall be one hundred and ten per cent of the cost of production or manufacture of such goods.

Captive consumption by related person: In case goods are supplied to a 'related person' but consumed by the related person and not sold, valuation will be done on the basis of cost of production plus 10% [Proviso to rule 9]. – CBE&C, vide its circular No. 643/34/2002-CX dated 1-7-2002, has clarified that this proviso applies when goods are transferred to a sister unit or another unit of the same factory for captive consumption in their factory.

Cost Sheet

Suggested Cost Sheet as per CAS-4 (issued by ICAI) is as follows -

Statement of cost of production of ....

manufactured/ to be manufactured during the period ....

Q1 Quantity Produced (Unit of Measure)

Q2 Quantity Dispatched (Unit of Measure)

Sr. No.	Particulars	Total Cost (₹)	Cost/ Unit (₹)
1.	Material Consumed		
2.	Direct Wages and Salaries		
3.	Direct Expenses		
4.	Works Overheads		
5.	Quality Control Cost		
6.	Research and Development Cost		
7.	Administrative Overheads (Relating to production capacity)		
8.	Total (1 to 7)		
9.	Add - Opening stock of Work-in-Progress		
10.	Less - Closing stock of Work-in-Progress		
11.	Total (8+9-10)		
12.	Less: Credit for Recoveries/Scrap/By-Products/Misc Income		
13.	Packing Cost		
14.	Cost of Production (11-12+13)		
15.	Add: Inputs received free of cost		
16.	Add: Amortised cost of moulds, tools, dies and patterns etc. received free of cost		
17.	Cost of Production for goods produced for captive consumption (1 4+15+16)		
18.	Add: Opening stock of finished goods		
19.	Less: Closing Stock of finished goods		
20.	Cost of production of goods dispatched (17+18-19)		

[Note - The form is common both for future cost and historical cost. In case of future cost (say for future quarter or half year), some of the columns e.g. opening and closing stock of WIP and FG are not relevant].

Example 29: Raj & Co. furnish the following expenditure incurred by them and want you to find the assessable value for the purpose of paying excise duty on captive consumption. Determine the cost of production in terms of rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 and as per CAS-4 (Cost Accounting Standard) (i) Direct material cost per unit inclusive of excise duty at 12.50% - ₹ 1,320, (ii) Direct wages - ₹ 250, (iii) Other direct expenses - ₹ 100, (iv) Indirect materials - ₹ 75, (v) Factory Overheads - ₹ 200, (vi) Administrative overhead (25% relating to production capacity) ₹ 100 (vii) Selling and distribution expenses - ₹ 150, (viii) Quality Control - ₹ 25, (ix) Sale of scrap realized - ₹ 20, (x) Actual profit margin - 15%.

Answer:

	Particulars	Amount (₹)
(i)	Direct Material (exclusive of Excise Duty) [1,320 x 100/112.50]	1173.33
(ii)	Direct Labour	250.00
(iii)	Direct Expenses	100.00
(iv)	Works Overhead [indirect material (75) plus Factory OHs (200)]	275.00
(v)	Quality Control Cost	25.00
(vi)	Research & Development Cost	Nil
(vii)	Administration Overheads (to the extent relates to production activity)	25.00
	Less: Realizable Value of scrap	(20.00)
	Cost of Production	1,828.33
	Add 10% as per Rule 8	182.83
	Assessable Value	2,011.16

Example 30: Determine the cost of production on manufacture of the under-mentioned product for purpose of captive consumption in terms of Rule 8 of the Central Excise Valuation (DPE) Rules, 2000 - Direct material - ₹ 11,600, Direct Wages & Salaries - ₹ 8,400, Works Overheads - ₹ 6,200, Quality Control Costs - ₹ 3,500, Research and Development Costs - ₹ 2,400, Administrative Overheads - ₹ 4,100, Selling and Distribution Costs ₹ 1,600, Realisable Value of Scrap - ₹ 1,200. Administrative overheads are in relation to production activities. Material cost includes Excise duty ₹ 1,054.

Answer: Cost of production is required to be computed as per CAS-4. Material cost is required to be exclusive of Cenvat credit available.

	Particulars	Total Cost (₹)
1	Material Consumed (Net of Excise duty) (11,600 – 1,289)	10,311
2	Direct Wages and Salaries	8,400
3	Direct Expenses	-
4	Works Overheads	6,200
5	Quality Control Cost	3,500
6	Research and Development Cost	2,400
7	Administrative Overheads	4,100
	Less: Sale of Scrap	(1,200)
	Cost of Production	33,711
	Add: 10% Profit margin on cost of production (i.e. 33,711 x 10%)	3,371
	Assessable Value as per Rule 8 of the Valuation Rules	37,082

Note - (1) Indirect labour and indirect expenses have been included in Works Overhead

(2) Actual profit margin earned is not relevant for excise valuation.

Example 31: Hero Electronics Ltd. is engaged in the manufacture of colour television sets having its factories at Kolkata and Gujarat. At Kolkata the company manufactures picture tubes which are stock transferred to Gujarat factory where it is consumed to produce television sets. Determine the Excise duty liability of captively consumed picture tubes from the following information: - Direct material cost (per unit) ₹ 800; Direct Labour ₹ 100; Indirect Labour ₹ 50; Direct Expenses ₹ 100; Indirect Expenses ₹ 50; Administrative Overheads ₹ 50; Selling and Distribution Overheads ₹ 100.

Additional Information: - (1) Profit Margin as per the Annual Report of the company for 2014-15 was 12% before Income Tax. (2) Material Cost includes Excise Duty paid ₹ 73 (3) Excise Duty Rate applicable is 12%, plus education cess of 2% and SHEC @ 1%.

Answer: Cost of production is required to be computed as per CAS-4. Material cost is required to be exclusive of Cenvat credit available.

Sr. No.	Particulars	Total Cost (₹)
1	Material Consumed (Net of Excise duty) (800 – 89)	711
2	Direct Labour	100
3	Direct Expenses	100
4	Works Overheads	100
5	Quality Control Cost	-
6	Research and Development Cost	-
7	Administrative Overheads	50
8	Total (1 to 7)	1,061
9	Less - Credit for Recoveries/Scrap/By-Products/Misc Income	-
10	Cost of Production (8-9)	1,061
11	Add - 10% as per rule 8	106
12	Assessable Value	1,167
13	Excise duty @ 12% of ₹ 1,185	145.88

∴ Total Duty Liability = ₹ 145.88

Note - (1) Indirect labour and indirect expenses have been included in Works Overhead (2) In absence of any information, it is presumed that administrative overheads pertain to production activity. (3) Actual profit margin earned is not relevant for excise valuation.

(vi) Sale to a Related Person: 'Transaction Value' can be accepted as 'Assessable Value' only when buyer is not related to seller. *In other words, price to an independent buyer has to be considered for excise valuation.*

As per section 4(3) (b) of Central Excise Act, persons shall be deemed to be 'related' if

(a) They are inter-connected undertakings

(b) They are relatives

(c) Amongst them, buyer is a relative and a distributor of assessee, or a sub-distributor of such distributor or

(d) They are so associated that they interest, directly or indirectly, in the business of each other.

Interconnected Undertakings: Buyer and seller are 'related' if they are inter-connected undertakings, as defined in section 2(g) of Monopolies and Restrictive Trade Practices Act, 1969 (MRTP). – *Explanation* (i) to section 4(3) (b) of Central Excise Act.

The essence of the definition under MRTP is that the inter-connection could be through ownership, control or management. Just 25% of total controlling power in both undertakings is enough to establish inter-connection.

Since only 25% control is enough to make to buyer and assessee as inter connected undertakings, many assessees would come under the definition. This would have affected many assessees.

However, the provisions in respect of 'inter connected undertaking' have been made almost ineffective in valuation rules. Now, the 'inter connected undertakings' will be treated as 'related person' only if they are holding and subsidiary or they are 'related person' under any other clause. In other cases, they will not be treated as 'related person'. If they are not treated as related person, price charged by assessee to buyer will be accepted as 'transaction value' – confirmed in South Asia Tyres v. CCE (2003) 152 ELT 434 (CEGAT)

Interest in business of 'each other': As per section 4(3)(b)(iv), buyer and seller are 'related' if they are associated that they have interest, directly or indirectly, in the business of each other. It is not enough if only buyer has interest in seller or seller has interest in buyer. Both must have interest, directly or indirectly, in each other - Atic Industries Ltd. v. UOI (1984) 3 SCR 930 = 1984 (17) ELT 323 (SC) = AIR 1984 SC 1495 = (1984) 3 SCC 575.

The term 'relative and distributor' should be 'read down' and understood to means as '*distributor who is a Relative'* of assessee.

The word 'relative' is defined in section 2(77) of Companies Act, 2013 as follows : - A person shall be deemed to be a relative of another if, and only if, - (a) they are members of a Hindu undivided family; or (b) they are husband and wife; or (c) the one is related to the other in the manner indicated in Schedule I-A of the Companies Act. This Schedule contains following relatives : (1) Father (2) Mother (including step-mother) (3) Son (including step-son) (4) Son's wife (5) Daughter (including step-daughter) (6) Father's father (7) Father's mother (8) Mother's mother (9) Mother's father (10) Son's son (11) Son's son's wife (12) Son's daughter (13) Son's daughter's husband (14) Daughter's husband (15) Daughter's son (16) Daughter's son's wife (17) Daughter's daughter (18) Daughter's daughter's husband (19) Brother (including step-brother) (20) Brother's wife (21) Sister (including step-sister) (22) Sister's husband.

It is obvious that only a living i.e. natural person can be 'relative' of other. Thus, a company, partnership firm, body corporate, HUF, trust cannot be 'relative' of other.

Valuation when sale is through related person [Rule 9]: Where whole or part of the excisable goods are sold by the assessee to or through a person who is related in the manner specified in any of the sub-clauses(ii), (iii) or (iv) of clause (b) of sub-section (3) of section 4 of the Act, the value of such goods shall be the normal transaction value at which these are sold by the related person at the time of removal, to buyers (not being related person)or where such goods are not sold to such buyers (being related person), who sells such goods in retail.

Provided that in a case where the related person does not sell the goods but uses or consumes such goods in the production or manufacture of articles, the value shall be determined in the manner specified in rule 8.

Valuation when sale is through inter-connected undertaking [Rule 10]: Where whole or part of the excisable goods are sold by the assessee to or through an inter-connected undertaking, the value of such goods shall be determined in the following manner, namely:-

(a) If the undertaking are so connected that they are also related in terms of sub-clause (ii) or (iii) or (iv) of clause (b) of sub-section (3) of section 4 of the Act or the buyer is a holding company or subsidiary company of the assessee, then the value shall be determined in the manner prescribed in rule 9.

(b) In any other case, the value shall be determined as if they are not related persons for the purpose of sub-section (1) of section 4.

(vii) Best Judgement Assessment: If assessment is not possible under any of the foregoing rules, assessment will be done by 'best judgement'. If the value of any excisable goods cannot be determined under the foregoing rules, the value shall be determined using reasonable means consistent with the principles and general provisions of these rules and sub-section (1) of section 4 of the Act. **[Rule 11]**

As the Valuation Rules stand today, there is no provision for calculating 'Value' in following cases- (a) If assessee makes sale partly to related person and partly to others. (b) Free samples. In these cases, valuation may be done under rule 11.

2.12 VALUATION IN CASE OF JOB WORK–RULE 10A

2.12.1 Meaning of Job Worker – As per *Explanation* to rule 10A, for the purposes of rule 10A, 'job worker' means a person engaged in manufacture or production of goods on behalf of a principal manufacturer, from any inputs or capital goods supplied by the said principal manufacturer or by any other person authorised by him.

Example 32: A Trader supplies raw material of ₹1,150 to processor. Processor processes the raw material and supplies finished product to the trader. The processor charges ₹450, which include ₹350 as processing expenses and ₹100 as his (processor's) profit. Transport cost for sending the raw material to the factory of processor is ₹50. Transport charges for returning the finished product to the trader from the premises of the processor is ₹60. The finished product is sold by the trader at ₹ 2,100 from his premises. He charges Vat separately in his invoice at applicable rates. The rate of duty is 12.5%. What is the AV, and what is total duty payable?

Answer:

Assessable Value is to be calculated on basis of selling price of trader which is ₹ 2,100 (cum-duty). This price is to be treated as inclusive of excise duty. Hence, assessable value will be (2,100 x 100)/112.50 i.e. ₹1,866.67. Basic excise duty @ 12.5% will be ₹ 233.33.

2.12.2 Valuation in Case of Job Work

Excise duty will not be payable if raw material/semi-finished components are sent for job work under Cenvat provisions or under notification No. 214/86-CE. However, in other cases, if job work results in 'manufacture' of a product, duty will become payable by job worker. Rule 1 0A of Valuation Rules, as inserted w.e.f. 1-4-2007 provides that in such cases, excise duty will be payable on the basis of price at which the raw material supplier (termed as 'principal manufacturer' in valuation rules) sales the goods. Rule 10A has been inserted in the Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000 to provide that where goods are manufactured by a job-worker on behalf of a person (commonly known as principal manufacturer), the value for payment of excise duty would be based on the sale value at which the principal manufacturer sells the goods, as against the present provision where the value is taken as cost of raw material plus the job charges - *Para 32.1 of DO letter F. No. 334/1 /2007-TRU dated 28-2 -2007*.

(i) **When the Goods are Sold by the Principal Manufacturer from the Premises of Job Worker:** In a case where the goods are sold by the principal manufacturer for delivery at the time of removal of goods from the factory of job-worker, where the principal manufacturer and the buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the transaction value of the said goods sold by the principal manufacturer;

(ii) **When the Goods are Sold by the Principal Manufacturer from a Place Other than the Premises of Job Worker:** In a case where the goods are not sold by the principal manufacturer at the time of removal of goods from the factory of the job-worker, but are transferred to some other place from where the said goods are to be sold after their clearance from the factory of job-worker and where the principal manufacturer and buyer of the goods are not related and the price is the sole consideration for the sale, the value of the excisable goods shall be the normal transaction value of such goods sold from such other place at or about the same time and, where such goods are not sold at or about the same time, at the time nearest to the time of removal of said goods from the factory of job-worker;

(iii) ***When Valuation as per Rule 10A(i) or 10A(ii) of Valuation Rules is not Possible –*** If valuation is not possible as per rule 10A(i) or 10A(2) of Valuation Rules, 'value' will be determined in accordance with the principles enunciated in the Valuation Rules on a case-to-case basis [rule 10A(iii) of Valuation Rules]. For example, if the excisable goods manufactured on job-work are sold by the principal manufacturer where the price is not the sole consideration for sale, the value of such goods shall be determined in terms of principles laid down in rule 6. If goods are captively consumed by Principal Manufacturer, valuation can be on basis of rule 8.

2.12.3 Manufacturer not Liable for Duty Liability of Scrap / Waste Generated at end of Job Worker

Earlier rule 57F provided that waste and scrap arising during job work is required to be returned to raw material supplier. New Cenvat Credit Rules make no such provision. Hence, in *Rocket Engineering Corporation* v. *CCE* 2006 (193) ELT 33 (CESTAT), it has been held that the scrap is not required to be returned to raw material supplier and the raw material supplier is not required to pay any duty on the scrap, since Cenvat Credit Rules after 1-4-2000 do not make any such provision – view confirmed in *CCE* v. *Rocket Engineering Corporation* (2008) 223 ELT 347 (Bom HC DB) - followed in *Emco Ltd.* v. *CCE* (2008) 223 ELT 613 (CESTAT). In Preetam Enterprises v. CCE 2004 (173) ELT 26 (CESTAT), it was held that even in respect of inputs sent under Cenvat Credit Rules, job worker is manufacturer of scrap and he is liable to pay duty on scrap. Duty on scrap cannot be demanded from raw material supplier after 1-4-2000 – same view in Rocket Engineering v. CCE 2006 (193) ELT 33 (CESTAT) [Scrap is treated as a final product if mentioned in the Tariff. However, it is 'final product' of job worker and not of raw material supplier].

In Silicon Cortec v. CCE (2004) 166 ELT 473 (CESTAT SMB), it has been held that waste and scrap is final product of job worker and he can clear the same on payment of duty. In Timken India v. CCE (2007) 215 ELT 182 (CESTAT), it was held that duty liability on scrap is of the job worker. If he is under SSI exemption, no duty is payable by him. In GKN Sinter Metals v. *CCE* 2007 (210) ELT 222 (CESTAT), it was held that if waste and scarp is only in nature of floor sweeping, and if there is invisible loss, no duty is required to be paid on such scrap.

2.13 SOME CRITICAL ISSUES IN CENTRAL EXCISE

2.13.1 Software is 'Goods', But Unbranded Software is Service

In Tata Consultancy Services v. State of Andhra Pradesh (2005) 1 SCC 308 = 141 Taxman 132 = 271 ITR 401 = AIR 2005 SC 371 = 2004 AIR SCW 6583 = 137 STC 620 = 178 ELT 22 (SC 5 member Constitution bench), it has been held that canned software (i.e. computer software packages sold off the shelf) like Oracle, Lotus, Master-Key etc. are 'goods'. The copyright in the programme may remain with originator of programme, but the moment copies are made and marketed, they become 'goods'. It was held that test to determine whether a property is 'goods' for purpose of sales tax, is not whether the property is tangible or intangible or in-corporal. The test is whether the concerned item is capable of abstraction, consumption and use, and whether it can be transmitted, transferred, delivered, stored, possessed etc. Even intellectual property, once it is put on a media, whether it be in form of books or canvas (in case of painting) or computer discs or cassettes and marketed would become goods. In all such cases, intellectual property has been incorporated on a media for purpose of transfer. The buyer is purchasing the intellectual property and not the media, i.e. the paper or cassette or discs or CD. There is no distinction between 'branded' and 'unbranded' software. In both cases, the software is capable of being abstracted, consumed and used. In both the cases, the software can be transmitted, transferred, delivered, stores, possessed etc. Unbranded software when marketed/sold may be goods.

However, Supreme Court did not express any opinion because in case of unbranded software, other questions like situations of contract of sale and/or whether the contract is a service contract may arise. Hence, in case of unbranded software, the issue is not yet fully settled. [SC upheld decision of AP High Court reported in Tata Consultancy Services v. State of AP (1997) 105 STC 421 (AP HC DB)].

In *Bharat Sanchar Nigam Ltd* . v. UOI (2006) 3 SCC 1 = 152 Taxman 135 = 3 STT 245 = 145 STC 91 = 282 ITR 273 (SC 3 member bench), following extract from decision in case of *Tata Consultancy Services v. State of Andhra Pradesh* was quoted with approval and adopted, 'A 'goods' may be a tangible property or an intangible one. It would become goods provided it has the attributes thereof having regard to (a) its utility; (b) capable of being bought and sold and (c) capable of being transferred, delivered, stored and possessed. If a software, whether customized or non-customized satisfies these attributes, the same would be goods'.

Earlier also, in *Associated Cement Companies Ltd*. v. CC 2001 (4) SCC 593 = 2001 AIR SCW 559 =128 ELT 21 = AIR 2001 SC 862 = 124 STC 59 (SC 3 member bench), it was held that computer software is 'goods' even if it is copyrightable as intellectual property.

In *State Bank of India v. Municipal Corporation* 1997(3) Mh LJ 718 = AIR 1997 Bom 220, it was held that 'computer software' is 'appliance' of computer. It was held that it is 'goods' and octroi can be levied on full value and not on only value of empty floppy. [In this case, it was held that octroi cannot be levied on license fee for duplicating the software for distribution outside the corporation limits].

Excise duty on software: All software, except canned software i.e. software that can be sold off the shelf, is 'exempt' under notification No. 6/2006-CE dated 1-3-2006.

Meaning of 'software': 'Information Technology Software' is defined in Supplementary Note of chapter 85 of Central Excise Tariff (and also Customs Tariff) as follows - 'For the purpose of heading 8523, 'Information Technology Software' means any representation of instructions, data, sound or image, including source code and object code, recorded in a machine readable form, and capable of being manipulated or providing interactivity to a user, by means of an automatic data processing machine'.

In CCE v. Pentamedia Graphics (2006) 198 ELT 164 (SC), it was held that 'motion picture animation file' recorded in a machine readable format and capable of being manipulated by automatic data processing machine is software – referred in Padmini Polymers v. CCE (2007) 215 ELT 392 (CESTAT), where it was held that multimedia application software on CD ROM is exempt. In this case, Cook Books and games which were interactive were held as 'software'. Reference was made to CBE&C circular No. 7/98-Cus dated 10-2-1998 where it was clarified that encyclopedia, games, books will be 'software' if these satisfy the interactivity criterion.

The SC decision was also followed in Gayatri Impex v. CC (2007) 215 ELT 397 (CESTAT) and Adani Exports v. CCE (2007) 210 ELT 443 (CESTAT). However, from the decision, it is not clear what was exactly imported. There is no requirement that to qualify as software, it must work without any operating system preloaded on computer. Any programme which requires anther programme like operating system will also be treated as software – Contessa Commercial Co. P Ltd. v. CC (2007) 208 ELT 299 (CESTAT). In this case, the importer had imported educational programmes and games.

Classification of encyclopedia, books on CD: In case of encyclopedia and books, there is hardly any 'interactivity', except that search engine helps in locating particular information. Further, search engine, which can be termed as 'software' forms insignificant part of the whole goods.

Applying the criteria of 'essential character' in case of mixture of goods, in my view, these cannot be termed as 'software'. These have to be classified as books.

Chapter 49, Note no 2 reads as follows, 'For the purpose of Chapter 49, the term 'printed' also means reproduced by means of a duplicating machine, produced under the control of an automatic data processing machine, embossed, photographed, photocopies, thermo-copied or type-written. Hence, it can be argued that a book can be 'printed' on CD since it is produced under the control of an automatic data processing machine.

As per item Sr. No. 26 of Notification No. 6/2006-CE dated 1-3-2006, CD-ROMs containing books of an educational nature, journal, periodicals (magazines) or newspaper are fully exempt from excise duty. Thus, a book can be on CD has been recognized in law.

Unbranded software is service

Though Supreme Court has held that tailor made software is also goods, Finance Bill, 2008 has imposed service tax on tailor made i.e. unbranded software. "Information technology software" means any representation of instructions, data, sound or image, including source code and object code, recorded in a machine readable form, and capable of being manipulated or providing interactivity to a user, by means of a computer or an automatic data processing machine or any other device or equipment. Any service provided or to be provided to any person, by any other person in relation to information technology software for use in the course, or furtherance, of business or commerce, including:—

(i) development of information technology software,

(ii) study, analysis, design and programming of information technology software,

(iii) adaptation, upgradation, enhancement, implementation and other similar services related to information technology software,

(iv) providing advice, consultancy and assistance on matters related to information technology software, including conducting feasibility studies on implementation of a system, specifications for a database design, guidance and assistance during the startup phase of a new system, specifications to secure a database, advice on proprietary information technology software

(v) acquiring the right to use information technology software for commercial exploitation including right to reproduce, distribute and sell information technology software and right to use software components for the creation of and inclusion in other information technology software products

(vi) acquiring the right to use information technology software supplied electronically, is a taxable service.

Departmental clarification : CBE&C TRU letter F. No.334/1/2008-TRU dated 29-1-2008 clarifies as follows -Software consists of carrier medium such as CD, Floppy and coded data. Softwares are categorized as "normal software" and "specific software". Normalised software is mass market product generally available in packaged form off the shelf in retail outlets. Specific software is tailored to the specific requirement of the customer and is known as customized software.

Packaged software sold off the shelf, being treated as goods, is leviable to excise duty. Number of IT services and IT enabled services (ITeS) are already leviable to service tax under various taxable services:

(i) Consulting engineer's service - advice, consultancy or technical assistance in the discipline of hardware engineering.

(ii) Management or business consultant's service - procurement and management of information technology resources.

(iii) Management, maintenance or repair service - maintenance of software, both packaged and customized and hardware.

(iv) Banking and other financial services - 'provision and transfer of information and data processing'.

(v) Business support service - various outsourced IT and IT enabled services.

(vi) Business auxiliary service - services provided on behalf of the client such as call centers.

IT software services provided for use in business or commerce are covered under the scope of the proposed service. Said services provided for use, other than in business or commerce, such as services provided to individuals for personal use, continue to be outside the scope of service tax levy. Service tax paid shall be available as input credit under Cenvat credit Scheme.

Software and upgrades of software are also supplied electronically, known as digital delivery. Taxation is to be neutral and should not depend on forms of delivery. Such supply of IT software electronically shall be covered within the scope of the proposed service.

With the proposed levy on IT software services, information technology related services will get covered comprehensively.

Duties on packaged/canned software [Notification No. 14/2011, dated 1-3-2011]:

Retail Sale Price (RSP) of packaged/canned software consist of two components namely

(i) Value of the software and

(ii) License (right to use)

The Central Board of Excise and Customs (CBE&C) issued Circular No. 15/2011 -Cus, dated 18.3.2011 to clarify the levy of Excise, Service Tax and Customs duties on packaged/canned software.

Packaged/Canned Software

- Affixation of RSP is mandatory
  - Assessable value based on MRP (Sec.4A of Central Excise Act, 1944)
    - Value of software and license will attract excise duty with an abatement of 15%
- Affixation of RSP is not mandatory
  - Assessable value based on Transaction value (Sec.4 of Central Excise Act, 1944)
    - Value of Software → Pay Excise duty
    - Value of License → Pay Service Tax

Note: if the packaged/canned software imported then the additional customs duty (CVD) under section 3(1) of the Customs Tariff Act, 1975 would be charged on value on the basis of MRP under section 4A of the Central Excise Act, 1944 provided affixation of RSP is mandatory. Otherwise additional customs duty (CVD) will be charged on the basis of Sec. 4 of the Central Excise Act, 1944.

2.13.2 Plant and Machinery Assembled at Site

Plant and Machinery assembled and erected at site cannot be treated as 'goods' for the purpose of Excise duty, if it is not marketable and movable. [It may be noted that even if goods are held as 'excisable', they will be exempt if manufactured within factory of production. See case law under '*Larsen & Toubro Ltd.* vs. *UOI* (*2009*(*243*)*ELT 662* (Mumbai)).

The word 'goods' applies to those which can be brought to market for being bought and sold, and it is implied that it applies to such goods as are movable. Goods erected and installed in the premises and embedded to earth cease to be goods and cannot be held to be excisable goods. - Quality Steel Tubes (P.) Ltd. v. CCE 75 ELT 17 (SC) = (1995) 2 SCC 372 = 6 RLT 131 = 1995 AIR SCW 11 - in this case, it was held that tube mill and welding head erected and installed in the premises and embedded in the earth for manufacture of steel tubes and pipes are not 'goods'. followed in Mittal Works v. CCE (1997) 1 SCC 203 = 1996 (88) ELT 622 (SC) = 106 STC 201 -quoted with approval in Thermax Ltd. v. CCE 1998(99) ELT 481 (SC) - same view in Triveni Engineering v. CCE AIR 2000 SC 2896 = 2000 AIR SCW 3144 = 40 RLT 1 = 120 ELT 273 (SC) * CCE v. Damodar Ropeways 2003(151) ELT 3 = 54 RLT 125 (SC 3 member bench).

In Municipal Corporation of Greater Bombay v. Indian Oil Corporation AIR 1991 SC 686 = 1991 Supp (2) SCC 18, it was held that if the chattel is movable to another place in the same position (condition?), it is movable property. If it has to be dismantled and re-erected at later place, it is attached to earth and is immovable property.

Assembly at site is not manufacture, if immovable product emerges: In Mittal Engg Works v. CCE

1996 (88) ELT 622 = 17 RLT 612 = 106 STC 201 = (1997) 1 SCC 203, it was held that if an article has to be assembled, erected and attached to the earth at site and if it is not capable of being sold as it is, without anything more, it is not 'goods'. Erection and installation of a plant is not excisable - followed in CCE v. Hyderabad Race Club 1996 (88) ELT 633 (SC), where it was held that an article embedded in the earth was not 'goods' and hence excise duty is not leviable – followed in TTG Industries v. CCE 2004 AIR SCW 3329 = 167 ELT 501 (SC) – same view in case of storage cabinets, kitchen counters etc. erected at site in Craft Interiors P Ltd. v. CCE 2006 (203) ELT 529 (SC) – same view in respect of refrigeration plant, air conditioning plant and caustic soda plant in CCE v. Virdi Brothers 2007 (207) ELT 321 (SC).

Capital Goods manufactured within factory of production are exempt even if manufactured by third party - It may be noted that capital goods manufactured within the factory and used within the factory are exempt from excise duty vide notification No. 67/1995-CE dated 16.3.1995.

The exemption is available even when the capital goods are manufactured in the factory of production by third party. [refer case law under 'Captive Consumption'].

Assembly is manufacture only if machinery can be removed without dis-assembly: In Triveni Engineering v. CCE AIR 2000 SC 2896 = 2000 AIR SCW 3144 = 40 RLT 1 = 120 ELT 273 (SC), it was observed, 'The marketability test requires that the goods as such should be in a position to be taken to market and sold. If they have to be separated, the test is not satisfied'. [Thus, if machine has to be dis-assembled for removal, it is not 'goods' and duty cannot be levied].

If machine (generating set in this case) is only bolted on a frame and is capable of being shifted from that place, it is capable of being sold. It is goods and not immovable property – Mallur Siddeswara Spinning Mills v. CCE 2004 (166) ELT 154 (SC).

Present legal position in respect of machinery erected at site: The latest judgment on the issue is of Triveni Engineering judgment dated 8-8-2000, which has been practically accepted by Board vide its circular dated 15-1-2002. Hence, the present legal provision is, as decided in Triveni Engineering , i.e. 'The marketability test requires that the goods as such should be in a position to be taken to market and sold. If they have to be separated, the test is not satisfied'. Thus, if machinery has to be dismantled before removal, it will not be goods. Following is also clear (a) Duty cannot be levied on immovable property (b) If plant is so embedded to earth that it is not possible to move it without dismantling, no duty can be levied (c) If machinery is superficially attached to earth for operational efficiency, and can be easily removed without dismantling, duty is leviable (d) Turnkey projects are not dutiable, but individual component/machinery will be dutiable, if marketable.

Article can be 'goods' if marketable before erection - An article will be liable to duty if its manufacture is complete before it is fastened to earth. Similarly, if 'machinery' is in marketable condition at the time of removal from factory of manufacture, duty will be leviable, even if subsequently, it is to be fastened to earth.

2.13.3 Dutiability of Steel and Concrete Structures

Following are covered in 'iron and steel structure' as defined in tariff heading 7308 – (i) big structures like bridges, transmission towers, and lattice masts, lock-gates, roofs etc. of iron and steel, (ii) parts of structures e.g. doors, windows and their frames, shutters, balustrades, pillars and columns etc. of iron and steel, (iii) Plates, rods, angles, shapes, sections, tubes and the like prepared for use in structures of iron and steel.

In Mahindra & Mahindra Ltd. v. CCE 2005 (190) ELT 301 (CESTAT 3 member LB), it has been held as follows –

(i) Immovable iron and steel structures are not goods.

(ii) Structures and parts mentioned in parenthesis of 7308 like bridges, lock-gates, towers, trusses, columns frames etc., in their movable state will be subject to excise duty, even if latter they get permanently fixed in the structures. (iii) Plates, rods, angles, sections, tubes and the like, prepared for use in the structures will also be excisable goods subject to duty *in their pre-assembled or disassembled state.*

Fabrication of steel structurals like columns, crane, grinders, trusses amounts to 'manufacture'- R S Avtar Singh v. CCE (2007) 213 ELT 105 (CESTAT).

Structure for pre-fabricated building is dutiable – Steel structure for prefabricated building is dutiable. – Mittal Pipe Mfg. Co . v. CCE 2002(146) ELT 624 (CEGAT).

Fabrication of steel structure at site is exempt : As per Sr. No. 64 of notification No. 3/2005-CE dated 24-2-2005, (earlier it was in tariff entry 7308.50), structures fabricated at site of work for use in construction at site are exempt from duty. In Delhi Tourism v. CCE 1999(114) ELT 421 (CEGAT), it was held that the term 'site' should be given wider meaning and not narrow meaning. Even if structure is cast at different place and brought to site of construction, it will be eligible for exemption.

2.13.4 Goods with Blank Duty Rate in Central Excise Tariff are 'Excisable Goods'

Some goods are mentioned in Central Excise Tariff but column of rate of duty is blank (e.g. live animals in Chapter 1, Electrical Energy in chapter 27, Newspaper and maps in Chapter 49).

As per additional note No. 1(c) to Central Excise Tariff, 'tariff item' means description of goods in the list of tariff provisions accompanying either eight-digit number and the rate of duty or eight-digit number with blank in the columns of the rate of duty. Hence, goods where duty rate is blank is excisable goods – para 22 of *Geetanjali Woolens* v. CCE (2007) 218 ELT 152 (CESTAT) [Interestingly, in case of Customs Tariff, the note 1(c) does not make mention of 'blank' rate in the column of rate of duty].

However, in CCE v. *Solaris Chemtech* (2007) 9 STT 412 = 214 ELT 481 (SC), it is observed that electricity is not an excisable item. In excise tariff, rate is 'blank' in items like rice, wheat, soya bean, cotton seed etc. These are 'produced'. In excise tariff, rate is 'blank' in items like rice, wheat, soya bean, cotton seed etc. These are 'produced'.

Goods mentioned as 'free' in Customs Tariff - In Associated Cement Companies Ltd . v. CC 2001 AIR SCW 559 = AIR 2001 SC 862 = (2001) 4 SCC 593 = 128 ELT 18 = 124 STC 59 = (SC 3 member bench), it was held that if duty rate specified in Customs Tariff Act is 'FREE' (i.e. no duty is payable), no duty is payable on such goods and hence these are not 'dutiable goods'. [In Central Excise Tariff, the duty rate indicated is 'Nil'. Hence, these are 'excisable goods'].

2.13.5 Manufacture –Other Aspects

Cutting of jumbo rolls of typewriter to make ribbon of standard length and winding on spool and blister packed - In Kores India v. CCE (2003) 152 ELT 395 (CEGAT), it was held that conversion of jumbo reels of ribbons into spool form to suit particular model and make of typewriting/telex machine is 'manufacture' as new and distinct product emerges – view upheld in Kores India v. CCE (2005) 1 SCC 385 = 174 ELT 7 (SC) – followed in CCE v. Sohum Industries Ltd .2006 (203) ELT 493 (CESTAT).

This decision was discussed in Anil Dang v. CCE (2007) 213 ELT 29 (CESTAT 3 member bench). It was held that this was no mere cutting and slitting but the roll was spooled on metal spools, plaster packed and sealed with aluminium foils. Hence, this decision will not apply where only slitting and cutting is involved.

Betel Nut to supari powder is not manufacture : Crushing betel nuts into smaller pieces and sweetening them does not result in a distinct product, as 'betel nut remains a betel nut' – Crane Betel Nut Powder Works v. CCE 2007 (210) ELT 171 = 6 VST 532 (SC) – decision of Tribunal in CCE v. Crane Betel Nut Powder Works 2005 (187) ELT 106 (CESTAT) is now not valid.

Upgradation of computer system is not manufacture : Upgradation of computer system by increasing its storage / processing capacity by increasing hard disk capacity, RAM or changing processor chip is not manufacture as new goods with different name, character and use do not come into existence. - CBE&C circular No. 454/20/99-CX dated 12-4-1999 – view confirmed in Maxim In formation Tech v. CCE 2005 (184) ELT 78 (CESTAT) * CCS Infotech v. CCE (2007) 216 ELT 107 (CESTAT).

2.13.6 Classification of Goods

Classification of parachute coconut oil : In Amardeo Plastics Industries v. CCE (2007) 210 ELT 360 (CESTAT 2 v. 1 order), on the basis of chapter notes, it was held that parachute coconut oil is 'vegetable oil' under chapter 15 and not 'preparation for use on the hair', since the marking on package did not say that it is for 'such specialized use', though advertisements did indicate so.

However, in Shalimar Chemical Works v. CST (2008) 12 VST 485 (WBTT), it has been held that except in a few Southern States, coconut oil is not treated as edible oil for use of daily cooking. In West Bengal, considering consumption pattern, coconut oil cannot be treated as 'edible oil'. It has to be treated as 'hair oil'.

Plastic name plate : Plastic name plate for motor vehicle is to be classified as 'accessory of motor vehicle' in chapter 87 and not 'other articles of plastic' in chapter 39, since 'name plate' is not specified in any heading in chapter 39 – Pragati Silicons P Ltd. v. CCE (2007) 8 VST 705 = 211 ELT 534 (SC).

Meaning of 'set of articles' : Distinction between laptop and desktop – 'Set of article' should consist of more than one item, each complementing the work of another and retaining their individual identity all the time – CC v. Acer India P Ltd. (2007) 218 ELT 17 (SC). In this case, it was held that a desktop computer is a combination of CPU with monitor, mouse and keyboard as a set. A desktop computer does not lose individual identities of CPU, monitor, mouse and keyboard. Not only they are marketable as separate items but are also used separately. On the other hand, a laptop (notebook computer) comes in an integrated and inseparable form. It is a combination of CPU, monitor, mouse and keyboard. A laptop cannot be said to be set of CPU with monitor mouse and keyboard – confirming Tribunal decision in CC v. Acer India P Ltd . (2007) 208 ELT 132 (CESTAT).

Software/records/tapes supplied along with equipment – Software imports are exempt from customs duty. Earlier, Customs and Central Excise Tariff had a note No. 6 which stated that software when presented with the apparatus for which it was intended will be classifiable as software. This note has been deleted w.e.f. 1-1-2007. Hence, software embedded or pre-loaded in machine is to be classified along with the machine. This will also be case when software is brought separately, but as a 'set'. If tangible software e.g. operating software or application software loaded on disk, floppy, CD-ROM etc. is imported, it will be classifiable as software under heading 8523 – CC (Import), Mumbai PN 39/2007 dated 3-12-2007. In CC v. Hewlett Packard India (Sales) P Ltd. (2007) 215 ELT 484 (SC), it was held that pre-loaded software in laptop forms integral part of the laptop. Without operating system like windows, the laptop cannot work. Hence, the laptop along with software has to be classified as laptop and values as one unit. Software pre-loaded cannot be classified separately as software (In this case, the importer wanted to classify hard disk along with software as 'software' and refused to give value of software even when called upon to do so. Hence, the decision has to be seen from peculiar facts of the case).

Principles of classification irrelevant for valuation : Classification decides the applicable rate. It is followed by valuation i.e. value at which rate is to be applied. The concept of 'classification' is therefore different from the concept of valuation. Section and chapter notes in Tariff and interpretative rules do not provide guidelines for valuation - CCE v. Frick India Ltd . (2007) 216 ELT 497 (SC).

2.14 ASSESSABLE VALUE UNDER SECTION 4

2.14.1 Factory can be Place of Removal even if Insurance taken by Assessee as Service to Customers

In Blue Star Ltd. v. *CCE* (2008) 224 ELT 258 (CESTAT), transport was arranged by assessee since individual customer cannot arrange for transportation. Insurance was taken for safe transport of goods, as a service to customers. It was held that insurance cover cannot be taken as criteria for determining ownership of goods. It was held that there was sale at factory gate and freight is not includible in assessable value.

2.14.2 Minimum Charges if Assured Quantity not Purchased, are not Part of Excise Assessable Value

In Jindal Praxair Oxygen v. CCE (2007) 208 ELT 181 (CESTAT), MTOP charges were payable to assessee if buyer fails to purchase minimum quantity assured, as in such cases, assessee is not in position to operate his plant at optimum capacity. It was held that these are not includible in assessable value - followed in CCE v. Praxair India (2008) 223 ELT 596 (CESTAT).

2.14.3 Place of Removal in Case of Exports

In case of exports, the place of removal is port where export documents are presented to customs office – Kuntal Granites v. CCE (2007) 215 ELT 515 = 2007 TIOL 930 (CESTAT) – quoted and followed in Rajasthan Spinning & Weaving Mills v. CCE (2007) 8 STR 575 (CESTAT).

2.14.4 Cash Discount Admissible Whether Availed or Not

In *CCE* v. *Arvind Mills Ltd.* (2006) 204 ELT 570 (CESTAT 3 member bench), it has been very clearly held that cash discount and finance cost are admissible under new section 4 of CEA also. Differential price represents interest for delayed payment. Cost of finance and cash discount whether availed or not are to be granted as abatement even after 1-7-2000.

2.14.5 Self Insurance Charges Addible

In *Gujarat Borosil* v. *CCE* (2007) 217 ELT 367 (CESTAT), assessee was collecting 7% amount was 'insurance charges'. Actual insurance premium paid was much less. The charge was to cover breakage of goods in transit. It was held that this cannot be permitted as deduction since assessee was not an insurance company.

2.14.6 Valuation of Free Samples

CBE&C, *vide* circular No. 813/10/2005-CX dated 25-4-2005 has clarified that in case of samples distributed free, valuation should be done on basis of rule 4 i.e. value of similar goods. The revised circular dated 25-4-2005 stating that valuation of samples should be on basis of rule 4, has been upheld as valid in *Indian Drugs Manufacturers' Assn* v. *UOI* (2008) 222 ELT 22 (Bom HC DB).

2.14.7 Valuation in Case of Stock Transfer

In case of stock transfer, value to be adopted is the price prevailing in depot at the time of clearance from factory. Once goods are cleared from factory to depot on payment of duty (on basis of price prevailing at the time of removal from factory), it is not necessary to chase the goods and see at what price the goods were subsequently sold -*CCE* v. *Carborandum Universal Ltd.* (2008) 224 ELT 290 (CESTAT).

2.14.8 Sale to Parent Company both as Spares as well as for Maintenance

In *CCE* v. *Aquamall Water Solutions* (2008) 223 ELT 385 (CESTAT), assessee sold its water purifying equipment to its parent company (Eureka Forbes Ltd.). Assessee also supplied parts of the water purifying equipment to its parent company, both for sale as spares and also for maintenance purposes. In case of spares for sale, duty was paid on the basis of selling price of spares of parent company. In case of parts supplied for use in maintenance, duty was paid on the basis of cost of production plus 10%. Department contended that in case of parts supplied for maintenance also, duty should be paid on basis of selling price of parent company. However, Tribunal held that when parts are not sold by parent company, duty should be paid under rule 8 on basis of cost of production plus 10% since no other specific rule to cover this (The decision is based on a Board circular which has since been withdrawn).

Part sale and part consumption – in *Ispat Industries Ltd.* v. *CCE* 2006 (201) ELT 65 (CESTAT), it was held that if goods are partially sold to unrelated buyers and partially supplied to sister concern, valuation should be under rule 4 i.e. on the basis of price at which goods are sold to other independent buyers – relying on *Aquamall Water Solutions* v. *CCE* 2003 (153) ELT 428 (CEGAT).- view upheld in *Ispat Industries* v. *CCE* 2007 (209) ELT 185 (CESTAT 3 member bench).

2.15 VALUE BASED ON RETAIL SALE PRICE

Section 4A of CEA empowers Central Government to specify goods on which duty will be payable based on 'retail sale price'.

The provisions for valuation on MRP basis are as follows :

(a) The goods should be covered under provisions of Legal Metrology Act, 2009, w.e.f. 1-8-2011 (earlier Standards of Weights and Measures Act, 1976) **[section 4A(1)].**

(b) Central Government has to issue a notification in Official Gazette specifying the commodities to which the provision is applicable and the abatements permissible. Central Government can permit reasonable abatement (deductions) from the 'retail sale price'**[section 4A(2)].**

(c) While allowing such abatement, Central Government shall take into account excise duty, sales tax and other taxes payable on the goods **[section 4A(3)].**

(d) The 'retail sale price' should be the maximum price at which excisable goods in packaged forms are sold to ultimate consumer. It includes all taxes, freight, transport charges, commission payable to dealers and all charges towards advertisement, delivery, packing, forwarding charges etc. If under certain law, MRP is required to be without taxes and duties, that price can be the 'retail sale price' **[Explanation 1 section 4A].**

(e) If more than one 'retail sale price' is printed on the same packing, the maximum of such retail price will be considered [Explanation 2(a) to section 4A]. If different MRP are printed on different packages for different areas, each such price will be 'retail sale price' for purpose of valuation **[Explanation 2(c) to section 4A].**

(f) Removing excisable goods without MRP or wrong MRP or tampering, altering or removing MRP declared on a package is an offence and goods are liable to confiscation [section 4A(4)] If price is altered, such increased price will be the 'retail sale price' for purpose of valuation **[Explanation 2(b) to section 4A]**.

For example, Government had issued a notification to the effect that excise duty on 'cosmetics and toilet preparations' will be payable on the basis of MRP printed on retail carton after allowing abatement of 40%. In such case, if MRP printed on carton is ₹ 200 and if the duty on 'cosmetics & toilet preparations' is 12.50%, the duty @ 12.50% will be payable on ₹ 120 (i.e. after allowing 40% abatement on MRP of ₹ 200). Thus duty payable per pack will be ₹ 15.

MRP provisions are overriding provisions– Section 4A(2) of Central Excise Act uses the words 'notwithstanding section 4A. Hence, when section 4A is applicable, provisions of section 4 for determination of assessable value are not applicable.

Provision of MRP based valuation are applicable only when product is statutorily covered both under Weights and Measures Act and notification issued under CEA - reiterated in Swan Sweets v. CCE 2006 (198) ELT 565 (CESTAT).

Same product sold in wholesale and under MRP– CBE&C has clarified in circular No. 737/53/2003-CX dated 19-8-2003 that when goods covered u/s 4A are supplied in bulk to large buyer (and not in retail), valuation is required to be done u/s 4. Provisions of section 4A apply only where manufacturer is legally obliged to print MRP on the packages of goods. Thus, there can be instances where the same commodity would be partly assessed on basis of section 4A and partly on basis of transaction value u/s 4.

Products covered under the MRP valuation scheme– So far, 96 articles have been covered under this scheme [Notification No. 2/2006-CE(NT) dated 1-3-2006.

Non-applicability of provisions of MRP– If an article is not covered under provisions in respect of marking MRP, provisions of duty payable on basis of MRP do not apply and in those cases, duty will be payable on *ad valorem* basis as per section 4. As per rules 2A and 34 of Standards of Weights and Measures (Packaged Commodities) Rules, 1977 (as amended w.e.f. 14-1-2007), the provisions of marking MRP are not applicable to following commodities – Packages above 25Kg (50 Kg in case of cement) * Packaged commodities for industrial or institutional consumers * Small packages of 10gm/10 ml or less * Fast food items * Scheduled drugs and formulations * Agricultural farm produce * Bidis for retail sale * Domestic LPG gas.

Deemed Manufacture of products covered under MRP– In respect of goods specified in third schedule to Central Excise Act, any process which involves packing or repacking of such goods in a unit container or labelling or re-labelling of containers including the declaration or alteration of retail sale price on the container or adoption of any other treatment on the goods to render the product marketable to consumer will be 'manufacture'. [section 2(f)(iii) effective from 14-5-2003].

2.16 MRP BASED VALUATION

2.16.1 Same product partly sold in retail and partly in wholesale

CBE&C has further clarified in circular No. 737/53/2003-CX dated 19-8-2003 that when goods covered u/s 4A are supplied in bulk to large buyer (and not in retail), valuation is required to be done u/s 4. Provisions of section 4A apply only where manufacturer is legally obliged to print MRP on the packages of goods. Thus, there can be instances where the same commodity would be partly assessed on basis of section 4A and partly on basis of transaction value u/s 4 – view noted and approved in Jayanti Food Processing v. CCE (2007) 10 STT 375 = 215 ELT 327 (SC).

2.16.2 Valuation on MRP basis even if package is not really intended for retail sale

In Jayanti Food Processing v. CCE (2007) 10 STT 375 = 215 ELT 327 (SC), it was observed that nature if sale is not the relevant factor for application of section 4A but application would depend on five factors i.e. (i) goods should be excisable goods (ii) They should be such as are sold in the package (iii) There should be requirement of SWM Act or rules or any other law to declare price of such goods relating to their retail price on package (iv) The Central Government must have specified such goods by notification of Official gazette and (v) Valuation of such goods would be as per the declared retail price on the package less the amount of abatement.

In ITEL Industries P Ltd. v. CCE 2004 (163) ELT 219 (CESTAT 2 v. 1 decision), telephone instruments were supplied to DOT/MTNL in bulk with MRP duly marked. DOT/MTNL lent these to subscribers retaining their ownership. It was held that since goods were packed, the valuation is required to be done u/s 4A on basis of MRP, even if goods were not sold to customers – followed in BPL Telecom v. CCE (2004) 168 ELT 251 = 60 RLT 664 (CESTAT), where it was held that there is no requirement under Packaged Commodities Rules that goods covered by those provisions must be actually sold in retail – view confirmed in Jayanti Food Processing v. CCE (2007) 10 STT 375 = 215 ELT 327 (SC).

This was followed in CCE v. Liberty Shoes (2007) 216 ELT 692 (CESTAT), where it was held that MRP provisions apply even when sale is in bulk to institutional buyers.

2.16.3 Provision does not apply to Ice Cream sold in bulk

In Monsanto Manufacturers v. CCE 2006 (193) ELT 495 (CESTAT), it was held that if ice cream is sold in bulk to hotels and not intended for retail sale, valuation will be as per section 4 and not on MRP basis – view confirmed in Jayanti Food Processing v. CCE (2007) 10 STT 375 = 215 ELT 327 (SC).

2.16.4 Two Items in Combi-Pack with One Item Free

In Icon Household Products v. CCE (2007) 216 ELT 579 (CESTAT), assessee was selling Mosquito Repellant Liquid (MRL) and Liquid Vapourising Device (LVD) as combi-pack. MRP was contained only on plastic container of MRL and not on LVD. It was held that this MRP will be taken for valuation of multipack. LVD supplied free in the multipack is not liable to assessment separately – relying on Himalaya Drug Company v. CCE (2006) 195 ELT 109 (CESTAT) - same view in CCE v. J L Morison (2008) 223 ELT 655 (CESTAT SMB).

2.16.5 No MRP on Free Gifts/Samples, Hence Valuation as Per Section 4

In Jayanti Food Processing v. CCE (2007) 10 STT 375 = 215 ELT 327 (SC), assessee as selling Kitkat chocolates to Pepsi. These were distributed as free gift along with Pepsi bottle as a marketing strategy. It was held that even if product (chocolate) is covered under MRP provisions, since the product was not to be sold in retail, MRP is not required. Hence, valuation should be on basis of section 4.

2.16.6 Provision when more than One Retail Price Declared

MRP printed on package is required to be inclusive of taxes. Rate of taxes vary from State to State. Hence, in some cases, a manufacturer may print different prices for different States. In some cases, manufacturer earmarks different packages for different areas and marks different prices for different areas.

If a package bears more than one retail sale price, maximum out of these will be deemed to be retail price for purpose of section 4A [Explanation 2(a) to section 4A(4)]. If retail price declared on the package at the time of removal is subsequently altered to increase the price, such increased retail price will be retail price for purpose of section 4A [Explanation 2(b) to section 4A(4)]. Where different retail sale prices are declared on different packages, each such retail price shall be the 'retail sale price' for purposes of valuation of excisable goods intended to be sold in area to which the retail price relates. [Explanation 2(c) to section 4A(4)]. Thus, if different prices are printed on different packages, each such price will be 'retail price'.

There is no stipulation in the Act that all packages should bear same MRP. Different MRPs for different buyers can be fixed. Even if MRP is different for each packet, such MRP is required to be adopted for assessable value– CCE v. Bell Granito Ceramics (209) 235 ELT 171 (CESTAT).

2.16.7 Provisions and Requirements of the Standards of Weights and Measures (Packaged Commodity) Rules, 1977 (''SWM Rules'')

The relevant provisions and requirements of the SWM Rules, are as follows

(1) **Only Packages Intended for Retail Sale Covered:** The requirement to declare retail sale price of the packages is applicable only in respect of packages intended for retail sale.

(2) **Goods on which RSP need not be Declared:** There is no requirement to declare RSP on-

(a) Packages of commodities containing quantity of more than 25 Kg or 25 Liters (excluding cement and fertilizer sold in bags up to 50 Kg.);

(b) Packaged commodities meant for industrial consumers or institutional consumers;

''Industrial consumer'' means those consumers who buy packaged commodities directly from the manufactures/packers for using the product in their industry for production etc.;

''Institutional consumers'' means those consumers who buy packaged commodities directly from the manufacturers/packers for service industry like transportation including airways, railways, hotel or any other similar service industry;

(c) Any domestic LPG cylinders of which the price is covered under the Administered Price Machanism of the Government;

(d) goods meant for export;

(e) goods supplied free as marketing strategy (e.g. physicians sample);

(f) any package containing fast food item packed by restaurant/ hotel and the like;

(g) any package containing a commodity if it contains schedule formulation and non-schedule formulations covered under the Drugs (price Control) order, 1995;

(h) Wholesale packages;

(i) agriculture farm produces in packages of above 50Kg.

(3) Certain Definitions:

(a) retail packages means the packages intended for retail sale to the ultimate consumer for consumption of the commodity contained therein and includes the imported packages. The expression 'ultimate consumer' doesn't include industrial or institutional consumers.

(b) retail sale means the sale, distribution or delivery of a commodity through retail sale agencies or other instrumentalities for consumption by an individual or a group of individual or any other consumer.

(c) wholesale package means a package containing-

(i) A number of retail packages, where wholesale package is intended for sale, distribution or delivery to an intermediary and is not intended for sale direct to a single consumer; or

(ii) A commodity sold to an intermediary in bulk to enable such intermediary to sell, distribute or delivery such commodity to the consumer in smaller quantities; or

(iii) Packages containing ten or more than ten retail packages provided that the retail packages are labeled as required under the rules.

Example 33: 1,500 pieces of a product 'A' were manufactured during the financial year. Its list price (i.e. retail price) is ₹250 per piece, exclusive of taxes. The manufacturer offers 20% discount to wholesalers on the list price. During the year, 840 pieces were sold in wholesale, 510 pieces were sold in retail, 35 pieces were distributed as free samples. Balance quantity of 115 pieces was in stock at the end of the year. The rate of duty is 12.5%. What is the total duty paid during the financial year?

Assume that the manufacture is not eligible for SSI concession.

Answer:

The total selling price is as follows –

Qty	Price	Total (₹)
510	250	1,27,500
840	200	1,68,000
35	200	7,000
Total		3,02,500

Duty payable is 12.5% of ₹ 3,02,500 i.e. ₹ 37,812.50.

Note – (a) Since 115 pieces were in stock at year end, no duty will be payable. Duty will be payable only when goods are cleared from factory. (b) In case of samples, as per rule 4 of Valuation Rules, value nearest to the time of removal, subject to reasonable adjustments is required to be taken. However, since prices are varying, value nearest to the time of removal may not be ascertainable and will not be acceptable for valuation as the prices are changing. In such case, recourse will be taken to rule 11 of Valuation Rules, i.e. best judgment assessment. We can take recourse to rule 7 and 9 where principle of 'normal transaction value' is accepted, when prices are varying.

As per rule 2(b) of Valuation Rules, 'normal transaction value' means the transaction value at which the greatest aggregate quantity of goods is sold. Since greatest quantity of 840 pieces are sold at ₹ 200, that will be 'normal transaction value', which can be taken for valuation of free samples.

Example 34: A manufacturer has appointed brokers for obtaining orders from wholesalers. The brokers procure orders for which they get brokerage of 5% on selling price. Manufacturer sells goods to buyers at ₹ 250 per piece. The price is inclusive of State Vat and Central Excise Duty. State Vat rate is 4% and excise duty rate is 12.5%. What is the AV, and what is duty payable per piece?

Answer:

Assume that Assessable Value = x. No deduction is available in respect of brokerage paid to third parties from Assessable Value.

Since Excise duty is 12.5%, State Vat rate is 4%, price including excise will be 1.125x.

State Vat @ 4% of 1.125*x* is 0.045x. Hence, price inclusive of sales tax and excise duty will be 1.17x.

Now,	1.17x = ₹ 250.00
Hence,	*X* = ₹ 213.68
Check the answer as follows –	
Assessable Value	= ₹ 213.68
Add duty @ 12.5% of ₹ 213.68	= ₹ 26.71
Add: State Vat @ 4% on ₹ 240.39 (213.68+26.71)	= ₹ 9.61
Total Price (Including duty and tax)	
(213.68+26.71+9.61)	= ₹ 250.00

Example 35: Find Assessable Value and duty payable. The product is not covered under section 4A. Maximum Retail Trade Price : ₹ 1,100 per unit, State Vat, Octroi and other Local Taxes: 10% of net price, Cash Discount : 2%, Trade Discount: 8%, Primary and Secondary packing cost included in the above MRP: ₹ 100, Excise duty rate: 12.5% ad valorem.

Answer:

Cash discount ₹ 22 (2% of ₹ 1,100) and trade discount ₹ 88 [8% of ₹1,100] are available as deduction. Packing cost is not allowable as deduction. Hence, price of excise purposes is ₹ 990. [₹1,100 – 22 – 88]. — Now, if x is the assessable value, price inclusive of excise duty is 1.125x. State Vat and local taxes @ 10% of 1.125x will be 0.11125x and price including Excise duty is inclusive of excise duty and sales tax will be 1.2375x.

Now,	1 .2375 x	=	₹ 990.00
Hence,	x	=	₹ 800.00
Excise Duty @ 12.5% of ₹ 800.00		=	₹ 100.00
Check the answer as follows: Assessable Value		=	₹ 800.00
Add: Excise duty @ 12.5% of ₹ 800.00		=	₹ 100.00
Add State Vat @ 10% on ₹ 900.00		=	₹ 90.00
(800 + 100)			
Total Price (After allowable deductions)		=	₹ 990

Example 36: A manufacturer has agreed to supply a machinery on following terms and conditions : (a) Price of machinery : ₹ 3,40,000 (net of taxes and duties), (b) Machinery erection expenses : ₹ 26,000, (c) Packing (normally done by him for all machinery) : ₹ 4,000, (d) Design and drawing charges relating to manufacture of machinery : 30,000 or (Net of taxes and duties), (e) Central Sales Tax @2%, (f) Central Excise Duty @ 12.5%, (g) Cash discount of ₹ 5,000 will be offered if full payment is received before dispatch of goods, (h) The buyer made all payment before delivery, (i) The manufacturer incurred cost of ₹ 1,200 in loading the machinery in the truck in his factory. These are not charged separately to buyer. Find the 'Assessable Value'and the duty payable.

Answer:

Erection expenses are not includible in AV. Cash discount is allowable as deduction. Duty is not payable on optional bought out accessories supplied along with the machinery. The cost of ₹ 1,200 is already included in the selling price of machinery (as it is not charged separately) and hence is not to be added again. Hence, AV is ₹ 3,69,000 [₹ 3,40,000 + ₹4,000 + ₹30,000 – ₹5,000]. Duty @ 12.5% will be ₹46,125.

Example 37: M/s. XYZ Ltd., sold machinery to Mr. Kapoor at a price of ₹ 5 lakhs on 15th June, 2015 and the same was removed from the factory at Kolkata. The rate of excise duty applicable is 12.5% on the date of removal. Mr. Kapoor refused to take delivery of the machine when it reached his destination. In the meantime, M/x. XYZ Ltd. increased the prices of the similar type of machinery to ₹ 6 lakhs with effect from 16th June, 2015. The machinery as refused by Mr. Kapoor has been sold on 20th June 2015 to Mr. Lal at the revised price of ₹ 6 lakhs. The excise duty including Education Cess is 12.5% applicable with effect from 10th June, 2015.

Explain the following with reasons:

(i) What is the value to be taken as assessable value?

(ii) What is the rate of excise duty applicable and duty payable on above transaction?

(iii) The Central Excise Officer is demanding duty on the price of ₹ 6 lakhs at the time of sale to Mr. L. Is he right in his approach?

(iv) Does cost of production have any bearing on the assessable value?

Answer:

(i) The price prevailing at the time of removal from factory i.e. ₹ 5 lacs on 15th June 2015 is the assessable value.

(ii) The applicable rate of duty is @12.5% and duty amount is ₹ 62,500 (i.e. ₹ 5 lacs x 12.5/100).

(iii) The Central Excise Officer is not right in his approach.

(iv) Cost of production has no bearing with assessable value in present case. Central Excise valuation can be below manufacturing cost. If price is the sole consideration and dealing between seller and buyer are arm's length, assessable value will be decided on the basis of selling price, even if it is below manufacturing cost. So cost of manufacturing will not change the assessable value.

Example 38: ABC Ltd of Kanpur agreed to sell an electronic motor to DEF Ltd of New Delhi for ₹ 15,000.00 on ex-factory basis. Other particulars are:

(i) Transportation and transit insurance were arranged by ABC Ltd. This was at the request of DEF Ltd and amounted to for ₹ 1,250 and ₹ 1,500 respectively which were charged separately. Actual transportation charges amounted to ₹ 1,000 only.

(ii) A discount of ₹ 1,000 was given to DEF Ltd. on the agreed price on payment of an advance of ₹ 3,500 with the order. (Ignore notional interest on advance).

(iii) Interest of ₹ 800 was charged from DEF Ltd. as it failed to make the payment within 30 days.

(iv) Packing charges of the motor amount to ₹ 1300.

(v) The expenditure incurred by ABC Ltd. towards 'free after sale service' during warranty period comes out to be ₹ 500 per motor.

(vi) Dharmada charges of ₹ 200 were recovered from DEF Ltd.

(vii) ABC Ltd. sold a lubricant worth ₹ 250 along with the motor to the interested customers. Lubricant which was purchased from the market by ABC Ltd. at ₹ 200 ensured durability and high efficiency of the motor. DEF Ltd. opted for the said lubricant.

Compute the Assessable Value.

Answer:

Calculation of Assessable Value

Offered Price to DEF	=	14,000
Add: Discount	=	1,000
Add: Packing charges	=	1,300
Add: Free after sale service	=	500
Add: Dharmada charges	=	200
Assessable Value	=	17,000

Example 39: How will the assessable value under the subject transaction be determined under section 4 of the Central Excise Act, 1944? Give reasons with suitable assumptions where necessary.

Contracted sale price for delivery at buyer's premises ₹ 10,00,000. The contracted sale price includes the following elements of cost:

(I)	Cost of drawings and designs	₹ 3,000
(II)	Cost of primary packing	₹ 3,500
(III)	Cost of packing at buyer's request for safety during transport	₹ 7,500
(IV)	Excise duty	₹ 2,11,200
(V)	VAT (Sales tax)	₹ 37,000
(VI)	Octroi	₹ 9,500
(VII)	Freight and insurance charges paid from factory to 'place of removal	₹ 20,000
(VIII)	Actual freight and insurance from 'place of removal' to buyer's premises	₹ 42,300

Answer:

Sale price	₹ 10,00,000
Less: Excise Duty	₹ 2,11,200
VAT	₹ 37,000
Octroi	₹ 9,500
Freight and insurance from Place of removal to buyers	₹ 42,300
	₹ 3,00,000
Assessable Value	₹ 7,00,0000

Example 40: Determine the assessable value for purpose of excise duty under the Central Excise Act, 1944 in the following cases:

(i) An assessee sells his excisable goods for ₹ 1,12,360 per unit and does not charge any duty of excise in his invoice. Subsequently it was found that the goods were not exempted from excise duty but were liable at 12.5%.

(ii) Certain excisable goods were sold for ₹ 1,12,360 per unit and @12.5% is the rate of excise duty. Subsequently it was found that the price cum duty was in fact ₹ 1,40,000 per unit as the assessee had collected ₹ 40,124 per unit separately.

(iii) The cum duty price per unit was ₹ 1,10,300 and the assessee had paid duty at 12.36%. subsequently it was found that the rate of duty was 12.5% and the assesee had not collected anything over and above ₹ 1,10,300 per unit.

Answer:

Statement showing Assessable Value for the Purpose of Excise Duty in each case: (As per CBE&C DO letter No. 334/1/2003- TRU dated 28.2.2003)

Sl. No.	Particulars	Value (₹)	Workings
(i)	Assessable value	99,876	₹ 1,12,360 x 100/112.50 = ₹ 99,876
(ii)	Assessable value	1,24,444	Cum-duty price ₹ 1,12,360 (12.5% duty inclusive). Hence, assessable value is ₹99,876. Additional consideration received subsequently of ₹ 40,124. Hence, Cum-duty price is ₹ 1,40,000. 1,40,000 x 100/112.5 = ₹ 1,24,444
(iii)	Assessable value	98,044	Cum-duty price ₹ 1,10,300 (excise duty included @12.36%). However, correct rate of duty is 12.5%. If no additional consideration has been received, then ₹ 1,10,300 is it self considered as inclusive of excise duty @12.5%. 1,10,300 x 100/112.5 = ₹ 98,044.

Maximum Retail Price (MRP)

Example 41: B Ltd manufactures two products namely, Eye Ointment and Skin Ointment. Skin Ointment is a specified product under section 4A of the Central Excise Act, 1944. The sale prices of the two products are ₹ 43 per unit and ₹ 33 per unit respectively. The sale price of both the products included 12.5% excise duty as BED, education cess of 2% and SAH of 1%. It also includes CST of 2%. Additional information is as follows:

Units cleared: Eye Ointment - 1,00,000 units, Skin Ointment – 1, 50,000 units. Deduction permissible under section 4A: 40%

Calculate the total excise duty liability of B Ltd for both the products.

Answer:

Eye Ointment:

Let us assume x as the assessable value

Assessable Value	=	x	
Add: BED @12.5%	=	0.125x	
	=	1.125x	
Add: CST @ 2%	=	0.0225x	
Selling price	=	1.1475x	
Assessable value per unit		₹ 43 x 1/1.1475	
	=	₹ 37.47 per unit	
Total Assessable Value	=	₹ 37,47,000	(i.e. ₹ 37.47 x 1,00,000 units)
Excise duty @12.5% on 1,00,000 units	=	₹ 4,68,375	

Skin Ointment

Maximum Retail Price	=	₹ 33	
Less: Abatement @40%	=	₹ (13)	
Assessable Value (per unit)	=	₹ 20	
Total Assessable Value	=	₹ 30,00,000	(i.e. ₹ 20 x 1,50,000 units)
Excise Duty @12.5%	=	₹ 3,75,000	
B Ltd liable to pay total excise duty	=	₹ **8,43,375**	

Transaction Value with Valuation Rules

Example 42: Cost of production of a product X calculated as per Cost Accounting Standard is ₹ 350 per piece.

550 pieces of a product were manufactured. 120 pieces were sold at ₹ 700 per piece to Industrial Consumers. 70 pieces were sold to a Central Government department @ ₹ 690 per piece. 210 pieces were sold to wholesalers at ₹ 720 per piece. 70 pieces were sold in retail @ ₹ 800 per piece. 20 pieces were given out as free samples. Out of the 70 pieces sold to Government department, 25 pieces were rejected, which were subsequently sold to other customers @ ₹ 300 per piece, without bringing them in the factory. Balance pieces were in stock, out of which 25 pieces were so damaged that they became unsaleable.

Note that all the prices are exclusive of excise and sales tax. The rate of duty on the product is 12.5% plus education cess as applicable.

(a) What is the total duty payable?

(b) Advise Management about steps to be taken in respect of 25 pieces which were damaged in storage.

Answer:

(a) Calculation of duty payable on product X

Name of the buyer	Number of pieces	Rate per piece (₹)	Total (₹)
Industrial Consumers	120	700	84,000
Central Government department	70	690	48,300
Wholesalers	210	720	1,51,200
Retailers	70	800	56,000
others (Free samples) (Rule 4)	20	720	14,400
Assessable Value			3,53,900

Total excise duty @12.5% (3,53,900×12.5%) ₹ 44,238

(b) As per Rule 21 of the Central Excise Rules, 2002, obtain the remission certificate from the central excise department for the damaged units of 25 pieces.

Valuation Rules:

Example 43: Compute the assessable value and excise duty under the Central Excise Act, 1944 in the following case:

Production	:	2,000 units on 1.7.2015
Quantity sold	:	450 units @ ₹ 200 per unit
	:	650 units @ ₹ 190 per unit
Samples clearances	:	50 units
Balance in stock	:	850 units (at the end of factory day for 1-7-2015)

Assume that the rate per unit is exclusive of Central Excise duty. Basic Excise Duty @12.5%.

Answer:

Assessable value

Units	Rate per unit (₹)	Total (₹)	Remarks
450	200	90,000	
650	190	1,23,500	
50	190	9,500	Samples are valued as per rule 4 read with rule 2(c) of C.Ex. Valuation Rules, 2000
Assessable Value		2,23,000	

Total excise duty = ₹ 27,875 (i.e.₹ 2,23,000 x 12.5%)

Example 44: A manufacturer having a factory at Mumbai has uniform price of ₹ 2,000 per unit (exclusive of taxes and duties) for sale anywhere in India. During the financial year 2015-16, he made the following sales:

Particulars	Quantity sold in units	Cost of transportation (₹)
Goods sold at factory in Mumbai	1,000	Nil
Goods sold from New Delhi	500	12,000
Goods sold from Chennai	600	48,000
Goods sold from Kolkata	900	30,000

Find assessable value per unit and total excise duty payable by the manufacturer. Excise duty @12.5%.

Answer:

(Rule 5 of valuation rule)

Selling price per unit	=	₹ 2,000
Less: cost of equalized freight	=	₹ 30
Assessable value per unit	=	₹ 1,970
Total excise duty payable	=	₹ 7,38,750 (3,000 units x ₹ 1 ,970 per unit × 12.5%)

Working note: (1)

Particulars	Quantity sold in units	Cost of transportation (₹)
Goods sold at factory in Mumbai	1,000	Nil
Goods sold from New Delhi	500	12,000
Goods sold from Chennai	600	48,000
Goods sold from Kolkata	900	30,000
Total	3,000	90,000

(2) Cost of equalized freight = ₹ 30 (₹ 90,000/3,000 units)

(3) The aforesaid equalized freight has to be certified by the Cost Accountant/Chartered Accountant/ Company Secretary in practice.

Example 45: Compute the assessable value and amount of excise duty payable under the Central Excise Act, 1944 and rules made there-under from the following information:

Particulars	No. of units	Price at Factory Per unit	Price at Depot Per unit	Rate of Duty Advalorem
(i) Goods transferred from factory to depot on 8th August	1,000	₹ 200	₹ 220	12.5%
(ii) Goods actually sold at depot on 18th August	950	₹ 320	₹ 350	8%

Answer:

(Rule 7 of valuation rules)

	Amount (₹)	
Assessable Value	2,20,000	[i.e. 1,000 units × ₹ 220]
Total Excise Duty	27,500	[i.e. ₹ 2,20,000 × 12.5/100]

Example 46: Name the Cost Accounting Standard which is to be used while calculating cost of production for valuation for captive consumption under Central Excise. Is the standard mandatory? AS per that standard, which of the following costs are includible/not includible in 'Cost of Production'?

(i) Research and Development Cost

(ii) Interest on capital borrowed,

(iii) Lay-off wages to workmen

(iv) Packing cost.

Answer:

(Rule 8 of valuation rules)

The Cost Accounting Standard 4 is required to be used while calculating cost of production for valuation for captive consumption under Central Excise. As per circular issued by CBEC, cost of production is required to be calculated as per CAS-4 issued by the Central Council Members of The Institute of Cost Accountants of India (ICAI). Hence, the standard is mandatory.

Cost includible	Cost not includible
(i) Research and Development	(i) Interest on capital borrowed
(ii) Packing cost	(ii) Lay off wages to workmen

Example 47: X Ltd. manufacturer manufactured components within factory for own use. Cost of raw materials purchased for ₹ 50,000 to manufacture said components. Cost of overheads as certified by a Cost Accountant, as per Cost Accounting Standard (CAS) – 4 is ₹ 20,000. Profit margin on inter departmental transfer @20%. These components are subject to Excise Duty @12.5% and State VAT rate @12.50%.

You are required to answer (a) Assessable Value of these Components, (b) Total Excise Duty and (c) Value Added Tax (VAT).

Answer:

(Rule 8 of valuation rules)		₹
Cost of Material	=	50,000
Overhead Cost	=	20,000
Cost of Production	=	70,000
ADD: 10% profit margin (as per Rule 8 of Valuation Rules)	=	7,000
(a) Assessable Value	=	77,000
(b) Excise Duty	=	₹ 77,000 x 12.5/100 = ₹ 9,625

(c) VAT payable is nil, since these components are consumed internally. VAT will attract only when there is a sale.

Example 48: R & Co. furnish the following expenditure incurred by them and want you to find the assessable value for the purpose of paying excise duty on captive consumption. Determine the cost of production in terms of rule 8 of the Central Excise Valuation (Determination of Price of Excisable Goods) Rules 2000 and as per CAS – 4 (Cost Accounting Standard):

(i)	Direct material cost per unit inclusive of excise duty at 12.5%	₹ 880
(ii)	Direct wages	₹ 250
(iii)	Other direct expenses	₹ 100
(iv)	Indirect materials	₹ 75
(v)	Factory overheads	₹ 200
(vi)	Administrative overhead (25% relating to production capacity)	₹ 100
(vii)	Selling and distribution expense	₹ 150
(viii)	Quality control	₹ 25
(ix)	Sale of scrap realised	₹ 20
(x)	Actual profit margin	15%

Answer:

Cost of production is required to be computed as per CAS-4. Material cost is required to be exclusive of Cenvat credit available.

	Particular	**Total Cost (₹)**
1.	Material Consumed (Net of Excise duty) [₹ (880 -97.77)]	782.23
2.	Direct Wages	250.00
3.	Other Direct Expenses	100.00
4.	Works Overhead [indirect material (₹ 75) plus factory overhead (₹ 200)	275.00
5.	Quality control cost	25.00
6.	Administrative Overhead (25% relates to production activity)	25.00
	Less : Sale of Scrap	(20.00)
	Cost of Production	1,437.23
	Add : 10% profit margin on cost of production (₹) 426.23 x 10%)	143.72
	Assessable value as per Rule 8 of the valuation rules	1,580.95

Note : Actual profit margin is not relevant for excise valuation.

Tax Planning

Example 49: A company manufacturing a dutiable product in the factory at Cochin, was making sales through its depot in Mumbai. The sale price at Mumbai depot at ₹ 30,000 per piece inclusive of transport charges from Cochin to Mumbai of ₹ 3,000. The depot price includes excise duty @12.5% but excludes Maharashtra VAT. Annually 2,000 pieces are sold by the depot. The company decides to make direct sale from Cochin to its customers which would attract CST at 2% to be borne by the company. The company wants to close down the depot at Mumbai bringing cost saving of ₹ 5,00,000 per annum. The sale price will continue to be as earlier.

Evaluate the implications of the decision.

Answer:

Depot continues:

Presently, goods are sold from depot. If the sale is from depot, excise duty is payable on the depot price of ₹ 30,000. No deduction of transport cost from Cochin to Mumbai depot is allowed.

Since, the price is inclusive of excise duty @ 12.5%, the duty payable is ₹ 3,333.33 (i.e. ₹ 30,000 x 12.50 /112.50) and Assessable Value is ₹ 666.67 (i.e. ₹30,000 x 100/112.5).

	Value per piece
Depot sale price	₹ 30,000
Less: Transport charges	₹ 3,000
Less: Excise duty	₹ 3,333
Net revenue if depot continues	₹ 23,667

Depot closes down:

If goods are sold directly from Cochin, CST @ 2% will be payable. The price chargeable to dealers is required to remain unchanged at ₹ 30,000 per piece.

Net price of Product	x
Add- Excise Duty @ 12.50%	0.125x
Taxable turnover	1.125x
Add- CST @ 2% on 1.125x	0.0225x
Total price	1.1475x
Add- Transport charges	₹ 3,000
Total Invoice Value	1.1475x + 3,000

Note. – Excise duty and CST are not payable on transport charges, if charged separately in invoice, because sale is from factory.

Now, 1.1475x + 3,000 = ₹ 30,000

Net price of the product = ₹ 23,529 [(i.e. ₹ 30,000 – 3,000)/1.1475]

Net realizable value is ₹ 23,529 per piece if the depot closes down.

If depot continues the revenue		₹ 23,667	per piece
Less: If depot closes down the revenue		₹ 23,529	per piece
Net revenue loss if depot closes down		₹ 138	per piece
Total revenue loss for 2,000 pieces annually if depot closes down (i.e. 2,000 pieces × ₹ 138 per piece)		₹ 2,76,000	
Less: Savings on account of closes down the depot	=	₹ 5,00,000	
Net savings on account of close down the depot	=	₹ 2,24,000	

If depot is closed, there will be net savings of ₹ 2,24,000 per annum.

Hence, it is economical to close down the depot.

2.17 ASSESSMENT UNDER CENTRAL EXCISE LAW

2.17.1 Assessment [Rule 6 & 7]

Before each removal, whether outside the factory of manufacture or production or for captive consumption, duty has to be assessed on the excisable goods.

The expressions ‘assessment’ and ‘assessee’ have been defined in the Central Excise Rules, 2002.

‘Assessment,’ as per Rule 2(b), includes

(a) Self-assessment of duty made by the assessee, and

(b) Provisional assessment under Rule 7 of the said Rules.

‘Assessee’, as per Rule 2(c), means

(a) any person, who is liable for payment of duty assessed or

(b) a producer or manufacturer of excisable goods or

(c) manufacturer of excisable goods or

(d) a registered person of a private warehouse in which excisable goods are stored and includes an authorized agent of such person.

2.17.2 Liability to Assessment and Payment of Duty

Rule 4 of the Central Excise Rules, 2002 provides that every person, who produces or manufactures any excisable goods, or who stores such goods in a warehouse, shall pay the duty leviable on such goods in the manner provided in Rule 8 or under any other law and no excisable goods, on which any duty is payable, shall be removed without payment of duty from any place, where they are produced or manufactured, or from a warehouse, unless otherwise provided.

Incidence of Duty i.e. Removal

For the purposes of the Rule 4, excisable goods manufactured in a factory and utilized, as such or after subjecting to any process, for the manufacture of any other commodity, in such factory, shall be deemed to have been removed from such factory immediately before such utilization.

Major Ingredients of Assessment

Before each removal, whether outside the factory of manufacture or production or for captive consumption, duty has to be assessed on the excisable goods.

Classification and Rate of Duty

For determining the rate of duty, classification is a prerequisite.

Classification means the appropriate classification code, which is applicable to the excisable goods in question under the First Schedule to Central Excise Tariff Act, 1985. There are Section Notes and Chapter Notes, in the Tariff which are helpful in determining the appropriate classification. In case of difficulties, there are "Interpretative Rules" in the said Act.

Determination of Rate of Duty

After classification, determine the appropriate rate of duty.

Valuation

Where rate of duty is dependent on the value of goods *(ad valorem duty)*, value has to be determined, in accordance with the provisions of Central Excise Act, 1944, as follows :

(i) Value under section 4 based on transaction value or determined in terms of valuation Rule,

(ii) Value based on retail sale price under section 4A,

(iii) Tariff value fixed under section 3.

Quantity

Where duty is on value, the total value is determined by multiplying Unit value with the Total Quantity. The unit quantity of goods is also required in cases where duty is charged at specific Rate.

2.17.3 Self Assessment [Rule 6]

(a) For Excisable goods other than Cigarettes

As per Rule 6 of the Central Excise Rules, 2002 a Central Excise assessee is himself (self-assessment) required to determine duty liability at the time of removal of excisable goods and discharge the same. In other words, the assessee should apply correct classification and value *(where duty is ad valorem)* on the quantities being removed by him and indicate the same in the invoice. However, in case assessee manufacturing cigarettes, the Superintendent or Inspector of Central Excise has to assess the duty payable before removal by the assessee.

(b) Cigarettes

Assessment before removal of the goods- by the Superintendent or Inspector of Central Excise.

(c) Scrutiny of assessment

(i) Resposibility of departmental officers to scrutinize the assessment

In view of the self-assessment procedure wherein the assessee himself assesses the duty liability, the responsibility of the Departmental officers [Central Excise Officers having jurisdiction over the factory/ premises of the assessee] is to scrutinize the assessment made for verification of its correctness.

(ii) Documents required by officer

For this purpose, the said officer(s) may require the relevant documents. Though the statutory records have been dispensed with, the assessee is required to maintain private records containing all requisite information as required by different rules and also provide a list of all records maintained by him to the Range Office.

The Officer responsible for scrutiny of return may require:

- Invoices issued by the assessee
- Daily Stock Account
- CENVAT Account
- Cash ledgers
- Ledger of all receipts and payments
- Source documents etc.

(iii) Compulsory for assessee to furnish the documents

It shall be compulsory for the assessee to provide the necessary records upon receiving the 'Requisition Letter' from the Range Officer or other superior officers. He shall hand over the records under proper acknowledgement and receive them back under proper acknowledgement. The officer scrutinizing return may require presence of the assessee or his authorised person at mutually convenient time, for seeking certain information relating to the records.

(iv) Scrutiny of assessment

The Superintendent of Central Excise in charge of the Range Office, with assistance of the Inspectors in-charge of the factory of an assessee, will scrutinise all the returns. They shall, in selected cases, call for all connecting documents including invoices and the records and scrutinise the correctness of assessment.

Central Excise Officer who will scrutinized the return	Amount of duty paid by the unit through PLA per annum every six months
Deputy/ Assistant Commissioner of Central Excise	> ₹ 1 Crore, but < ₹ 5 crores
Additional/ Joint Commissioner of Central Excise	≥ ₹ 5 Crores

2.17.4 Provisional Assessment

Provisional assessment is resorted to, where the assessee is unable to determine the

(i) Value of Excisable goods, or

(ii) Rate of duty applicable

AC or DC of central excise, as the case may be, shall pass order for final assessment, as soon as may be, after the relevant information, as may be required for finalizing the assessment, is available, but within a period not exceeding six months from the date of the communication of the order issued under sub-rule (1);

Provided that the period specified in this sub-rule may, on sufficient cause being shown and the reason to be recorded in writing, be extended by the commissioner of central Excise for a further period not exceeding six months and by the Chief Commissioner of Central Excise for such further period as he may deemed fit.

Guidelines and Procedure for Provisional Assessment

(a) Request in Writing

Rule 7 of the Central Excise Rules lays down that where the assessee is unable to determine the value of excisable goods or determine the rate of duty applicable thereto, they may request the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise, as the case may be, indicating:

(i) Specific grounds and reasons and the documents or information's, for want of which final assessment cannot be made.

(ii) Period for which provisional assessment is required.

(iii) The rate of duty or the value or both, as the case may be, proposed to be applied by the assessee, for Provisional Assessment.

(iv) The assessee undertakes to appear before the Assistant Commissioner or Deputy Commissioner of Central Excise within 7 days or such date fixed by him, and furnish all relevant information and documents within the time specified by the Assistant or Deputy Commissioner of Central Excise in his order, so as to enable the proper officer to finalize the provisional assessment.

(b) Order

On receipt of the request, the Deputy/Assistant Commissioner of Central Excise will examine it, if necessary, in consultation with the concerned Range Officer, to ascertain whether provisional assessment is necessary at all.

(i) Order rejecting provisional assessment : If the reasons/ grounds are not sufficient, he may ask the assessee to appear before him on an appointed day and time, and if he is satisfied that provisional assessment is not necessary, he may pass a reasoned order rejecting the same and also ordering the rate of duty or the value, to be applied by the assessee.

(ii) Order directing provisional assessment: Where the Deputy/Assistant Commissioner of Central Excise is satisfied with the genuineness of the assessee's request he will issue a specific order directing provisional assessment clearly stating:-

- The grounds on which provisional assessment has been ordered.
- The rate and for value, as the case may be, at which duty has to be provisionally paid.
- The amount of differential duty for which bond is to be executed covering the period, if any, during which assessee paid duty provisionally under the deeming provisions, after applying the rate and or value specified in (b) above.
- The amount of security or surety as may be fixed by Assistant Commissioner keeping in view the instructions issued by the Board from time to time.

(c) Furnishing of bonds

As mentioned earlier, provisional payment of duty is allowed if the assessee executes a bond in the prescribed form with such surety or security in such amount as the Assistant Deputy Commissioner may order. Such bond shall bind the assessee for payment of the difference between the amount of duty finally assessed and the amount of duty paid provisionally.

Though it is incumbent upon the assessee to ensure that the bond amount and corresponding securities are sufficient, the Divisional as well as the Range Officer will also keep a strict vigil on such cases with the help of 'Provisional Assessment Register'.

The Assistant/Deputy Commissioner of Central Excise will be held responsible to ensure that bonds for proper amount i.e., 3 times of the estimated differential duty are taken, in case of general bonds and that these are backed by proper (25%) security/ bank guarantee of the bond amount.

(d) Finalization of Assessment

Finalisation of provisional assessment means finalisation of an issue/ ground and thereafter finalization of each E.R.1s.

Final Assessment order may be passed by the Assistant Commissioner of Central Excise or the Deputy Commissioner of Central Excise after the relevant information required for finalizing the assessment is available. The amount of duty finalized will be communicated to the assessee at the earliest.

(d) Time limit for passing the order

Normally, final order should be passed within 6 months from the date of Provisional Assessment is available. Time limit may be extended by another 6 months by the Principal Commissioner or Commissioner of Central Excise. And it can be extended for any period by the Chief Principal Commissioner or Chief Commissioner of Central Excise.

(e) Interest payable on differential amount

The amount of each differential duty shall be paid along with interest @ 18% under section 11AA of the Act from the first day of the month succeeding the month for which such amount is determined, till the date of payment thereof.

Note:

(i) In the event the assessee is in a position to ascertain the duty himself, he may pay the duty on his own at the earliest and in that case, he will not have to incur interest on account of time taken by the Department to finalise assessment and communicate the amount.

(ii) As per the general law, the provisions of provisional assessment relating to interest clause and statutory time limit can only be prospective. Therefore, the provisions of interest and statutory time limit shall be applicable only to those cases of provisional assessment, which are ordered on or after 1st July, 2001.

(f) Refund after finalization of assessment

(i) **Refund order -** Where any refund becomes due to the assessee, order shall be passed for such refund, but disbursement shall be subject to further verification about incidence of such duty.

(ii) **Refund subject to provision of unjust enrichment -** The assessee will be required to submit proof to the Assistant/ Deputy Commissioner of Central Excise that the duty incidence was borne by him (assessee). If the assessee fails to produce such proof/evidence, the Assistant/ Deputy Commissioner of Central Excise will pass an order for depositing the amount in Consumer Welfare Fund in the prescribed manner.

(iii) **Interest payable on refund -** Otherwise, the refund shall be given along with interest under section 11BB of the Act from the first day of the month succeeding the month for which such refund is determined, till the date of refund.

(g) Department, suo motu, cannot issue directions for provisional assessment

It is important to note that rule 7 of the said Rules does not provide for the Department, suo motu, issuing directions for resorting to provisional assessment. Therefore, when the Central Excise Officers, during scrutiny or otherwise, find that self-assessment is not in order the assessee may be asked for all necessary documents, records or other information for issue of duty demand for differential duty, if any, after conducting inquiry. Where the assessee fails to provide the records or information and Department is unable to issue demand, 'Best Judgement' method may be used to raise demand based on collateral evidences. The burden will be on the assessee to provide information for appropriate re-determination of duty, if any.

2.17.5 Payment of Duty under Protest

Sometimes it happens that the classification of goods done by excise authorities, Assessable Value determined by the excise authorities in adjudication proceedings, etc. are not agreeable or acceptable to the assessee. In such cases, the assessee can file an appeal and in the meanwhile he can pay duty under protest (If no stay is obtained from Appellate Authorities).

2.17.6 Budget and Central Excise

Every year, taxation proposals are introduced at the time of annual budget which is presented usually on last day of February every year, by way of a Finance Bill. Major changes in excise, customs and service tax duties are announced on budget day.

Increased rates become effective immediately - Normally, any provision of legislation, takes effect only after it is passed by the Parliament and assented by President. However, in case of excise and customs provisions, this might create complications.

Provisional Collection of Taxes Act - Section 4 of 'Provisional Collection of Taxes Act, 1931' provides that budget provisions in respect of imposition or increase in duty of excise and customs will take effect immediately if a declaration is inserted in the Bill that it is expedient in Public interest to have immediate effect to the provisions of the Bill.

This provision is not applicable for reduction in duty.

Once this declaration is given, the new rates become effective on the expiry of the day when the bill is introduced. Accordingly, every year, the declaration is given and budget provisions come into effect immediately. Such declaration is valid only for 75 days or the date when the Finance Bill is passed, whichever is earlier.

Thus, if budget is presented on last day of February [28 or 29 as the case may be], new rates will become effective on 1st March itself.

If rates are reduced when the bill is passed, refund will be granted of excess duty collected [subject to provisions of refund of Unjust Enrichment of section 11B(2) of CEA].

2.17.7 Duty liability of Pre-budget Stock

Some goods in stock on the budget day are cleared subsequent to presentation of budget. The rate applicable at the time of clearance from the factory will be applicable for payment of excise duty.

2.18 PROCEDURAL ASPECTS UNDER CENTRAL EXCISE DUTY

2.18.1 Registration Under Central Excise Law

A manufacturer has to compulsorily get registered under the central excise law if he manufactures dutiable goods.

The following persons are also required to get registered under central excise law:

i. First Stage Dealer,

ii. Second Stage Dealer,

iii. Importer

iv. Person who stores dutiable goods in the specified area or in a warehouse before exports.

v. Manufacturers liable to pay excise duty @1% or 2% as the case may be

First Stage Dealer: Rule 2(ij) of CENVAT Credit Rules defines first stage dealer to mean a person who purchases directly from manufacturer or depot of the said manufacturer or consignment agent of the said manufacturer or any other place from where goods are sold by or on behalf of the said manufacturer under cover of excise invoice and includes purchases from importer or consignment agent of the importer or depot of the said importer under an invoice.

First stage dealer shall also includes an importer who sells goods imported by him under the cover of an invoice on which CENVAT credit may be taken and such invoice shall include an invoice issued from his depot or the premises of his consignment agent. [w.e.f. 1-3-2014]

The concept of dealer has been introduced under Central Excise merely to enable a buyer to avail the CENVAT credit when the goods are bought from a person other than the manufacturer. Here the dealer can pass on the CENVAT credit of the excise duty paid on the goods by the manufacturer, to his buyer. If a person is registered as dealer then he shall pass on credit which is equal to the amount of duty per unit of the goods in question, paid by the manufacturer at the time of clearance. The dealer does not pay any duty from his pocket as there is no processing or value addition at his end and he only enjoys a margin on his cost. However his margin on sales can be arrived at by calculating backwards.

Second Stage Dealer means a dealer who purchases goods from a first stage dealer. Dealer of any subsequent stage after second stage cannot issue Cenvatable Invoice.

The following manufacturers are exempt from registration and consequently payment of excise duty:

i. Manufacturer of dutiable goods who claims exemption under SSI notification Manufacturer in a unit of 100% Export Oriented Units (EOUs) and Software Technology Park are exempted from the registration provided they do not procure and sell the goods in the Domestic Tariff Area (DTA).

ii. Dealers

2.18.2 Exemption from Registration

- Persons who manufacture the excisable goods, which are chargeable to nil rate of excise duty or are fully exempt from duty by a notification;
- Small scale units availing the exemption based on value of clearances under a notification. However, such units will be required to give a declaration once the value of their clearances crosses ₹ 90 lakhs for a financial year;
- Persons manufacturing excisable goods by following the warehousing procedure under the Customs Act, 1962 subject to certain conditions;
- The person who carries on wholesale trade or deals in excisable goods (except first and second stage dealer, as defined in Cenvat Credit Rules, 2004);
- Persons who use excisable goods for any purpose other than for processing or manufacture of goods availing benefit of concessional duty exemption notification. (Notification 36/2001-C.E. (N.T.), dated 26-6-2001)

2.18.3 Procedure for Obtaining Central Excise Registration

i. Fill up Form A-1 in full and have it duly signed. If the applicant is a manufacturer/producer/ dealer/ warehouse incharge/importer.

ii. Submit copy of PAN card issued by the Income Tax Department.

iii. The Inspector in the office of Assistant Commissioner/Deputy Commissioner will scrutinize the A-1 form and if found in order it shall be fed into computer through System for Allotment of Central Excise Registration (SACER).

iv. A 15 digit PAN based registration number (ECC) will be allotted to the assessee on the spot; otherwise the same will be delivered to him within the next working day.

v. Registration under Central Excise can be granted in the name of minor, provided a legal guardian undertakes to conduct the business.

vi. Normally separate registrations are required if factories are located in different locations. Similarly if the warehouse is at a significant distance from the factory these must be registered separately. A single registration can be allowed by the Principal Commissioner or Commissioner of Central Excise for factories located in adjoining premises, or premises separated by road; railway, etc can if the facts and circumstance facilitates to do so.

Example 50: A manufacturer has place of business in the Factory in one location and in the warehouse at another location. If these locations are bifurcated by road, railway etc., then with the permission of Principal Commissioner or Commissioner of Central Excise the assessee can avail a single registration for these two locations. Otherwise each location has to be registered separately. In that case each factory of the manufacturer is considered a separate registration.

Centralized registration: Every mine engaged in the production/manufacture of specified goods is exempt from obtaining registration where the producer/manufacturer of such goods has a centralized billing/accounting system in respect of such goods produced by different mines and opts for registering only the premises or office from where such centralized billing or accounting is done (Notification No. 10/2011-CE dt. 24-3-2011).

vii. If the assessee ceases to carry on operations for which he is registered his registration certificate can be cancelled. This is called de-registration.

Sometimes registration certificate can also be revoked by registering authority. Registration certificate can be revoked in the following cases.

(a) If the manufacturer manufactures prevented goods. (like arms, explosive devise without license).

(b) Manufacturer carries higher risk (evasion of duty continuously, repeatedly producing the malafide evidences etc).

2.18.4 Provisions Relating to Non Registration

As per Rule 25 of the Central Excise Rules, 2002, where registration under Central Excise is required for a manufacturer but not registered then, all such goods shall be liable to confiscation. Such manufacturer is supposed to face the punishment and penalty. This provision also applies to an importer who issues an invoice on which Cenvat Credit can be taken (w.e.f. 1.3.2015).

Punishment: (Section 9 of the Central Excise Act, 1944)

i. if the duty leviable on the excisable goods exceeds ₹ 50,00,000 (w.e.f. 28-5-2012)

(a) imprisonment upto seven years and fine without any upper limit.

(b) 6 months minimum imprisonment unless there are special and adequate reasons for granting lesser punishment.

ii. if the duty leviable on the excisable goods is less than or equal to ₹ 50,00,000 (w.e.f 28-5-2012)

(a) Imprisonment upto three years or fine or both can be imposed

(b) 6 months minimum imprisonment unless there are special and adequate reasons for granting lesser punishment

Section 9A is being amended to make an offence cognizable and non-bailable where the duty liability exceeds ₹50 lakhs and punishable under clauses (b) or clause (bbbb) of Sub-section (1) of Section 9.

Penalty for Non-Registration

The penalty for non-registration is amount of duty of contravening goods or ₹ 2,000 whichever is higher. [Rule 25(1)(c) of the Central Excise Rules]

2.18.5 Daily Stock Account (DSA)

Every assessee registered under Central Excise should maintain the Daily Stock Account (DSA) [Rule 10(1) of Central Excise Rules, 2002]

There is no specific format for Daily Stock Account. The following information should be captured in the DSA:

i. Description of goods manufactured
ii. Opening balance of goods manufactured
iii. Quantity manufactured
iv, Inventory of goods (closing stock)
v. Goods removed from the place of removal (quantity)
vi. Assessable value of goods removed
vii. Amount of duty payable to the department
viii. Particulars with regard to the amount of duty actually paid.

The first page and the last page of the DSA shall be duly authenticated by the manufacturer or his authorized person. The DSA shall be preserved for five years immediately after the financial year to which such records pertain.

The records under this rule may be preserved in electronic form and every page of the record so preserved shall be authenticated by means of a digital signature. The Board may, by notification, specify the conditions, safeguards and procedure to be followed by an assessee preserving digitally signed records.

Penalty upto the amount of duty payable can be imposed and the offending goods can be confiscated if DSA is not maintained by the manufacturer. [Rule 25(1)(b) of Central Excise Rules]

2.19 REFUND & OTHER IMPORTANT PROVISIONS

Other important provisions are summarized below.

2.19.1 Refund of Excise Duty

i. Assessee can claim refund of duty before the expiry of one year from relevant date u/s 11B, in form R.
ii. Refund is subject to doctrine of unjust enrichment, i.e. refund will be available only if the amount was not recovered from buyer. These are overriding provisions.
iii. Doctrine of unjust enrichment applies to captive consumption, provisional assessment and also when duty was paid under protest.
iv. If refund is delayed beyond three months, interest is payable @ 6% p.a.

2.19.2 Exemption from Duty

Goods exported under bond are not 'Exempted Goods'

Rule 19(1) of Central Excise Rules states that any Excisable goods may be exported without payment of duty from factory of producer or manufacturer, as may be approved by the Commissioner or notified by the board. Thus, the goods are cleared 'without payment of duty'. They are not 'exempt' goods. Ministry of Law Advice dated 29.10.1974 – confirmed and circulated vide CBE&C circular No. 278/112/96-CX dated 11.12.1996, states as follows, 'Under Central Excise, 'exemption' means exemption by notification under section 5A of CEA [earlier rule 8]. Thus, goods exported under bond are not 'exempt' from duty. These goods also cannot be termed as 'chargeable to Nil rate of duty', as in fact, the goods are dutiable.

i. Section 5A(1) of Central Excise Act and section 25(1) of Customs Act empower Central government to exempt any excisable goods from duty, by issuing notification in Official Gazette.

ii. Such exemption may be partial or full, conditional or unconditional.

iii. Absolute i.e. unconditional exemption is compulsory, while conditional notification is at option of assessee.

iv. Central Government can also grant exemptions in exceptional cases u/s 5A(2).

v. An exemption notification should be strictly construed, but purposeful construction is permissible.

vi. Principle of promissory estoppel can apply to an exemption notification.

2.19.3 Remission of Duty for Goods Lost, Destroyed or unfit for Consumption or Marketing

i. Rule 21 of the Central Excise Rules, 2002 provides for remission of duty if the assessee can prove to the satisfaction of the Principal Commissioner or Commissioner of Central Excise that the goods have been lost or destroyed by natural cause or by unavoidable accident or the manufacturer claims them as unfit for consumption or for marketing, before their clearance. In such cases Principal Commissioner or Commissioner can remit the duty on such goods subject to such conditions as may be imposed by him or ordered in writing. Power of remission given to various officers have been increased in 2007. The assessee should apply for destruction and remission in duplicate. Credit taken for inputs of the goods so lost or destroyed need not be reversed as such loss cannot be equated to exemption to goods - 2007 (208) E.L.T. 336 (Tri.-LB) - *Grasim Industries* v. *CCE*. But as per new sub-rule (5C) of Rule 3 of Cenvat Credit Rules, 2004, such credit on input requires reversal. No remission is allowable if goods are lost due to theft or dacoity - 2008 (232) E.L.T. 796 (Tri.-LB) - *Gupta Metal Sheets* v. *CCE*.

ii. But no remission of duty is grantable for any loss or destruction or deterioration of any goods taking place after the goods have been cleared for home consumption on payment of duty or in cases of theft.

iii. For duty upto ₹ 10,000, Superintendent of Central Excise has been empowered to grant remission. Deputy /Assistant Commissioner can grant remission of duty exceeding ₹ 10,000 and upto ₹ 1 lakh. Additional/Joint Commissioner will have the power to remit duty exceeding ₹ 1 lakh and upto ₹ 5 lakhs. No limit has been prescribed for Principal Commissioner or Commissioner in this regard.

iv. Remissions have to be claimed by the assessee and the burden to furnish adequate evidence of loss is on the assessee. Remission when granted is subject to conditions as may reasonably be imposed by the officer, such as irretrievable destruction under official supervision of goods claimed to be unfit for consumption or for marketing.

2.19.4 Compounded Levy Schemes

i. As per Rule 15, the Central Government may by notification specify the goods in respect of which the assessee shall have the option to pay excise duty on the basis of such factors as may be relevant to production of such goods and at such rate as may be notified in this respect. The Central Government has, therefore, notified the *Compounded Levy Scheme for Stainless Steel pattis/pattas, aluminium circles, subject* to *the process of cold rolling. - Notification No. 17/2007-C.E., dated 1-3 -2007*. These units have to pay Education Cess and SHE Cess also over and above the compounded levy rates as per C.B.E. & c. Letter F. No. 27/16/2008-CX.1, dated 25-8-2008 [2008 (230) E.L.T. T19].

ii. Section 3A has been inserted by Finance Act, 2008, empowering the Central Government to charge excise duty on the basis of capacity of production in respect of notified goods and to notify the procedure for the same. Accordingly, pan masala and pan masala containing tobacco commonly known as gutkha manufactured with the aid of packing machine and packed in pouches have been notified for this purpose with effect from 1-7-2008. Pan masala with betel nut content not exceeding 15% is not covered. Detailed procedures and other matters like filing of specified declaration/intimation, payment of duty at notified rates, abatement in case of non-production, requirement of declaration of retail sale price on packages, bar on Cenvat credit availment, addition or removal of packing machines, penalty and confiscation for contravention and the like are provided in Pan Masala Packing Machines (Capacity Determination And Collection of Duty) Rules, 2008.

New procedure for End-Use Exemption (erstwhile Chapter X procedure) - A new procedure for End-Use Exemption has been notified in Central Excise (Removal of Goods at Concessional Rate of Duty for Manufacture of Excisable Goods) Rules, 2001.

The new Rules contemplate that procurement of goods for end-use under concessional (including fully exemted) rate of duty.

iii. Goods received duty free can be removed to another eligible manufacturer under the new end-use exemption procedure. Principal Commissioner or Commissioner can also allow sending goods outside the factory for test, repair, reconditioning etc. and return thereof under their supplemental instruction power under Central Excise Rule 31.

2.19.5 Removal of Goods from FTZ, EOU and SEZ to Domestic Tariff Area

i. As per Rule 17 of the Central Excise Rules, 2002, removal of goods from FTZ and EOU to the domestic tariff area shall be made under an invoice and on payment of appropriate duty by 5th of the following month except March, like other units in DTA. Such unit shall maintain proper account relating to production, description of goods, quantity removed, duty paid and each removal made on an invoice. Unit shall also submit a monthly Return to the Superintendent, Central Excise within ten days from the close of the month to which the return relates. The Return shall be submitted in form ER-2.

ii. For the period prior to 11-5-2001 when Section 3 of the Act was amended to substitute the words "allowed to be sold" with the words "brought to any other place", clearances from EOUs if not allowed to be sold into India shall continue to be chargeable to duty under main Section 3(1) of Central Excise Act, 1944 as such units are also situated in India.

iii. SEZ having been given the status of foreign territory, imports there from to DTA will be governed by the provisions of the Special Economic Zones Act, 2005. Removal of semi-finished goods or finished goods for further processing, or testing has been permitted under Rules 16B and 16C, broadly on the pattern of old Rule 56B.

2.19.6 Return of Duty paid Goods for Repairs etc. - Credit of Duty

i. As per Rule 16 of the Central Excise Rules, 2002 where any duty paid goods (whether originally manufactured in the same or another factory) are subsequently returned to the factory for being remade, refined, reconditioned or for any other reason, the assessee shall record the particulars of such returned goods in his record and take Cenvat Credit of the duty paid on such goods as if they are inputs and shall utilize this credit according to the Cenvat Credit Rules, 2004. But the goods received must be eventually returned.

ii. When the process to which the returned goods are subjected, does not amount to manufacture, the assessee shall pay the amount equal to Cenvat credit taken in respect to such returned goods. In other cases the returned goods after processing shall be removed on payment of duty according to the value and rate of duty applicable as on the date of removal.

iii. As per sub-rule (3) of Rule 16, where it is difficult to follow the provisions of sub-rule (1) and sub-rule (2) of Rule 16, the assessee can receive the goods subject to such conditions as may be specified by the Principal Commissioner or Commissioner of Central Excise. Thus, in case where it is not possible to know the amount of the duty paid on returned goods as they may have been removed originally long back and the original invoice may not be available, in such or similar cases the return of goods shall be subject to the general or specific orders of the Principal Commissioner or Commissioner of Central Excise and there will be no credit and no payment of duty.

iv. According to one school of thought, under the Rules there are now no restrictions on return, re-entry, retention and re-issue of duty paid goods if no credit is desired and taken. But presence of the retuned goods in the factory may cause accounting and surprise stock checking problems unless the returned goods are clearly identifiable as such and are stored and accounted for (in private accounts) separately It has been held that restrictions for re-entry apply only to identical or similar to those manufactured in the factory and not to other goods - 2004 (168) E.L.T. 53 (Tri.) - *Varsha Engineering* v. *C.C.E.*

2.19.7 Removal of Excisable Goods on Payment of Duty

i. As per Rule 4, no excisable goods on which duty is payable shall be removed without payment of duty from any place where they have been produced, manufactured or warehoused, unless otherwise provided. Duty, however is payable as specified in Rule 8.

ii. As per Rule 4(2), where molasses are produced in a khandsari sugar fatory, the person who procures such molasses, whether directly from such factory or otherwise, for use in the manufacture of any commodity (whether or not excisable) shall pay the duty payable on such molasses as if it is produced by him.

iii. By virtue of Rule 12AA excise duty can be paid either by the principle jewellery manufacturer or by his job worker.

iv. Full amount collected from the customer by way of duty should be shown distinctly in the invoice and paid to the credit of the Government.

2.19.8 Storage of Non-Duty paid goods outside the Factory

As per Rule 4(4) of the Central Excise Rules, 2002, the storage of non-duty paid goods outside the factory can be permitted by the Principal Commissioner or Commissioner of Central Excise subject to such safeguards as he may specify. Such storage outside the factory premises is permissible in exceptional circumstances having regard to the nature of the goods and shortage of storage space in the factory. No merchant overtime charges would be recovered for supervision over such storage.

2.19.9 Manner of Payment of Duty Monthly

(i) Rule 8 provides the manner of payment of duty. 'Duty' for this purpose includes the 'amount' payable in terms of the Cenvat Credit Rules, 2004. This rule allows payment of duty on monthly basis by 6th day of the succeeding month by e-payment through internet banking except for the month of March when duty is to be paid by 31st March.

Provided that the Assistant Commissioner or Deputy Commissioner of Central Excise for reasons to be recorded in writing allow an assessee payment of duty by any mode other than internet bank.

(ii) The buyers of the goods cleared by manufacturers would be allowed to avail credit in respect of the duty payable on such goods immediately on receipt of the goods by them.

(iii) Every assessee shall electronically pay duty through internet banking.

Provided that the Assistant Commissioner or the Deputy Commissioner of Central Excise, for reason to be recorded in writing, allow an asessee payment of duty by any mode other than internet banking.

2.19.10 Action in Case of Default

As per Rules 8(3) of Central Excise Rules, 2002 if the assessee fails to pay the amount of duty by the due date, he shall be liable to pay the outstanding amount along with interest @ 18% under section 11AA of the Act on the outstanding amount, for the period starting with the first day after due date till the date of actual payment of the outstanding amount.

As per Rule 8(3A), if the assessee fails to pay the duty declared as payable by him in the return within a period of 1 month from the due date, then the assessee is liable to pay the penalty at the rate of 1% on such amount of the duty not paid, for each month or part thereof calculated from the due date, for the period during which such failure continues.

2.20 OTHER PROCEDURES IN CENTRAL EXCISE

Some procedures are basic, which every assessee is required to follow. Besides, some procedures are required to be followed as and when required.

Basic Procedures

(i) Every person who produces or manufactures excisable goods, is required to get registered, unless exempted. [Rule 9 of Central Excise Rules]. If there is any change in information supplied in Form A-1, the same should be supplied in Form A-1.

(ii) Manufacturer is required to maintain Daily Stock Account (DSA) of goods manufactured, cleared and in stock. [Rule 10 of Central Excise Rules]

(iii) Goods must be cleared under invoice of assessee, duly authenticated by the owner or his authorised agent. In case of cigarettes, invoice should be countersigned by Excise officer. [Rule 11 of Central Excise Rules]

(iv) Duty is payable on monthly basis through e-payment by 6th of following month, except in March. Assessee paying duty by any mode other than internet Banking within 5th of following month.

Excise Duty Due Date w.e.f. 1.4.2010 by SSI units: (Notification No. 05/2010-CE (N.T.) dated 27.02.2010)

Frequency –Quarterly (other than e-pay)

April – December	5th of the following month from the end of the relevant quarter
January – March	31st March itself.

Frequency –Quarterly (e-pay)

April – December	6th of the following month from the end of the relevant quarter
January – March	31st March itself.

(v) Monthly return in form ER-1 should be filed by 10th of following month. SSI units have to file quarterly return in form ER-3. [Rule 12 of Central Excise Rules] — EOU/STP units to file monthly return in form ER-2 – see rule 1 7(3) of CE Rules.

(vi) Assessees paying duty of ₹ 1 crore or more per annum through PLA are required to submit Annual Financial Information Statement for each financial year by 30th November of succeeding year in prescribed form ER-4 [Rule 12(2) of Central Excise Rules].

(vii) Specified assessees are required to submit Information relating to Principal Inputs every year before 30th April in form ER-5, to Superintendent of Central Excise. Return for 2004-05 was required to be submitted by 31-12-2004 [rule 9A(1) to Cenvat Credit rules inserted w.e.f. 25-11-2004]. Any alteration in principal inputs is also required to be submitted to Superintendent of Central Excise in form ER-5 within 15 days [rule 9A(2) to Cenvat Credit Rules inserted w.e.f. 25-11-2004]. Only assessees manufacturing goods under specified tariff heading are required to submit the return. The specified tariff headings are – 22, 28 to 30, 32, 34, 38 to 40, 48, 72 to 74, 76, 84, 85, 87, 90 and 94; 54.02, 54.03, 55.01, 55.02, 55.03, 55.04. Even in case of assessees manufacturing those products, only assessees paying duty of ₹ 1 crore or more through PLA (current account) are required to submit the return.

(viii) Assessee who is required to submit ER-5 is also required to submit monthly return of receipt and consumption of each of Principal Inputs in form ER-6 to Superintendent of Central Excise by tenth of following month [rule 9A(3) to Cenvat Credit rules inserted w.e.f. 25-11-2004]. *Only those assessees who are required to submit ER-5 return are required to submit ER-6 return.*

(ix) Every assessee is required to submit a list in duplicate of records maintained in respect of transactions of receipt, purchase, sales or delivery of goods including inputs and capital goods, input services and financial records and statements including trial balance [Rule 22(2)].

(x) Inform change in boundary of premises, address, name of authorised person, change in name of partners, directors or Managing Director in form A-1.

These are core procedures which each assessee has to follow.

2.20.1 Periodic Returns under Central Excise

Mandatory e-filing of Central Excise Returns in ACES w.e.f. 1-10-2011 (vide CBEC Circular No.955/16/2011 - CX dt. 15-9-2011). It means all assesses are required to file returns mandatorily through e-filing, irrespective of the payment of excise duty. Penalty for delayed submission of return can extend upto ₹ 5,000 and with confiscation of the goods in respect of which the offence is committed. [Rule 27 of Central Excise Rules]

Form of return	Description	Assessee	Time Limit
ER-1	Monthly	Manufacturer	10th of the following month from the end of the relevant month.
ER-2	Monthly	EOU	10th of the following month from the end of the relevant month.
ER-3	Quarterly	SSI	10th of the following month from the end of relevant quarter w.e.f. 1.4.2010
Annexure 13B	Quarterly	First Stage Dealer (or) Second Stage Dealer	15th of the following month from the end of the relevant quarter.
ER-4	Annual Financial Information Statement (AFI)	Duty paid including CENVAT Credit ₹ 100 lakhs in the previous year.	Annually by 30th November of next year.
ER-5	Information relating to principal inputs statement	Duty paid including CENVAT Credit ₹ 100 lakhs in the previous year.	Annually by 30th April for the current year.
ER-6	monthly input and output	ER-5	10th of the following month from the end of the relevant month.
ER-7	Annual Installed Capacity Statement	by every assessee*	30th April of the succeeding Financial Year
ER-8	Quarterly	An assessee is availing the exemption under N.T. 1/2011 dt. 1-3-2011 namely paying duty @1% or 2% as the case may be and does not manufacture any other products.	10th of the following month from the end of relevant quarter. For the year end quarter 31st March.

Exempted from filing Annual Installed Capacity Statement (i.e. ER-7)

The following manufacturers are exempted from filing Annual Installed Capacity Statement, vide Notification No. 26/2009-CE-(NT), dated 18.11.2009, namely:

- biris manufactured without the aid of machines falling under tariff item 2403 10 31.
- matches manufactured without the aid of power falling under heading 3605.
- reinforced cement concrete pipes falling under heading 6810.

The Following Assessees are Exempted From E-Filing (Nt 21 & 22/2011 W.E.F. 1.10.2011:

(a) Exempted goods are cleared from the state of Uttaranchal or Himachal Pradesh

(b) Units located in the Industrial Growth Centre or

(c) Industrial development centre

(d) Industrial Infrastructure Development centre

(e) Export promotion industrial park

2.20.2 Automation of Central Excise and Service Tax (ACES)

The Central Board of Excise & Customs (CBE & C) has developed a new software application called ***Automation of Central Excise and Service Tax (ACES),*** which aims at improving tax-payer services, transparency, accountability and efficiency in indirect tax administration.

It is a centralized, web based software application which automates various processes of Central Excise and Service Tax for Assessees and Department, and gives complete end to end solution. Any Assessee can register with Department using ACES application, can file tax return, claims & intimations, track its status and get online messages.

Benefits to the Assessees

i. Reduce Physical Interface with the Department

ii. Save Time

iii. Reduce Paper Work

iv. Online Registration and Amendment of Registration Details

v. Electronic filing of all documents such as applications for registration, returns [On-line and off-line downloadable versions of ER 1, 2, 3, 4, 5, 6, Dealer Return, and ST3], claims, permissions and intimations; provisional assessment request, export-related documents, refund request

vi. System-generated e-acknowledgement

vii. Online tracking of the status of selected documents

viii. Online view facility to see selected documents

ix. Internal messaging system on business-related matters

Salient features of ACES homepage

i. ACES homepage is an interface for users/Assesses to access the Central Excise and Service Tax applications.

ii. The website also enables users to make online payment through e-payment option, download the Returns offline utilities through Download option.

iii. The website also keeps track on latest updates of the ACES application and gives links to various other sites under CBEC.

Certified Facilitation Centre (CFC)

CFC stand for Certified Facilitation Centre under ACES project of CBEC and is an e-facility, which may be set-up and operated by a Cost Accountant/Chartered Accountant/Company Secretary or a proprietary concern/firm of Cost Accountants or Chartered Accountants or Company Secretaries in practice to whom a certificate is issued under the ACES project, where the assessees of Central Excise and Service Tax can avail this facility to file their returns and other documents electronically along with associated facilitation on payment of specified fees.

2.20.3 There are other Procedures Which are not Routine

Non-core procedures - The non-core procedures are as follows: -

(a) Export without payment of duty or under claim of rebate [Rules 18 and 19 of Central Excise Rules].

(b) Receipt of goods for repairs / reconditioning [Rule 16 of Central Excise Rules].

(c) Receipt of Goods at concessional rate of duty for manufacture of Excisable Goods.

(d) Payment of duty under Compounded Levy Scheme.

(e) Provisional Assessment [Rule 7 of Central Excise Rules].

(f) Warehousing of goods.

(g) Appeals and settlement.

2.20.4 Invoice for Removal of Final Products

Rule 11(1) of Central Excise Rules provides that excisable goods can be removed from factory or warehouse only under an 'Invoice' signed by owner or his authorised agent. In case of cigarettes, invoice shall be counter-signed by Inspector. Invoice should bear serial number and should be in triplicate. As per Rule 11(2) of Central Excise Rules, Invoice shall contain –

(a) Registration Number,

(b) Address of jurisdictional Central Excise Division,

(c) Name of consignee,

(d) Description and classification of goods,

(e) Time and date of removal,

(f) Mode of transport and vehicle registration number,

(g) Rate of duty,

(h) Quantity and Value of goods,

(i) Duty payable on the goods.

2.20.5 Export Procedures

Exports are free from taxes and duties.

i. Goods can be exported without payment of excise duty under bond under rule 19 or under claim of rebate of duty under rule 18.

ii. Excisable Goods should be exported under cover of Invoice and ARE-1 form.

iii. Merchant exporter has to execute a bond and issue CT-1 so that goods can be cleared without payment of duty. Manufacturer has to issue Letter of Undertaking.

iv. Export to Nepal/Bhutan are required to be made on payment of excise duty.

v. EOU has to issue CT-3 certificate for obtaining inputs without payment of excise duty.

Bringing goods for repairs, re-making etc.

i. Duty paid goods can be brought in factory for being re-made, refined, reconditioned or for any other reason under rule 16.

ii. The goods need not have been manufactured by assessee himself.

iii. Cenvat credit of duty paid on such goods can be taken, on basis of duty paying documents of such goods.

iv. After processing/repairs, if the process amounts to 'manufacture', excise duty based on assessable value is payable.

v. If process does not amount to manufacture, an 'amount' equal to Cenvat credit availed should be paid [rule 16(2)].

vi. If some self manufactured components are used, duty will have to be paid on such components

vii. Buyer/recipient of such goods can avail Cenvat credit of such amount/duty.

viii. If the above procedure cannot be followed, permission of Principal Commissioner or Commissioner is required [rule 16(3)].

2.20.6 Receipt of Goods at Concessional Rate of Duty

Some users of excisable goods can obtain goods at nil or lower rate of duty, subject to certain conditions. In other words, the exemption is based on end use. If the buyer is entitled to obtain excisable goods at nil or concessional rate of duty, he is required to follow prescribed procedure. The provisions are contained in Central Excise (Removal of Goods at Concessional Rate for Manufacture of Excisable Goods) Rules, 2001.

Payment of Duty through Personal Ledger Account (PLA)

The Personal Ledger Account (PLA) is a running account through which the manufacturer can avail the credit the excise duty credit, pay the shortfall, if any, or carry forward the surplus if any.

In order to open a new Personal Ledger Account, the manufacturer, quoting his registration number, shall obtain the New Excise control Code Number (New ECC Number), which is a Permanent Acccount Number (PAN). Once the department adopts 'common number' for registration and accounts, separate ECC number shall not be required.

The manufacturer working under the procedure shall maintain an account current (Personal Ledger Account) in the Form specified in Annexure-8.

Each credit and debit entry should be made on separate lines and assigned a running serial number for the financial year. The PLA is credited when duty is deposited in the bank by GAR- 7 challan. The PLA is debited with the duty required to be paid on manufacture of goods on monthly basis. PLA and CENVAT credit should be used only for payment of excise duty and not other payments like fines, penalties etc.

The PLA must be prepared in triplicate by writing with indelible pencil and using double-sided carbon-original. Duplicate copies of the PLA should be detached by the manufacturers and sent to the central Excise Officer in charge along with the monthly/ quarterly periodical return in form E.R 1 or E.R 3.

2.21 CENTRAL EXCISE AUDIT AND SPECIAL AUDIT UNDER SECTION 14A AND 14AA

Goods are removed by the assessee under a system of self-removal. Returns are filed by the assessee without verification by the Excise department. Hence there is a need for audit by the Excise department to protect the interests of the government i.e. to check that there are no revenue leakages. A series of audits under the Central Excise Law is contemplated.

2.21.1 Types of Audits

Three types of audit are contemplated under Central Excise Law.

(1) Central Excise Revenue Audit (known as CERA Audit) conducted by the office of the Comptroller and Auditor General of India. (C & AG)

(2) Internal audit conducted by the Excise Department (known as Excise Audit 2000)

(3) Special audit conducted by Cost Accountant/Chartered Accountant.

(1) Central Excise Revenue Audit

The key points relating to this audit are as under:

(i) Conducted by the Comptroller and Auditor General of India (C & A G) it is called Central Excise Revenue Audit (CERA).

(ii) This is an audit of the Central Excise Department's functioning and is carried out at the office of the Central Excise Department.

(iii) This is not an audit of the assessee.

(iv) The audit focuses on ascertaining revenue leakage and is assessed on the basis of the periodical returns filed by the assessee, the execution of various bonds, and other relevant information such as cost audit reports, and income-tax audit reports of the assessee.

(v) The CERA auditor has the right to visit the office of the assessee though the audit is not of the assessee.

(vi) There is no defined frequency for the carrying out of this audit.

(vii) C & A G submits the report to the President of India, who causes these to be laid before each House of Parliament.

(2) Special Audit u/s 14A of CEA

If at any stage of enquiry, investigation or any other proceedings before him, any Central Excise Officer not below the rank of an Assistant/Deputy Commissioner of Central Excise having regard to the nature and complexity of the case and the interest of revenue, is of the **opinion that the value has not been correctly declared or determined** by a manufacturer or any person, he may, with the previous approval of the Principal Chief Commissioner or Chief Commissioner of Central Excise, direct such manufacturer of such person to get the accounts of his factory, offices, depots, distributors or any other place, as may be specified by the said Central Excise officer, audited by a Cost/Chartered Accountant, nominated by the Principal Chief Commissioner or Chief Commissioner of Central Excise in this behalf. Cost Accountant shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959. Chartered Accountant shall have the meaning assigned to it in section 2(1) (b) of the Chartered Accountants Act, 1949.

The directions given by Assistant/Deputy Commissioner for special audit after obtaining prior approval of Principal Chief Commissioner or Chief Commissioner of Central Excise is not an appealable order in terms of section 35B. The Tribunal in the case of *Neelam Products Ltd. vs. CCE Delhi III* held that an opportunity for hearing is to be given to the assessee before the issuance of the direction for special audit. As the opportunity for hearing would help the authority to form an objective opinion on the complexity of the case based on prescribed factors.

The Cost Accountant/ Chartered Accountant, so nominated shall, within the period specified by the Central Excise Officer, submit a report of such audit duly signed and certified by him to the said Central Excise Officer mentioning therein such other particulars as may be specified :

Provided that the Central Excise Officer may, on an application made to him in this behalf by the manufacturer or the person and for any material and sufficient reason, extend the said period by such further period or periods as he thinks fit; so, however, that the aggregate of the period originally fixed and the period or periods so extended shall not, in any case, exceed one hundred and eighty days from the date on which the direction under sub-section (1) is received by the manufacturer or the person.

The manufacturer shall be given an opportunity of being heard in respect of any material gathered on the basis of audit and proposed to be utilized in any proceedings under the Central Excise Act or Rules. This special audit can be conducted notwithstanding that the accounts of the manufacturer or the person have been audited under any other law for the time being in force or otherwise.

The expenses of, and incidental to, such audit (including the remuneration of the Cost Accountant/ Chartered Accountant) shall be determined by the Principal Chief Commissioner or Chief Commissioner of Central Excise (which determination shall be final) and paid by the manufacturer or person and in default of such payment, shall be recoverable from the manufacturer or the person in the manner provided in section 11 for the recovery of sums due to the Government.

The Cost Accountant or the Chartered Accountant has to submit the duly signed and certified audit report within the period specified by the Central Excise Officer. He shall also mention in the report such other particulars as may be prescribed by such Central Excise Officer.

Advisory from The Institute of Cost Accountants of India

The members of the Institute are undertaking Valuation Audit under Section 14A of Central Excise Act,1944. The basic objective of the Section 14A is to ensure correct determination of value for the manufacture of excisable goods produced or manufactured for correct realisation of revenue.

Consequent upon the Supreme Court judgment in the case of Principal Commissioner or Commissioner of Central Excise, Mumbai Vs. M/s Fiat India (P) Ltd. & ANR. dated 29th August, 2012, it has been observed that greater responsibilities have been thrown on the shoulders of the Cost Accountants in Practice while undertaking Special Audit under Section 14A of the Central Excise Act, 1944.

The members of the Institute are hereby advised to take into consideration the Compliance Report and the Cost Audit Report, if the product is covered under the Cost Audit, to ensure the correct determination of the value and thus fair assessment of revenue by the Excise Department.

(3) Special Audit u/s 14AA (CENVAT Credit Audit)

Special Audit in Cases where Credit of Duty Availed or Utilised is not within the Normal Limits, etc.

(1) If the Principal Commissioner of Central Excise or Commissioner of Central Excise may call for an audit if he has reason to believe that the credit of duty availed of or utilized by a manufacturer of any excisable goods –

(a) is not within the normal limits having regard to the nature of the excisable goods produced or manufactured, the type of inputs used and other relevant factors, as he may deem appropriate;

(b) has been availed of or utilized by reason of fraud, collusion or any willful mis-statement or suppression of facts.

The Principal Commissioner or Commissioner shall direct such manufacturer to get the accounts of his factory, office, depot, distributor or any other place, as may be specified by him, audited by a Cost Accountant or Chartered Accountant nominated by him. Cost Accountant shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959. Chartered Accountant shall have the meaning assigned to it in section 2(1)(b) of the Chartered Accountants Act, 1949.

(2) The cost accountant so nominated shall, within the period specified by the Principal Chief Commissioner of Central Excises or Commissioner of Central Excise, submit a report of such audit duly signed and certified by him to the said Principal Commissioner or Commissioner mentioning therein such other particulars as may be specified.

(3) The provisions of sub-section (1) shall have effect notwithstanding that the accounts of the said manufacturer aforesaid have been audited under any other law for the time being in force or otherwise.

(4) The expenses of, and incidental to, such audit (including the remuneration of the cost accountant) shall be determined by the Principal Commissioner or Commissioner of Central Excise (which determination shall be final) and paid by the manufacturer and in default of such payment shall be recoverable from the manufacturer in the manner provided in section 11 for the recovery of sums due to the Government.

(5) The manufacturer shall be given an opportunity of being heard in respect of any material gathered on the basis of the audit under sub-section (1) and proposed to be utilized in any proceeding under this Act or rules made thereunder.

Explanation : For the purpose of this section, "cost accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959 (23 of 1959). 84]

Note: Finance Act 2009, amendment of Section 14A and 14AA, for the words "cost accountant,", the words "cost accountant or chartered accountant" shall be substituted.

Audit prescribed by Central Excise Department

The Central Excise Department also has evolved a system of departmental audit in view of the fact that all the statutory records to be maintained by the assessee have been abolished in year 2000/01.

History of provisions

In conventional sense, "audit" means scrutiny and verification of documents, events and processes in order to verify facts and, draw conclusions regarding the correctness of recording of facts and the efficiency of a system under study. For Central Excise purposes "audit" means scrutiny of the records of assessee and the verification of the actual process of receipt, storage, production and clearance of goods with a view to check whether the assessee is paying the central excise duty correctly and following the central excise procedures.

Under the conventional /traditional system of central excise audit, audit parties visit assessees unit without much preparation and verify all the statutory records (i.e. those prescribed under the Central Excise law) to check compliance of procedures and also leakage of revenue, if any. Experiences show that such audits do not result in detection of major aberrations. Most of the audit objections pertain to either minor procedural irregularity or duty short payment of small amounts mostly due to human error. Further, this method of auditing does not envisage checking of the internal records of the assessee as well as those records which are maintained by the assessee under the other laws like Income-tax Act, Sales Tax Act, Companies Act etc.

One of the announcements made during Budget 2000 as a measure of simplification of procedures, was the dispensation of all statutory records under the central excise law. No longer was the assessee required to record the receipt of raw material, production and clearance/sale of finished goods etc. in registers/documents prescribed by the central excise department. As a result, the assessees are now allowed to maintain all their records in whichever form they like (including maintenance of the entire records in electronic form) provided the essential information required for calculation of central excise duty liability can be obtained from such records. Under these circumstances it becomes necessary for the auditors to look into the assessees own (private) records to verify whether the assessee is paying central excise duty correctly and following the laid down procedures.

Another change brought in recent years is doing away the system of assessment of the returns by the departmental officers. Now the assessee is required to self assess his monthly tax returns (called the E.R.1/E.R.2) before filing the same with the department. The departmental officers only scrutinise this return to check for any apparent mistake made by the assessee. They are not required to carry out detailed verification. Therefore, the entire burden of checking whether the assessee actually paying his taxes correctly, now lies with audit.

The statutory changes resulting in dispensation of statutory records as well as self assessment of central excise duty by the assessee has led to the conventional/traditional system of audit becoming irrelevant.

(4) Excise Audit 2000

Excise Audit 2000 (EA 2000) is a new system of audit initiated from 1st December 1999. The essential philosophy of EA 2000 is that this audit is based on the scrutiny of business records of the assessee. This is a more systematic form of audit wherein the auditors are required to gather basic information about the assesee and analyze them to find out vulnerable areas before conducting the actual audit. The audit is therefore more focused and in-depth as compared to the traditional audit. Further, at every stage of audit, the assessee is consulted. This makes EA 2000 audit user friendly.

The frequency of conducting the Excise Audit 2000 is as follows:

Amount of Annual duty (In cash + CENVAT credit) Paid by assessee	**Frequency of Audit**
(i) Above ₹ 3 Crores	Every Year
(ii) Between ₹ 1 Crore and ₹ 3 Crores	Once every two years
(iii) Between ₹ 50 lakhs and ₹ 1 Crore	Once every five years
(iv) Less than ₹ 50 lakh	10% of the units audited every year

Procedure of Excise Audit 2000

(i) Selection of Assessee

The process of EA 2000 begins with identification of a unit to be audited. Normally, there are about 1000 to 1500 assessees under the jurisdiction of a Central Excise Commissionerate. It is not possible for the audit staff to conduct audits of all the units every year. Therefore, depending upon the manpower availability, about 300 to 400 units are selected for conducting audit during a financial year. Under the conventional system of audit the units were picked up randomly without any scientific basis of selection. Under EA 2000, the selection of the unit is based taking into account in the 'risk-factors'. This means that the assessees who have a bad track record (having past duty evasion cases, major audit objections, past duty dues etc.) are given priority for conducting audit over those having clean track record.

(ii) Desk Review

The auditors are assigned the assessees to be audited at the beginning of the financial year. The auditors are required to gather as much information about the assessee as possible. They can gather information from the departmental records, published documents like balance sheets annual statements etc., and through market enquirer. Since this can be done without interacting with the assessee, this step called as 'desk-review'.

(iii) Documenting Information

At the stage of 'Desk Review' the auditors may have already identified certain areas, which warrant closer examination. The auditor may also require certain documents or information from the assessee to complete his preliminary investigation. For this he may write letter to the assessee or send him a questionnaire to obtain this information. This step is called 'gathering and documenting assessee information'.

(iv) Touring

The auditor then visits the unit of the assessee to see the actual running of the unit, the systems that are followed for maintaining records in various sections and the system of movement of goods and the related documents within the unit. This step is called 'touring of the premises'. This gives the auditors a general overview about the procedure adopted by the assessee and the possible loopholes through which revenue leakage can take place.

(v) Audit Plan

Based on his experiences and the information gathered so far about the assessee, the auditor now makes a 'audit plan'. The idea of developing audit plan is to list the areas which, as per the auditor are the vulnerable areas from the revenue point of view. Since number of documents/ records maintained by assessee is huge in number, it also necessary that the auditor should select only some of them for the actual verification. The preparation of audit plan helps him to do that.

It must be remembered that audit plan is not rigid but a dynamic concept. During the course of audit if the auditor notices certain new facts or new aspects of the planned area of audit, he can always alter the audit plan accordingly, with the approval of his supervisor. Similarly, during the actual audit, if the auditor is convinced that any area which was earlier planned for verification does not require in-depth scrutiny, he may alter the plan midway after obtaining approval of the superior officers. Preparation of audit plan is one of the most important steps of EA 2000. A well thought audit plan generally increases the success of audit result manifolds.

(vi) Verification

The most important step of audit is the conduct of actual audit, which in technical parlance is called 'Verification'. The auditors visit the unit of the assessee on a scheduled date (informed to the assessee in advance) and carry out the scrutiny of the records of the assessee as per the audit plan. The auditor is required to compare the documentation of a fact from different documents. For example, the auditor may check the figures of clearance of finished goods showed by the assessee in central excise return with the sales figures of the said goods in Balance Sheet, Sales Tax Returns, Bank statements etc. The auditor may also enquire about the entries which appear vague (say an entry like 'Misc. Income') in various records and documents. The idea behind conduct of verification is to reasonably ensure that no amount, which as per the Central Excise law is chargeable to duty, escapes taxation. The process of verification is always carried out in presence of the assessee so that he can clarify the doubts and provide required information to the auditor.

(vii) Audit Objection and Audit Para

Where the auditor finds instances of short payment of duty or non-observance of Central excise procedures, he is required to discuss the issue with the assessee. After explanation provided by the assessee, if the auditor is satisfied that such non-tax compliance has occurred, he records the same as an 'Audit Objection' or 'Audit Para' of the 'draft audit report' that he would be preparing at the end of the verification process. Auditor is advised not to take formal objections to mere procedural lapses/ infractions/ adoption of wrong procedures, which do not result in any short payment of duty or do not have bearing upon the duty payment. In such cases the auditor is required to discuss the matter with the assessee and advise him to follow the correct procedure in future. Further, while making an audit para, attempt should be made to tabulate the duty short paid by the assessee at the spot and incorporate it in the para itself. However, if this is not possible for the paucity of time or for the want of some information not available at that time, the auditor should make a note of the same in his report.

(viii) Audit Report

At the end of the process of verification the auditor prepares an 'Draft Audit Report' which incorporates all the audit objections/audit paras. An audit report provides (issue or para wise) the issue in brief, the reply or the explanation of the assessee, the reason for the auditor not being satisfied with the reply, the amount of short payment (if tabulated) and the recoveries of the same (if could be made at the spot). The draft audit report is then submitted to the superior officers for review, who examine the sustainability of the objections raised by the auditors. After such review, the audit report becomes final and in cases where the disputed amounts have not already been paid by the assessee at the spot, demand notices are issued by the department for their recoveries.

(ix) Conclusion

EA 2000 is a modern, transparent and interactive method of audit wherein the auditor proceeds with audit fully conversant with the business of the assessee. On his part, the assessee is given full opportunity to explain his stand on any particular matter so that matters are resolved in full appreciation of legal position. EA 2000 is thus a participative audit.

A requirement of EA 2000 is that the auditors must be thorough in their knowledge of Central Excise law and procedures, notifications, instructions and circulars issued by the Finance Ministry and the judicial decisions on issues relating to central excise laws. To be successful auditor, knowledge about financial bookkeeping, accountancy and proficiency in understanding commonly used commercial books and documents is of great help. Further, being computer literate is an added requirement while auditing an assessee who maintains his accounts in electronic format.

Departmental Verification

(a) The assessee has to submit periodic returns to Superintendent of Central Excise and date stamped acknowledgement for the same should be obtained.

(b) In general the Superintendent and Inspectors of Central Excise may visit factories of the assessee to verify the records, stock taking and so on. Stock taking can be done for finished goods and CENVAT goods.

(c) Sometimes road checks are carried out by the department authorities to check whether all goods moving are accompanied by duty paying documents or not.

(d) Moreover, each Commissionerate has a preventive section to have surprise checks and raids when evasion is suspected. Directorate of Central Excise Intelligence under Central Board of Excise and Customs gathers information from various sources about the duty evasion and initiate suitable action against them.

In short, in addition to the audit, the Central Excise Department is empowered to carry out verification at ANY point in time.

Submission of Records and Books (vide NT 22/2012 C.Ex. dt. 30-3-201 2)

As per Rule 22(3) of the Central Excise Rules, 2002, every assesse, and an importer who issues an invoice on which Cenvat Credit can be taken and first stage and second stage dealer shall, on demand make available to the officer empowered by the Principal Commissioner or Commissioner or the audit party deputed by the Principal Commissioner or Commissioner or Comptroller and Auditor General of India, or a Cost Accountant or Chartered Accountant nominated under section 14A or section 14AA of the Act,

(i) the records maintained or prepared by the assesse.

(ii) the cost audit reports, if any under section 148 of the Companies Act, 2013.

(iii) the income-tax audit report, if any under section 44AB of the Income-tax Act, 1961.

for the scrutiny of the officer or the audit party or the Cost Accountant or Chartered Accountant, as the case may be.

2.22 EXPORT BENEFITS AND PROCEDURES

2.22.1 Export Benefits and Incentives

In order to boost exports from India various incentives and benefits have been allowed *inter alia* under the Excise and Customs Law. A brief account of the same is given below:

(i) Rebate of duty on "export goods" and "material" used in manufacture of such goods : Rule 18 of the Central Excise Rules, 2002 provides for grant of rebate of duty paid on goods exported or duty paid on the material used in the manufacture of export goods, subject to such conditions, limitations and procedures as specified in the Notifications Nos. 40/2001 -CE(NT) and 41/2001-CE(NT), both dated 26-6-2001.

(ii) Export of goods without payment of excise duty under Bond: As per Rule 19, any excisable goods can be exported or inputs for manufacture of such goods can be removed without payment of duty from the factory or warehouse or any other premises as may be approved by the Principal Commissioner or Commissioner under Bond subject to the conditions safeguards and procedures notified by CBEC *vide* the Notifications Nos. 42/2001-CE(NT) to 45/2001-CE(NT), all dated 26-6-2001.

Further, to facilitate export under Bond , export warehouses have been allowed to be setup, from where goods can also be exported directly. Goods can also be cleared directly from the job workers' premises to export warehouses of even merchant exporters for export.

(iii) Cenvat credit of input excise duty provided drawback for the same is not taken : Where goods are exported under bond, the input credit taken on account of export can be utilized for paying duty on similar products cleared for home consumption. Assessee may also obtain cash refund. However, cash refund of input credit is not admissible for 'deemed exports to FTZ units and 100% EOU's.

(*iv*) Setting up of units in FTZ/EPZ/ETP and Jewellery Complexes and 100% EOU/SEZ : All required inputs and capital goods, whether indigenous or imported, are made available to these units free of customs and excise duties under bond. For getting indigenous/imported inputs, CT-3 book-lets/ Procurement Certificate is issued to them by the Range Officer. These are customs bonded units set up under section 65 of the Customs Act, 1962 but with a much relaxed control and in accordance with the EXIM Policy for manufacture of articles for export out of India or for production or packaging or job work for export of goods or services out of India.

Inter-unit transfers for valid reasons are freely allowed among EPZ/EOU/SEZ units themselves. The warehousing licence for that would be valid for 5 years.

100% EOUs have been given the facility of sending the Customs bonded goods to such contractors in DTA for job work and EOUs/EPZ units have also been allowed to carry out job work for DTA units. Capital goods can be sent to DTA for repairs and return under the Range Superintendent's permission. All EOUs and units having an investment of ₹ 5 crores or above, in plant and machinery, have to show positive value addition only.

(v) Drawback of Customs and Central Excise Duties in respect of Inputs, both Indigenous and Imported: An All Industry Rate Schedule is laid down and published for this purpose within 3 months of presentation of each Budget. If an exporter's goods do not figure therein or if he finds the all Industry rate too low (less than four-fifths of the input duties paid by him), he can apply for fixation of brand rate(s) for his goods. Anti-dumping duty, if actually paid on inputs, can only be claimed by way of brand rate. It is a Simplified Brand Rate Fixation Scheme under which all applicant exporters can be allowed a provisional brand rate within 15 days without pre-verification of data submitted by them. Exporters should send the data duly verified by them and accompanied by original duty paying documents (bills of entry and invoices) direct to the Ministry of Finance (Revenue Department), Joint Secretary (Drawback), Jeevan Deep Building 10, Parliament Street, New Delhi – 110001.

DTA exporters are also eligible for grant of drawback at *brand* rate only in respect of duties suffered on their inputs which are processed by EOU/EPZ units. Sanctions for brand rate are normally valid for one year but for brand rates having all Industry Rate linkage, validity is up to notification of the next AIR Schedule.

Drawback for inputs is permissible not only in case of manufacture but also for processing or other operations for export of goods.

(vi) Drawback of 98% customs duty (including anti-dumping duty): If imported goods are re-exported as such, drawback of 98% customs duty is permitted. Re-export can be through any port and to any party (not necessarily the original supplier of the goods).

(vii) Duty free Replenishment Scheme: The scheme allows duty free replenishment on post-export basis for import of inputs on the basis of input-output norms where such norms exist and on condition of uniform value addition of 33%. The duty exemption is only for basic customs duty, surcharge and

SAD. There would be no exemption for anti-dumping duty or safeguard duty or CVD. But Cenvat credit of CVD can be taken.

(viii) DEEC Scheme: For imported inputs against Advance Licence (Quantity Based only) Duty Entitlement Export Certificate has to be taken subject to bond executed with customs authorities undertaking to export stipulated quantity/value of specified finished goods. These licences are not transferable. However, imports against these licenses have been exempted from payment of all kinds of duties like basic, additional Customs duty, special customs duty, anti-dumping/ safeguard duty.

(ix) DEPB Scheme: Duty entitlement pass book scheme patterned on the credit-debit system of Central Excise CENVAT scheme was scheduled to phase out by March 31, 2002 but is being continued till VAT comes into force.

This scheme has been abolished w.e.f. 01.10.2011 as it was said to be non-complaint of WTO requirement.

(x) Imports for repair, jobbing, etc. free of duties (both basic and additional) : Such imports are made subject to bond for their re-export with 10% value addition. No CCP is required now. Jobbing operations would be carried out in accordance with the Customs (Import of Capital Goods at Concessional Rate for Manufacture of Excisable Goods) Rules, 1996 and not in Customs Bond under section 65. Such export should be completed within 6 months.

(xi) Import of capital goods at 5% concessional rate under EPCG Scheme: Such imports are subject to export obligation and are applicable to all sectors and to all capital goods without any threshold limit. No payment of additional Customs duty (e.v.d.) and special additional duty (SAD) applies. The scheme has also been extended to identified service sectors. The export obligation is to be completed in eight years. However, for the following categories, export obligation period will be 12 years :

1. EPCG licenses of ₹ 100 crores or more;
2. Units in agri-export zones; and
3. Companies under the revival plan of the BIFR.

Further, supplies under deemed exports are eligible to counting for discharge of export obligation.

(xii) Duty Free Entitlement Credit Certificate to Status holders: Who show incremental growth of more than 25% in exports, such certificate would be equal to 10% of the incremental growth achieved during 2002-2003 subject to a maximum turnover of ₹ 25 crores. Imports under it would be exempt from basic customs duty, CVD and SAD. Actual user condition would apply to certificate and the goods imported thereunder [Notificatio No. 53/2003-Cus]

(xiii) Duty Free Entitlement Credit Certificate to Service Providers: It would be equal to 10% (5% in the case of hotels) of average forex earnings of the preceding three years subject to a maximum earning of ₹ 10 lakhs. Extent of exemption and all conditions shall be same as in case of status holders. Service providers should register themselves with FIEO. [Notification No. 54/2003-Cus]

(xiv) Special Economic Zones: By new notifications 22, 23,24, 25/2003-CE & 51 -52/2003-Cus. Special incentives have been provided for the special economic zones set up on Chinese model at Mumbai, Kandla, Cochin and other locations by converting the existing EPZs into SEZ, which would be treated as under outside territory of India.

2.22.2 Export Without Payment of Duty

The Rule 19 of the Central excise Rules, 2002, which corresponds to Rule 13 of the Central excise Rules. 1944 provides that:

i. Any excisable goods may be exported without payment of duty from a factory of the producer or the manufacturer or the warehouse or any other premises, as may be approved by the Principal Commissioner or Commissioner.

ii. Any material may be removed without payment of duty from a factory of the producer or the manufacturer or the warehouse or any other premises for use in the manufacture or processing of goods which are exported, as may be approved by the Principal Commissioner or Commissioner.

iii. The export under sub-rule (1) or sub-rule (2) shall be subject to such conditions, safeguards and procedure as may be specified by notification by the Board.

Categories of Exports

There are two categories of export without payment of duty –

(i) Export of finished goods without payment of duty under bond or undertaking.

(ii) Export of manufactured/processed goods after procuring raw material without payment of duty under bond.

Simplified Export Procedure For Exempted Units

Units, which are fully exempted from payment of duty by a notification granting exemption based on value of clearances for home consumption, may be exempted from filing ARE. 1 and Bond till they remain within the full exemption limit. The following simplified export procedure, as detailed out in the Central Excise Manual, 2001, shall be followed in this regard by such units:

Filing of Declaration

Manufacturers exempted for payment of duty will not be required to take Central Excise Registration. They shall however, file a declaration in terms of Para 2 of Notification No. 36/2001-CE(NT), dated 26-6-2001, and obtain declarant code number [notwithstanding they are exempted from declaration], but for this procedure.

Documentation

The clearance document will be as follows:

(i) Such manufacturers are permitted to use invoices or other similar documents bearing printed Serial Numbers beginning from 1st day of a financial year for the purpose of clearances for home consumption as well as for exports. (The printing of Serial Numbers can be done by use of franking machine). The invoices meant for use during a month shall be pre-authenticated by the owner or partner or Director/ Managing Director of a Company or other authorized person.

(ii) The declarant's Code Number should be mentioned on all clearance documents.

(iii) Such declarant's document should contain particulars of the description of goods, name and address of the buyer, destination, value, [progressive total of total value of excisable goods cleared for home consumption since beginning of the financial year], vehicle number, date and time of the removal of the goods.

(iv) The clearance document will be signed by the manufacturer or his authorized agent at the time of clearance.

(v) In case of export through merchant exporters, the manufacturer will also mention on the top "EXPORT THROUGH MERCHANT EXPORTERS" and will mention the Export-Import Code No. of such merchant exporters.

(vi) In case of direct export by the manufacturer-exporters, he will mention on the top "FOR EXPORT" and his own Export-Import Code No., if any.

2.23 EXCISE ON SMALL SCALE INDUSTRIES

2.23.1 Small Scale Industries

The contribution of Small Scale Sector in the industrial growth of the Indian economy and to the Gross Domestic Product is significant, besides the potential for employment generation. Keeping this into consideration, special provisions of Central Excise are applicable to small-scale units.

2.23.2 Exemption to SSI

- SSI are eligible for exemption from duty under Notification No. 8/2003-CE dated 1-3- 2003. The SSI unit need not be registered with any authority.
- Broadly, items generally manufactured by SSI (except in tobacco, matches and textile sector) are eligible for SSI exemption. Some items like pan masala, matches, watches, tobacco products, Power driven pumps for water not confirming to BIS, products covered under compounded levy scheme etc. are specifically excluded, even when these can be manufactured by SSI. Some items like automobiles, primary iron and steel etc. are not eligible for SSI exemption, but anyway, these are beyond capacity of SSI unit to manufacture.
- Unit whose turnover was less than or equal to ₹ 400 lakh in previous year are entitled to full exemption upto ₹ 150 lakhs in current financial year.
- SSI units manufacturing goods with brand name of others are not eligible for exemption, unless the goods are manufactured in rural area.
- Turnover of all units belonging to a manufacturer will be clubbed for calculating SSI exemption limit.
- Clubbing is also possible if two units are sham or bogus or if there is unity of interest and practically they are one. While calculating limit of ₹ 400/150 lakhs -
- Turnover of Exports, deemed exports, turnover of non-excisable goods, goods manufactured with other's brand name and cleared on full payment of duty, job work done under notification No. 214/86-CE, 83/94-CE and 84/94-CE, processing not amounting to manufacture, strips of plastics used within factory is to be excluded.
- Value of intermediate products (when final product is exempt under notification other than SSI exemption notification), branded goods manufactured in rural area and cleared without payment of duty, export to Nepal and Bhutan and goods cleared on payment of duty is to be included.
- Value of turnover of goods exempted under notification (other than SSI exemption notification or job work exemption notification) is to be included for purpose of limit of ₹ 400 lakhs, but excluded for limit of ₹ 150 lakhs.

Distinction between mode of calculations of ₹ (150/ 400) lakhs

Generally, provisions for calculation of turnover for ₹ 150 lakhs and ₹ 400 lakhs are similar. Major distinction is that if goods are exempt under a notification other than SSI exemption notification or job work exemption notification, that turnover is included for calculating ₹ 400 lakhs limit but *not* for ₹ 150 lakhs limit. If final product is exempt under job work exemption notification, it is not to be considered either for ₹ 150 lakhs or for ₹ 400 lakhs.

Clearances of goods exempted under any other notification to be excluded for ₹150 lakhs but includible for ₹ 400 lakhs - Some goods may be exempt under some other notification, i.e. other than SSI exemption notification. In some cases, duty may not be payable on such goods for some other reason. Turnover of such goods is not to be considered for calculating exemption limit of ₹ 150 lakhs. *However, this turnover (except clearances to EOU, SEZ, STP, EHTP, UN etc. and job work under notifications 214/86-CE, 83/94-CE and 84/94-CE) will have to be considered for calculating exemption limit of ₹ 400 lakhs.*

If some intermediate product gets produced during manufacture of exempted final product, its turnover will be held as includible for calculating exemption limit of ₹ 150 lakhs, if such intermediate product is dutiable.

Example 51: A Ltd. is having a manufacturing unit at Faridabad. In the financial year 2015-16 the value of total clearances from the unit was ₹ 750 lakhs as per the following details: (i) Exports to USA - ₹ 100 lakhs; to Nepal - ₹ 50 lakhs (ii) Clearances to a 100% export oriented unit - ₹ 75 lakhs (iii) Clearances as loan licensee of goods carrying the brand name of another upon full payment of duty - ₹ 200 lakhs (iv) Clearances exempted *vide* Notification No. 214/86-C.E. dated 25-3-86 - ₹ 125 lakhs. (v) Balance clearances of goods in the normal course: ₹ 200 lakhs. You are required to state with reasons whether the unit is entitled to the benefit of exemption under Notification No. 8/2003-C.E.dated 1-3-2003 as amended in the financial year 2009-10.

Answer:

Following is includible for calculating limit of ₹ 400 lakhs : (i) Exports to Nepal - ₹ 50 lakhs (ii) Normal clearances ₹ 200 lakhs. Total ₹ 250 lakhs. Since the turnover is less than ₹ 400 lakhs, A Ltd. is entitled to SSI concession in 2016-17.

Example 52: Z Associates is a Small Scale unit located in a rural area and is availing the benefit of Small Scale exemption under Notification No. 8/2003-C.E. in the year 2015-16. Determine the value of the first clearance and duty liability on the basis of data given below: (i) Total value of clearances of goods with own brand name - ₹ 75,00,000, (ii) Total value of clearances of goods with brand name of other parties - ₹ 90,00,000, (iii) Clearances of goods which are totally exempt under another notification (other than an exemption based on quantity or value of clearances) ₹ 35,00,000.

Normal rate of Excise duty @12.50%. Calculations should be supported with appropriate notes. It may be assumed that the unit is eligible for exemption under Notification No. 8/2003.

Answer:

While calculating SSI exemption limit of ₹ 150 lakhs, goods cleared under brand name in rural area are to be included, since goods manufactured in rural area with brand name of others are entitled for SSI exemption. However, goods which are exempted from duty under notification other than exemption based on quantity or value of clearances is not required to be considered. Thus, for purpose of SSI exemption, the value of turnover is ₹ 165 lakhs. His first turnover of ₹ 150 lakhs is exempt. Thus, he is liable to pay excise duty on ₹ 15 lakhs.

Hence, Excise duty @ 12.50% is ₹ 1,87,500.

Example 53: S & Co., a small scale unit, had cleared goods of the value of ₹ 750 lakhs during the financial year 2015-16. Records show that the following clearances were included in the total turnover of ₹ 750 lakhs : (i) Total exports during the year - ₹ 200 lakhs (30% of total exports were to Nepal), (ii) Job-work in terms of Notification No. 214/86 - ₹ 50 lakhs, (iii) Job-work in terms of Notification No.83 /94-E - 50 lakhs, (iv) Clearances of excisable goods without payment of duty to a 100% E.O.U. ₹ 20 lakhs, (v) Goods manufactured in rural area with others brand - ₹ 100 lakhs. Find out whether the unit is eligible to avail concession for the year 2016-17, under Notification No. 8/2003-CE dated 1st March, 2003, giving reasons for your answer.

Answer:

Turnover not to be considered for ₹400 lakhs - (i) ₹140 lakhs, (ii) ₹50 lakhs, (iii) ₹50 lakhs, (iv) ₹ 20 lakhs. Excluding this turnover, his turnover during 2013-14 was ₹ 490 lakhs. Since it is more than ₹ 400 lakhs, he is not eligible for SSI exemption in 2016-17.

Example 54: The clearances of Dreams Ltd. were ₹ 400 lakh during the financial year 2015-16. The following are included in the said clearances: (i) Exports to Nepal and Bhutan - ₹1,20,00,000, (ii) Exports to countries other than Nepal and Bhutan - ₹1,00,00,000 (iii) Job work exempted from duty under Notification No. 214/86 - ₹ 90,00,000, (iv) Sales to 100% EOU against Form CT-3 - ₹ 50,00,000. The company is of the view that it is not liable to pay any duty on its clearances in the financial year 2016-17 as per Notification No. 8/2003 dated 1st March, 2003. Do you agree with the company? Give reasons for your answer.

Answer:

SSI exemption is available upto first clearances of ₹ 150 lakhs. While calculating limit of ₹ 150 lakhs, exports to countries other than Nepal and Bhutan, job work under notification No. 214/86-CE and supplies to EOU (deemed exports) are not required to be considered. However, supplies to Nepal and Bhutan are required to be considered. If these are excluded, the turnover of the assessee for purpose of calculation of limit of ₹ 150 lakhs is ₹ 160 lakhs [(= ₹400 – ₹100 – ₹ 90 – ₹50) lakhs]. Thus, the assessee can avail exemption of ₹ 150 lakhs and will have to pay duty on ₹ 10 lakhs.

Example 55: A Small Scale Unit (SSI) has effected clearances of goods of the value of ₹ 460 lakhs during the financial year 2015-16. The said clearances include the following: (i) Clearance of excisable goods without payment of Excise duty to a 100% EOU unit - ₹ 40 lakhs. (ii) Export to Nepal and Bhutan - ₹ 50 lakhs, (iii) Job-work in terms of Notification No. 214/86 C.E., which is exempt from duty - ₹ 60 lakhs. (iv) Goods manufactured in rural area with the brand name of others - ₹ 70 lakhs. Write a brief note with reference to the Notifications governing SSI under the Central Excise Act whether the benefit of exemption would be available to the unit for the financial year 2016-17.

Answer:

Turnover in respect of sale to EOU (₹ 40 lakhs) and job work under notification No. 214/86-CE (₹ 60 lakhs) is required to be excluded for purpose of SSI exemption limit of ₹ 400 lakhs. Turnover of SSI excluding these sales is ₹ 360 lakhs (₹460-₹40-₹60 lakhs). Hence, the SSI unit will be entitled to exemption in 2016-17 upto first turnover of ₹ 150 lakhs.

Example 56: A SSI unit has effected clearances of goods of the value of ₹ 475 lacs during the Financial Year 2015-16. The said clearances include the following: (i) Clearance of excisable goods without payment of excise duty to a 100% EOU unit ₹ 120 lacs, (ii) Job work in terms of notification no. 214/86 CE, which is exempt from duty - ₹ 75 lacs, (iii) Export to Nepal and Bhutan - ₹ 50 lacs, (iv) Goods manufactured in rural area with the brand name of the others ₹ 90 lacs. Examine with reference to the notification governing SSI, under the Central Excise Act whether the benefit of exemption would be available to the unit for the Financial Year, 2016-17.

Answer:

While calculating the turnover of ₹ 400 lakhs, following are not required to be considered -

(a) Deemed exports i.e. supplies to 100% EOU (₹ 120 lakhs);

(b) Job work that amounts to 'manufacture' done under notifications No. 214/86-CE, 83/ 94-CE and 84/94-CE (₹ 75 lakhs).

Turnover in respect of sale to EOU (₹ 120 lakhs) and job work under notification No. 214/86-CE (₹ 75 lakhs) is required to be excluded for purpose of SSI exemption limit of ₹ 400 lakhs. Turnover of SSI excluding these sales is ₹ 280 lakhs (₹475-₹120-₹75 lakhs). Hence, the SSI unit will be entitled to exemption in 2016-17 upto first turnovers of ₹ 150 lakhs.

2.23.3 Goods not Eligible for SSI Concession

Many of goods manufactured by SSI are eligible for the concession. However, some items are not eligible (some of the items not eligible for SSI exemption are eligible for exemption under different notifications. Some are not exempt at all). Thus, SSI exemption is available only if the item is covered in this notification.

Broadly, items generally manufactured by SSI (except in tobacco, matches and textile sector) are eligible for SSI exemption. Some items like pan masala, matches, watches, tobacco prodxucts, Power driven pumps for water not confirming to BIS, products covered under compounded levy scheme etc. are specifically excluded, even when these can be manufactured by SSI. Some items like automobiles, primary iron and steel etc. are not eligible for SSI exemption, but anyway, these are beyond capacity of SSI unit to manufacture.

Goods with other's brand name not eligible, but packing material with other's brand name eligible- Goods manufactured by an SSI unit with brand name of others are not eligible for SSI concession, unless goods are manufactured in a rural area. However, SSI exemption will be available to all packing materials meant for use as packing material by or on behalf of the person whose brand name they bear.

2.23.4 Other Provisions in respect of Concession to SSI

Other provisions for concession to SSI are as follows.

'Value' for calculating SSI exemption limit

Value for purpose of calculating the SSI exemption limit of ₹ 150 and ₹ 400 lakhs is the '*Assessable Value*' as per section 4, i.e. transaction value.

However, when goods are assessed on basis of MRP (Maximum Retail Price), the 'value' will be as determined under section 4A.

SSI exemption available in respect of goods exported to Nepal & Bhutan

The SSI exemption is available for home consumption, i.e. for consumption within India. However, explanations to SSI exemption notifications make it clear that clearances for home consumption shall also include clearances for export to Bhutan & Nepal. Thus, exports to Nepal & Bhutan will qualify for SSI exemption, whether the Indian exporter receives payment in Indian Rupees or foreign exchange.

Question 57: Small and company a small scale industry provides the following details. Determine the eligibility for exemption based on value of clearances for the Financial year 2015-16 in terms of Notfn. No. 8/2003-CE dated 1.3.2003 as: (I) Total value of clearances during the financial Year 2014-15 (including VAT ₹ 50 lakhs) ₹ 870 lakhs, (II) Total exports (including for Nepal and Bhutan ₹ 200 lakhs) ₹ 500 lakhs, (III) Clearances of excisable goods without payment of duty to a Unit in software technology park ₹ 20 lakhs, (IV) Job work under Notfn.No.84/94-CE dated 11.4.1994 ₹ 50 lakhs. Job work under Notfn. No. 214/86-CE dated 25.3.1986 ₹ 50 lakhs (v) Clearances of excisable goods bearing brand name of Khadi and Village Industries board ₹ 200 lakhs. Make suitable assumptions and provide brief reasons for your answers where necessary.

Answer:

	₹ in Lakhs
Total turnover	870.00
Less: Value of clearances including VAT	50.00
Total Exports excluding Nepal & Bhutan (500-200)	300.00
Clearance for STP jobs	20.00
Clearance for job work	100.00
Turnover (for calculating limit of crores)	400.00

Goods bearing brand name of Khadi and Village Board are eligible for SSI exemption. Hence, its turnover cannot be excluded for calculating limit of ₹ 4 crores.

Thus, his turnover for purpose of SSI exemption limit is 400 lakhs. The requirement is that turnover should not exceed ₹ 400 lakhs.

Since it is not exceeding ₹ 400 lakhs, the company will be entitled to avail exemption upto first ₹ 150 lakhs in financial year 2015-16.

Question 58: M/s Punctual Ltd., (manufacturing watches) has cleared goods of the value of ₹ 120 lakhs during the financial year 2015-16 exclusive of duties and taxes. The goods attract 12.5% *ad valorem* Excise Duty. Determine the Excise Duty liability when the assessee opts for CENVAT facility and also in the case when the assessee decides not to avail CENVAT benefit. The turnover of the assessee in the previous year 2014-15 was ₹ 100 lakhs.

Answer:

Watches are not eligible for SSI exemption. Hence, the assessee has to pay excise duty on entire turnover of ₹ 120 lakhs @12.5%. Thus, total duty payable is ₹ 15 lakh.

Question 59: Mahesh Ltd., which is engaged in manufacturing of excisable goods, started its business on 1st June, 2014. It availed SSI exemption during the financial year 2015-16. The following are the details available to you:

(i) 12,500 Kg of inputs purchased @ ₹1,190.64 per Kg (Inclusive of Central excise duty @12.5%) ₹ 1,48,83,000;

(ii) Capital goods purchased on 31.5.2015 (Inclusive of Excise duty @12.5%) ₹ 80,09,400;

(iii) Finished goods sold (at uniform transaction value throughout the year) ₹ 3,00,00,000.

You are required to calculate the amount of excise duty payable by M/s Mahesh Ltd. in cash, if any, during the year 2016-17. Rate of duty on finished goods sold may be taken @12.5% for the year and you may assume the selling price exclusive of central excise duty.

There is neither any processing loss nor any inventory of input and output.

Answer:

Statement showing Excise duty liability of M/s Mahesh Ltd for the financial year 2015-16

Particulars	**Value (₹)**	**Cenvat credit (₹)**
Cost of Purchases [i.e. ₹ 1,48,83,000 × 100/112.5]	1,32,29,333	16,53,667
Cost of Capital goods [i.e. ₹ 80,09,400 × 100/112.5] CENVAT credit on capital goods ₹ 8,89,933 (i.e. ₹ 80,09,400 - ₹ 71,19,467)	71,19,467	8,89,933
Total CENVAT credit		25,43,600
Value of Finished goods	3,00,00,000	
Less: Exemption limit	1,50,00,000	
Value of Finished goods attract excise duty	1,50,00,000	
Excise duty @12.5% on ₹ 1,50,00,000	18,75,000	
Less: CENVAT credit (Note 1)		
— on input goods (note 1)	(8,26,834)	
— on capital goods	(8,89,933)	
Net Excess Excise Duty C/F	1,58,233	

Working Note:

(i) Output value = ₹ 3,00,00,000
Input value = ₹ 1,50,00,000

Eligible Cenvat credit on input goods used for manufacture of finished goods beyond ₹150 lakhs is ₹ 8,26,834 (i.e. 16,53,667 × ₹ 150 : ₹ 300).

(ii) For SSI unit, Excise duty is nil, upto ₹ 1,50,00,000 of Finished Goods.

(iii) **Rule 2(a) of the CENVAT Credit Rules, 2004**

CENVAT credit on Capital Goods allowed upto 100% in the year of receipt of such goods for SSI units (w.e.f. 01.04.2010).

Question 60: An SSI unit (manufacturing goods eligible for benefits of SSI exemption notification) has cleared goods of the value of ₹ 60 lakhs during the financial year 2015-16. The effective rate of Central Excise Duty on the goods manufactured by it is 12.5% Ad valorem. What is the correct amount of duty which the unit should have paid on the above clearances for 2015-16?

Answer:

(a) If unit intends to avail Cenvat credit on inputs, duty payable is normal duty i.e. 12.5% of ₹ 60 lakhs, i.e. ₹ 7,50,000. (b) If unit does not intend to avail Cenvat credit on inputs, duty payable is Nil.

Question 61: The value of excisable goods viz. Iron and Steel articles manufactured by M/s. Alpha Ltd. was ₹ 120 lakhs during the financial year 2015-16, net of taxes and duties. The goods attract 12.5% *ad-valorem* basic duty. Determine the excise duty liability when the assessee opts for 'CENVAT' and opts for not to avail 'CENVAT' under SSI exemption notification respectively.

Answer:

M/s Alpha Ltd has no option to opt for SSI exemption benefit since Iron and Steel are ineligible industries for availing the said benefit.

Hence, the duty liability can be calculated is as follows:

Basic excise duty	=	₹ 120 Lakhs × 12.5%	=	₹ 15 Lakhs

Therefore the total excise duty payable is ₹ 15 Lakhs

Question 62: A small scale manufacturer had achieved sales of ₹ 86 lakhs in 2014-15. Turnover achieved during 2015-16 was ₹ 1.52 crores. Normal duty payable on the product is 12.5%. Find the total excise duty paid by the manufacturer during 2015-16 (a) If the unit has availed Cenvat credit, (b) If the unit has not availed Cenvat credit. [The turnover is without taxes and duties].

Answer:

(a) If the unit has availed Cenvat credit, it has to pay full duty on entire turnover. Hence, duty payable is 12.5% of ₹ 1.52 crores i.e. ₹ 19 lakhs.

(b) If the SSI unit has not availed Cenvat, the duty payable is as follows: (i) On first ₹ 150 lakhs : Nil (ii) On subsequent sales - Normal duty of 12.5%. Thus, duty on remaining ₹ 2 lakhs will be ₹ 25,000. Thus, excise duty paid is ₹ 25,000.

Question 63: Z Ltd. is a small-scale industrial unit manufacturing a product X. The Annual report for the year 2015-16 of the unit shows a gross sale turnover of ₹ 1,91,40,000, which includes excise duty and sales tax. The product attracted an excise duty rate of 12.5% as BED, Sales Tax 10%. Determine the duty liability under Notification No. 8/2003-CE, if SSI unit had availed SSI exemption and then paid duty. On the other hand, if SSI had availed Cenvat Credit on all its inputs, what would be the excise duty liability?

Answer:

Duty liability of Z Ltd. in each case is as follows -

(a) In respect of first net turnover of ₹ 150 lakhs (₹ 1,50,00,000), excise duty is Nil. Sales tax @ 10% is payable on net turnover on ₹ 1,50,00,000. Hence, sales tax @ 10% is ₹15,00,000. Thus, gross sale turnover in respect of first net turnover of ₹ 150 lakhs (where excise duty is not paid) is ₹ 1,65,00,000.

Therefore, balance gross sale turnover is ₹ 26,40,000 (₹1,91,40,000 - ₹1,65,00,000). This includes excise duty at 12.5% and sales tax @ 10%.

Excise Duty = [(₹26,40,000 × 100/110) × 12.5/112.5] = ₹ 2,66,667

Sales Tax = ₹26,40,000 × 10/110 = 2,40,000

(b) If SSI unit intends to avail Cenvat credit on all its inputs, it has to pay full 12.50% duty on its entire turnover is as follows:

Excise duty = [(₹1,91,40,000 x 100/110) x 12.5/112.5] = ₹ 19,33,333

Sales tax = ₹1,91,40,000 x 10/110 = ₹ 17,40,000.

Example 64: A small scale manufacturer produces a product ' P'. Some of the production bears his own brand name, while some productions bears brand name of his customer. The customer purchases the goods from the small scale unit and sales himself by adding 20% margin over his purchase cost ₹ 3,53,00,000. He achieved clearances SSI unit in 2015-16 was ₹ 445 lakhs.

The following break up [These clearances are without considering excise duty and sales tax] are —

Clearances with his own brand name - ₹80 lakhs, (ii) Clearances of product bearing his customer's brand name - ₹ 365 lakhs. Normal excise duty of his product is 12.5%. The SSI unit intends to avail Cenvat benefit on inputs on goods supplied to the brand name owner but intends to avail SSI exemption on his own clearances.

(A) Find the total duty paid by the manufacturer in 2015-16, if(i) Inputs are common but SSI unit is able to maintain separate records of inputs in respect of final products under his brand name and those with other's brand name (ii) The inputs are common and SSI unit is not able to maintain separate records on inputs used in final products manufactured under his brand name and with other's brand name.

(B) What will be the rate of excise duty payable by him in April 2016 (i) on product bearing his own brand name and (ii) on product bearing his customer's brand name.

(C) Will there be any difference in duty payable in April 2016 if all his clearances of ₹445 lakhs in 2015-16 were of product under his own brand name?

Answer :

(A) SSI unit can avail Cenvat on final products cleared under other's brand name and avail SSI exemption in respect of his own production.

(i) In the first case, he has to pay duty @ 12.5% on ₹ 365 lakhs, i.e. ₹ 45.63 lakhs. He cannot avail Cenvat credit in respect of inputs used to manufacture product under his own brand name.

(ii) In the second case, since he is unable to maintain separate record of inputs, he will have to pay 6% on ₹ 80 lakhs as per rule 6(3) (i) of Cenvat Credit Rules. Thus, he has to pay duty of ₹ 45.63 lakhs, plus an 'amount' of ₹ 4.80 lakhs. He can avail Cenvat on all the inputs. — Note that in respect of goods bearing customer's brand name, duty is payable on his selling price to the customer even if customer sells them subsequently at higher price.

The assessee has to carefully do his costing and decide (i) whether to avail Cenvat on all inputs, pay full duty on all final products and 6% on final products cleared under his own brand name or (ii) Not avail Cenvat at all and avail exemption from duty on his own production with his brand name.

(B) The turnover of SSI during 2015-16 was not exceeds ₹ 4 crores. However, for purposes of calculating the upper limit of ₹ 4 crores, clearances with other's brand name are not to be considered. Hence, from 1st April 2016, he can clear goods bearing his own brand name upto ₹ 150 lakhs without payment of duty, if he does not avail Cenvat credit on inputs used in such products. If he is unable to maintain separate records, he will have to pay 6% 'amount' on goods manufactured under his own brand name.

(C) If total turnover of ₹ 4.45 crores in 2015-16 was under his own brand name, the manufacturer is not eligible for any Small Scale industry concession in April 2016, and he will have to pay duty at normal rates on his total clearances in April 2016.

Example 65: The value of clearances from four units of M/s X Ltd. during 2015-16 are as follows:—

Units situated at	Value of clearances (₹ in lakh)
Guwahati	120
Patna	100
Delhi	130
Chennai	170

M/s X Ltd. seeks your advice as a consultant whether benefit under Notification No. 8/2003 shall be available to M/s X Ltd. during 2016-17. You are required to indicate your advice in this context.

Answer:

In the given case M/s X Ltd. total turnover for the year 2015-16 is ₹ 520 Lakh (i.e. ₹ 120 + ₹100 + ₹130 + ₹170). Hence, the benefit of exemption Notification No. 8/2003 shall not be available to M/s X Ltd. in the year 2016-17.

Example 66: Determine the amount CENVAT Credit available to M/s Y Ltd. in respect of following items procured by them in the month of October 2015:

(i) If the aggregate value of clearances of M/s Y Ltd. for the financial year 2014-15 is ₹ 450 lakhs;

(ii) If the aggregate value of clearances of M/s Y Ltd. for the financial year 2014-15 is ₹ 350 lakhs and in the current year opted to claim the benefit of the SSI exemption from payment of duty.

Items	Excise duty paid (₹)
Raw materials	52,000
Capital goods used for generation of electricity for captive use within the factory	1,00,000
Motor spirit	40,000
Inputs used for construction of a building	1,00,000
Dairy and bakery products consumed by the employees	5,000
Motor vehicle (not capital goods)	4,50,000

Aggregate clearance of dutiable goods for the month of October 2015 is ₹ 180 lakhs.

Answer:

Statement showing CENVAT Credit allowed or not allowed:

Items	Excise duty paid (₹)	Remarks
Raw materials	52,000	100% CENVAT Credit allowed
Capital goods used for generation of electricity for captive use within the factory	1,00,000	For SSI Units 100% CENVAT Credit allowed. For other than SSI Units upto 50% in the 1st year of receipt of capital goods and balance in subsequent year's
Motor spirit	Nil	CENVAT Credit not allowed
Inputs used for construction of a building	Nil	CENVAT Credit not allowed
Dairy and bakery products consumed by the employees	Nil	CENVAT Credit not allowed
Motor vehicle	Nil	CENVAT Credit not allowed

Statement showing CENVAT Credit allowed amount:

Despcriptoin	**CENVAT Credit eligible for the month of October, 2015 (₹)**	
(i) The aggregate value of clearances of M/s Y Ltd. for the financial year 2014-15 is ₹450 lakhs.	1,02,000 (i.e. 52,000 + [1,00,000 × 50%])	
(ii) The aggregate value of clearances of M/s Y Ltd. for the financial year 2014-15 is ₹350 lakhs.	CENVAT Credit on input goods (i.e. ₹52,000 x 30 lakhs/180 lakhs)	8,667
	CENVAT Cenvat on Capital goods	1,00,000
	Therefore, total CENVAT Credit	1,08,667

Example 67: XYZ & Co., a SSI unit manufactures different products and the value of the clearances for the financial year 2014-15 is given below:

(₹ lakhs)

	Products:	A1	A2	A3
(i)	Clearance for home consumption	55	40	60
(ii)	Captive consumption in the manufacture of excisable goods	100	80	60
(iii)	Export to U.S.A.	90	80	Nil
(iv)	Export to Nepal	50	40	39
(v)	Job work done under Notification 214/86-C.E.	55	30	60
(vi)	Goods manufactured in rural area with brand name of others	45	35	35

The unit seeks your advice as to whether they are eligible for SSI unit exemption for the year 2015-16. Explain the basis for your conclusions.

Answer:

Statement showing aggregate clearance in the financial year 2014-15 (₹ in lakhs)

S. No.	**Particulars**	**Product A1**	**Product A2**	**Product A3**	**Total**	**Remarks**
(i)	Clearance for home consumption	55	40	60	155	
(ii)	Captive consumption in the manufacture of excisable goods	-	-	-	-	This turnover not addable, since it is forming part of finished goods
(iii)	Export to U.S.A.	-	-	-	-	Export turnover excluded
(iv)	Export to Nepal	50	40	39	129	Not considered as export turnover.
(v)	Job work done under Notification 214/86- C.E.	-	-	-	-	Not addable, because it is exempted from duty in the hands of jobworker
(vi)	Goods manufactured in rural area with brand name of others	45	35	35	115	
	Total	**150**	**115**	**134**	**399**	

Note: Option to claim SSI exemption benefit is applicable only when the previous year turnover is less than ₹400 lakhs.

For current year 2015-16 XYZ & Co. is eligible to avail the SSI exemption since, during the previous year the aggregate clearance is ₹ 399 lakhs.

2.24 EXEMPTIONS (SECTION 5A)

Power to grant exemption from duty of excise

(1) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by notification in the Official Gazette exempt generally either absolutely or subject to such conditions (to be fulfilled before or after removal) as may be specified in the notification, excisable goods of any specified description from the whole or any part of the duty of excise leviable thereon:

Provided that, unless specifically provided in such notification, no exemption therein shall apply to excisable goods which are produced or manufactured —

(i) in a free trade zone or a special economic zone and brought to any other place in India; or

(ii) by a hundred per cent export-oriented undertaking and brought to any place in India.

Explanation. — In this proviso, "free trade zone", "special economic zone" and "hundred per cent export-oriented undertaking" shall have the same meanings as in Explanation 2 to sub-section (1) of section 3.

(1A) For the removal of doubts, it is hereby declared that where an exemption under sub-section (1) in respect of any excisable goods from the whole of the duty of excise leviable thereon has been granted absolutely, the manufacturer of such excisable goods shall not pay the duty of excise on such goods.

(2) If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by special order in each case, exempt from payment of duty of excise, under circumstances of an exceptional nature to be stated in such order, any excisable goods on which duty of excise is leviable.

(2A) The Central Government may, if it considers it necessary or expedient so to do for the purpose of clarifying the scope or applicability of any notification issued under sub-section (1) or order issued under sub-section (2), insert an explanation in such notification or order, as the case may be, by notification in the Official Gazette at any time within one year of issue of the notification under sub-section (1) or order under sub-section (2), and every such explanation shall have effect as if it had always been the part of the first such notification or order, as the case may be.

(3) An exemption under sub-section (1) or sub-section (2) in respect of any excisable goods from any part of the duty of excise leviable thereon (the duty of excise leviable thereon being hereinafter referred to as the statutory duty) may be granted by providing for the levy of a duty on such goods at a rate expressed in a form or method different from the form or method in which the statutory duty is leviable and any exemption granted in relation to any excisable goods in the manner provided in this sub-section shall have effect subject to the condition that the duty of excise chargeable on such goods shall in no case exceed the statutory duty.

Explanation. — "Form or method", in relation to a rate of duty of excise means the basis, namely, valuation, weight, number, length, area, volume or other measure with reference to which the duty is leviable.

(4) Every notification issued under sub-rule (1), and every order made under sub-rule (2), of rule 8 of the Central Excise Rules, 1944, and in force immediately before the commencement of the Customs and Central Excises Laws (Amendment) Act, 1988 shall be deemed to have been issued or made under the provisions of this section and shall continue to have the same force and effect after such commencement until it is amended, varied, rescinded or superseded under the provisions of this section.

(5) Every notification issued under sub-section (1) or sub-section 2(A) shall, —

(a) unless otherwise provided, come into force on the date of its issue by the Central Government for publication in the Official Gazette;

(b) also be published and offered for sale on the date of its issue by the Directorate of Publicity and Public Relations, Customs and Central Excise, New Delhi, under the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963.

(6) Notwithstanding anything contained in sub-section (5), where a notification comes into force on a date later than the date of its issue, the same shall be published and offered for sale by the said Directorate of Publicity and Public Relations on a date on or before the date on which the said notification comes into force.

2.25 DEMANDS AND PENALTIES

2.25.1 Recovery of duties not levied or not paid or short-levied or short-paid or erroneously refunded [Section 11A]

(1) Where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, for any reason, other than the reason of fraud or collusion or any wilful misstatement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty,—

(a) the Central Excise Officer shall, within one year from the relevant date, serve notice on the person chargeable with the duty which has not been so levied or paid or which has been so short-levied or short-paid or to whom the refund has erroneously been made, requiring him to show cause why he should not pay the amount specified in the notice;

(b) the person chargeable with duty may, before service of notice under clause (a), pay on the basis of,—

(i) his own ascertainment of such duty; or

(ii) duty ascertained by the Central Excise Officer, the amount of duty along with interest payable thereon under section 11AA.

(2) The person who has paid the duty under clause (b) of sub-section (1), shall inform the Central Excise Officer of such payment in writing, who, on receipt of such information, shall not serve any notice under clause (a) of that sub-section in respect of the duty so paid or any penalty leviable under the provisions of this Act or the rules made thereunder.

(3) Where the Central Excise Officer is of the opinion that the amount paid under clause (b) of sub-section (1) falls short of the amount actually payable, then, he shall proceed to issue the notice as provided for in clause (a) of that sub-section in respect of such amount which falls short of the amount actually payable in the manner specified under that sub-section and the period of one year shall be computed from the date of receipt of information under sub-section (2).

(4) Where any duty of excise has not been levied or paid or has been short levied or short-paid or erroneously refunded, by the reason of—

(a) fraud; or

(b) collusion; or

(c) any wilful mis-statement; or

(d) suppression of facts; or

(e) contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty,

by any person chargeable with the duty, the Central Excise Officer shall, within five years from the relevant date, serve notice on such person requiring him to show cause why he should not pay the amount specified in the notice along with interest payable thereon under section 11AA and a penalty equivalent to the duty specified in the notice.

(5) Omitted vide FA 2015

(6) Omitted vide FA 2015

(7) Omitted vide FA 2015

(7A) Service of a statement containing details of duty not paid, short levied or erroneously refunded shall be deemed to be a Service of notice under Sub-section (1) or (3) or (4) of this section.

(8) In computing the period of one year referred to in clause (a) of subsection (1) or five years referred to in sub-section (4), the period during which there was any stay by an order of the court or Tribunal in respect of payment of such duty shall be excluded.

(9) Where any appellate authority or Tribunal or court concludes that the notice issued under sub-section (4) is not sustainable for the reason that the charges of fraud or collusion or any wilful mis-statement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty has not been established against the person to whom the notice was issued, the Central Excise Officer shall determine the duty of excise payable by such person for the period of one year, deeming as if the notice were issued under clause (a) of sub-section (1).

(10) The Central Excise Officer shall, after allowing the concerned person an opportunity of being heard, and after considering the representation, if any, made by such person, determine the amount of duty of excise due from such person not being in excess of the amount specified in the notice.

(11) The Central Excise Officer shall determine the amount of duty of excise under sub-section (10)—

(a) within six months from the date of notice in respect of cases falling under subsection (1);

(b) within one year from the date of notice in respect of cases falling under subsection (4).

(12) Where the appellate authority modifies the amount of duty of excise determined by the Central Excise Officer under sub-section (10), then the amount of penalties and interest under this section shall stand modified accordingly, taking into account the amount of duty of excise so modified.

(13) Where the amount as modified by the appellate authority is more than the amount determined under sub-section (10) by the Central Excise Officer, the time within which the interest or penalty is payable under this Act shall be counted from the date of the order of the appellate authority in respect of such increased amount.

(14) Where an order determining the duty of excise is passed by the Central Excise Officer under this section, the person liable to pay the said duty of excise shall pay the amount so determined along with the interest due on such amount whether or not the amount of interest is specified separately.

(15) The provisions of sub sections (1) to (14) shall apply, mutadis mutandis, to the recovery of interest where interest payable has not been paid or part paid or erroneously refunded.

(16) The provisions of this section shall not apply to a case where the liability of duty not paid or short-paid is self-assessed and declared as duty payable by the assessee in the periodic returns filed by him, and in such case, recovery of non-payment or short-payment of duty shall be made in such manner as may be prescribed.

Explanation 1—For the purposes of this section and section 11AC,—

(a) "refund" includes rebate of duty of excise on excisable goods exported out of India or on excisable materials used in the manufacture of goods which are exported out of India;

(b) "relevant date" means,—

(i) in the case of excisable goods on which duty of excise has not been levied or paid or has been short-levied or short-paid, and no periodical return as required by the provisions of this Act has been filed, the last date on which such return is required to be filed under this Act and the rules made thereunder;

(ii) in the case of excisable goods on which duty of excise has not been levied or paid or has been short-levied or short-paid and the return has been filed, the date on which such return has been filed;

(iii) in any other case, the date on which duty of excise is required to be paid under this Act or the rules made thereunder;

(iv) in a case where duty of excise is provisionally assessed under this Act or the rules made thereunder, the date of adjustment of duty after the final assessment thereof;

(v) in the case of excisable goods on which duty of excise has been erroneously refunded, the date of such refund;

(vi) In the case where only interest is to be recovered, the date of payment of duty to which such interest relates.

(c) Omitted vide FA 2015.

Explanation 1—For the removal of doubts, it is hereby declared that any non-levy, short-levy, non-payment, short-payment or erroneous refund where no show cause notice has been issued before the date on which the Finance Bill, 2015 receives the assent of the President, shall be governed by the provisions of section 11A as amended by the Finance Act, 2015.

2.25.2 Interest on delayed payment of duty [Section 11AA]

(1) Notwithstanding anything contained in any judgment, decree, order or direction of the Appellate Tribunal or any court or in any other provision of this Act or the rules made thereunder, the person, who is liable to pay duty, shall, in addition to the duty, be liable to pay interest at the rate specified in sub-section (2), whether such payment is made voluntarily or after determination of the amount of duty under section 11A.

(2) Interest, at such rate not below ten per cent and not exceeding thirty-six per cent per annum, as the Central Government may, by notification in the Official Gazette, fix, shall be paid in terms of section 11A after the due date by the person liable to pay duty and such interest shall be calculated from the date on which such duty becomes due up to the date of actual payment of the amount due.

(3) Notwithstanding anything contained in sub-section (1), no interest shall be payable where,—

(a) the duty becomes payable consequent to the issue of an order, instruction or direction by the Board under section 37B; and

(b) such amount of duty is voluntarily paid in full, within forty-five days from the date of issue of such order, instruction or direction, without reserving any right to appeal against the said payment at any subsequent stage of such payment.

2.25.3 Penalty for short-levy or non-levy of duty in certain cases [Section 11AC]

"11AC. Penalty for short-levy or non-levy of duty in certain cases. — (1) The amount of penalty for non-levy or short-levy or non-payment or short-payment or erroneous refund shall be as follows :-

(a) where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, for any reason other than the reason of fraud or collusion or any wilful mis-statement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay a penalty not exceeding ten per cent. of the duty so determined or rupees five thousand, whichever is higher :

Provided that where such duty and interest payable under section 11AA is paid either before the issue of show cause notice or within thirty days of issue of show cause notice, no penalty shall be payable by the person liable to pay duty or the person who has paid the duty and all proceedings in respect of said duty and interest shall be deemed to be concluded;

(b) where any duty as determined under sub-section (10) of section 11A and the interest payable thereon under section 11AA in respect of transactions referred to in clause (a) is paid within thirty days of the date of communication of the order of the Central Excise Officer who has determined such duty, the amount of penalty liable to be paid by such person shall be twenty-five per cent. of the penalty imposed, subject to the condition that such reduced penalty is also paid within the period so specified;

(c) where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, by reason of fraud or collusion or any wilful mis-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay a penalty equal to the duty so determined :

Provided that in respect of the cases where the details relating to such transactions are recorded in the specified record for the period beginning with the 8th April, 2011 up to the date on which the Finance Bill, 2015 receives the assent of the President (both days inclusive), the penalty shall be fifty per cent. of the duty so determined;

(d) where any duty demanded in a show cause notice and the interest payable thereon under section 11AA, issued in respect of transactions referred to in clause (c), is paid within thirty days of the communication of show cause notice, the amount of penalty liable to be paid by such person shall be fifteen per cent. of the duty demanded, subject to the condition that such reduced penalty is also paid within the period so specified and all proceedings in respect of the said duty, interest and penalty shall be deemed to be concluded;

(e) where any duty as determined under sub-section (10) of section 11A and the interest payable thereon under section 11AA in respect of transactions referred to in clause (c) is paid within thirty days of the date of communication of the order of the Central Excise Officer who has determined such duty, the amount of penalty liable to be paid by such person shall be twenty-five per cent. of the duty so determined, subject to the condition that such reduced penalty is also paid within the period so specified.

(2) Where the appellate authority or tribunal or court modifies the amount of duty of excise determined by the Central Excise Officer under sub-section (10) of section 11A, then, the amount of penalty payable under clause (c) of sub-section (1) and the interest payable under section 11AA shall stand modified accordingly and after taking into account the amount of duty of excise so modified, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay such amount of penalty and interest so modified.

(3) Where the amount of duty or penalty is increased by the appellate authority or tribunal or court over the amount determined under sub-section (10) of section 11A by the Central Excise Officer, the time within which the interest and the reduced penalty is payable under clause (b) or clause (e) of sub-section (1) in relation to such increased amount of duty shall be counted from the date of the order of the appellate authority or tribunal or court.

Explanation 1. — For the removal of doubts, it is hereby declared that–

(i) any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where no show cause notice has been issued before the date on which the Finance Bill, 2015 receives the assent of the President shall be governed by the provisions of section 11AC as amended by the Finance Act, 2015;

(ii) any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where show cause notice has been issued but an order determining duty under sub-section (10) of section 11A has not been passed before the date on which the Finance Bill, 2015 receives the assent of the President, shall be eligible to closure of proceedings on payment of duty and interest under the proviso to clause (a) of sub-section (1) or on payment of duty, interest and penalty under clause (d) of sub-section (1), subject to the condition that the payment of duty, interest and penalty, as the case may be, is made within thirty days from the date on which the Finance Bill, 2015 receives the assent of the President;

(iii) any case of non-levy, short-levy, non-payment, short-payment or erroneous refund where an order determining duty under sub-section (10) of section 11A is passed after the date on which the Finance Bill, 2015 receives the assent of the President shall be eligible to payment of reduced penalty under clause (b) or clause (e) of sub-section (1), subject to the condition that the payment of duty, interest and penalty is made within thirty days of the communication of the order.

Explanation 2. — For the purposes of this section, the expression "specified records" means records maintained by the person chargeable with the duty in accordance with any law for the time being in force and includes computerised records.".

2.25.4 Claim for refund of duty and interest, if any, paid on such duty [Section11B]

(1) Any person claiming refund of any duty of excise and interest, if any, paid on such duty may make an application for refund of such duty and interest, if any, paid on such duty to the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise before the expiry of one year from the relevant date in such form and manner as may be prescribed and the application shall be accompanied by such documentary or other evidence (including the documents referred to in section 12A) as the applicant may furnish to establish that the amount of duty of excise and interest, if any, paid on such duty in relation to which such refund is claimed was collected from, or paid by, him and the incidence of such duty and interest, if any, paid on such duty had not been passed on by him to any other person.

Provided that where an application for refund has been made before the commencement of the Central Excises and Customs Laws (Amendment) Act, 1991, such application shall be deemed to have been made under this sub-section as amended by the said Act and the same shall be dealt with in accordance with the provisions of sub-section (2) substituted by that Act.

Provided further that] the limitation of one year shall not apply where any duty and interest, if any, paid on such duty has been paid under protest.

(2) If, on receipt of any such application, the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise is satisfied that the whole or any part of the duty of excise and interest, if any, paid on such duty paid by the applicant is refundable, he may make an order accordingly and the amount so determined shall be credited to the Fund.

Provided that the amount of duty of excise and interest, if any, paid on such duty as determined by the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise]under the foregoing provisions of this sub-section shall, instead of being credited to the Fund, be paid to the applicant, if such amount is relatable to –

(a) rebate of duty of excise on excisable goods exported out of India or on excisable materials used in the manufacture of goods which are exported out of India;

(b) unspent advance deposits lying in balance in the applicant's account current maintained with the Principal Commissioner or Commissioner of Central Excise;

(c) refund of credit of duty paid on excisable goods used as inputs in accordance with the rules made, or any notification issued, under this Act;

(d) the duty of excise and interest, if any, paid on such duty paid by the manufacturer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;

(e) the duty of excise and interest, if any, paid on such duty borne by the buyer, if he had not passed on the incidence of such duty and interest, if any, paid on such duty to any other person;

(f) the duty of excise and interest, if any, paid on such duty borne by any other such class of applicants as the Central Government may, by notification in the Official Gazette, specify :

Provided further that no notification under clause (f) of the first proviso shall be issued unless in the opinion of the Central Government the incidence of duty and interest, if any, paid on such duty has not been passed on by the persons concerned to any other person.

(3) Notwithstanding anything to the contrary contained in any judgment, decree, order or direction of the Appellate Tribunal or any Court or in any other provision of this Act or the rules made thereunder or any other law for the time being in force, no refund shall be made except as provided in sub-section (2).

(4) Every notification under clause (f) of the first proviso to sub-section (2) shall be laid before each House of Parliament, if it is sitting, as soon as may be after the issue of the notification, and, if it is not sitting, within seven days of its re-assembly, and the Central Government shall seek the approval of Parliament to the notification by a resolution moved within a period of fifteen days beginning with the day on which the notification is so laid before the House of the People and if Parliament makes any modification in the notification or directs that the notification should cease to have effect, the notification shall thereafter have effect only in such modified form or be of no effect, as the case may be, but without prejudice to the validity of anything previously done thereunder.

(5) For the removal of doubts, it is hereby declared that any notification issued under clause (f) of the first proviso to sub-section (2), including any such notification approved or modified under sub-section (4), may be rescinded by the Central Government at any time by notification in the Official Gazette.

Explanation. — For the purposes of this section, -

(A) "refund" includes rebate of duty of excise on excisable goods exported out of India or on excisable materials used in the manufacture of goods which are exported out of India;

(B) "relevant date" means, -

(a) in the case of goods exported out of India where a refund of excise duty paid is available in respect of the goods themselves or, as the case may be, the excisable materials used in the manufacture of such goods, -

(i) if the goods are exported by sea or air, the date on which the ship or the aircraft in which such goods are loaded, leaves India, or

(ii) if the goods are exported by land, the date on which such goods pass the frontier, or

(iii) if the goods are exported by post, the date of despatch of goods by the Post Office concerned to a place outside India;

(b) in the case of goods returned for being remade, refined, reconditioned, or subjected to any other similar process, in any factory, the date of entry into the factory for the purposes aforesaid;

(c) in the case of goods to which banderols are required to be affixed if removed for home consumption but not so required when exported outside India, if returned to a factory after having been removed from such factory for export out of India, the date of entry into the factory;

(d) in a case where a manufacturer is required to pay a sum, for a certain period, on the basis of the rate fixed by the Central Government by notification in the Official Gazette in full discharge of his liability for the duty leviable on his production of certain goods, if after the manufacturer has made the payment on the basis of such rate for any period but before the expiry of that period such rate is reduced, the date of such reduction;

(e) in the case of a person, other than the manufacturer, the date of purchase of the goods by such person;

(ea) in the case of goods which are exempt from payment of duty by a special order issued under sub-section (2) of section 5A, the date of issue of such order;

(eb) in case where duty of excise is paid provisionally under this Act or the rules made there under, the date of adjustment of duty after the final assessment thereof;

(ec) in case where the duty becomes refundable as a consequence of judgment, decree, order or direction of appellate authority, Appellate Tribunal or any court, the date of such judgment, decree, order or direction;

(f) in any other case, the date of payment of duty.

2.25.5 Interest on delayed refunds [Section 11BB]

If any duty ordered to be refunded under sub-section (2) of section 11B to any applicant is not refunded within three months from the date of receipt of application under sub-section (1) of that section, there shall be paid to that applicant interest at such rate, not below five per cent and not exceeding thirty per cent per annum as is for the time being fixed by the Central Government, by Notification in the Official Gazette, on such duty from the date immediately after the expiry of three months from the date of receipt of such application till the date of refund of such duty.

Provided that where any duty ordered to be refunded under sub-section (2) of section 11B in respect of an application under sub-section (1) of that section made before the date on which the Finance Bill, 1995 receives the assent of the President, is not refunded within three months from such date, there shall be paid to the applicant interest under this section from the date immediately after three months from such date, till the date of refund of such duty.

Explanation*:* - Where any order of refund is made by the Commissioner (Appeals), Appellate Tribunal, National Tax Tribunal or any court against an order of the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, under sub-section (2) of section 11B, the order passed by the Commissioner (Appeals), Appellate Tribunal, National Tax Tribunal or, as the case may be, by the court shall be deemed to be an order passed under the said sub-section (2) for the purposes of this section.

2.25.6 Power not to recover duty of excise not levied or short-levied as a result of general practice [Section 11C]

(1) Notwithstanding anything contained in this Act, if the Central Government is satisfied -

(a) that a practice was, or is, generally prevalent regarding levy of duty of excise (including non-levy thereof) on any excisable goods; and

(b) that such goods were, or are, liable -

(i) to duty of excise, in cases where according to the said practice the duty was not, or is not being, levied, or

(ii) to a higher amount of duty of excise than what was, or is being, levied, according to the said practice,

then, the Central Government may, by notification in the Official Gazette, direct that the whole of the duty of excise payable on such goods, or as the case may be, the duty of excise in excess of that payable on such goods, but for the said practice, shall not be required to be paid in respect of the goods on which the duty of excise was not, or is not being, levied, or was, or is being, short-levied, in accordance with the said practice.

(2) Where any notification under sub-section (1) in respect of any goods has been issued, the whole of the duty of excise paid on such goods or, as the case may be, the duty of excise paid in excess of that payable on such goods, which would not have been paid if the said notification had been in force, shall be dealt with in accordance with the provisions of sub-section (2) of section 11B.

Provided that the person claiming the refund of such duty or, as the case may be, excess duty, makes an application in this behalf to the Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, in the form referred to in sub-section (1) of section 11B, before the expiry of six months from the date of issue of the said notification.

2.25.7 Duties of excise collected from the buyer to be deposited with the Central Government [Section 11D]

(1) Notwithstanding anything to the contrary contained in any order or direction of the Appellate Tribunal or any Court or in any other provision of this Act or the rules made thereunder, every person who is liable to pay duty under this Act or the rules made thereunder, and has collected any amount in excess of the duty assessed or determined and paid on any excisable goods under this Act or the rules made thereunder from the buyer of such goods in any manner as representing duty of excise, shall forthwith pay the amount so collected to the credit of the Central Government.

(1A) Every person, who has collected any amount in excess of duty assessed or determined and paid on any excisable goods or has collected any amount as representing duty of excise on any excisable goods which are wholly exempt or chargeable to nil rate of duty from any person in any manner, shall forthwith pay the amount so collected to the credit of the Central Government.

(2) Where any amount is required to be paid to the credit of the Central Government under sub-section (1) or sub-section (1A), as the case may be, and which has not been so paid, the Central Excise Officer may serve, on the person liable to pay such amount, a notice requiring him to show cause why the said amount, as specified in the notice, should not be paid by him to the credit of the Central Government.

(3) The Central Excise Officer shall, after considering the representation, if any, made by the person on whom the notice is served under sub-section (2), determine the amount due from such person (not being in excess of the amount specified in the notice) and thereupon such person shall pay the amount so determined.

(4) The amount paid to the credit of the Central Government under sub-section (1) or sub-section (1A) or sub-section (3), as the case may be, shall be adjusted against the duty of excise payable by the person on finalisation of assessment or any other proceeding for determination of the duty of excise relating to the excisable goods referred to in sub-section (1) and sub-section (1A).

(5) Where any surplus is left after the adjustment under sub-section (4), the amount of such surplus shall either be credited to the Fund or, as the case may be, refunded to the person who has borne the incidence of such amount, in accordance with the provisions of section 11B and such person may make an application under that section in such cases within six months from the date of the public notice to be issued by the Assistant Commissioner of Central Excise for the refund of such surplus amount.

2.25.8 Interest on the amounts collected in excess of the duty [Section 11DD]

(1) Where an amount has been collected in excess of the duty assessed or determined and paid on any excisable goods under this Act or the rules made thereunder from the buyer of such goods, or from any person or where a person has collected any amount as representing duty of excise on any excisable which are wholly exempt or are chargeable to Nil rate of duty, the person who is liable to pay such amount as determined under sub-section (3) of section 11D, shall, in addition to the amount, be liable to pay interest at such rate not below ten per cent, and not exceeding thirty-six per cent. per annum, as is for the time being fixed by the Central Government, by notification in the Official Gazette, from the first day of the month succeeding the month in which the amount ought to have been paid under this Act, but for the provisions contained in sub-section (3) of section 11D, till the date of payment of such amount.

Provided that in such cases where the amount becomes payable consequent to issue of an order, instruction or direction by the Board under section 37B, and such amount payable is voluntarily paid in full, without reserving any right to appeal against such payment at any subsequent stage, within forty-five days from the date of issue of such order, instruction or direction, as the case may be, no interest shall be payable and in other cases the interest shall be payable on the whole amount, including the amount already paid.

(2) The provisions of sub-section (1) shall not apply to cases where the amount had become payable or ought to have been paid before the day on which the Finance Bill, 2003 receives the assent of the President.

Explanation *1*. - Where the amount determined under sub-section (3) of section 11D is reduced by the Commissioner (Appeals), the Appellate Tribunal or, as the case may be, the court, the interest payable thereon under sub-section (1) shall be on such reduced amount.

Explanation *2*. - Where the amount determined under sub-section (3) of section 11D is increased by the Commissioner (Appeals), the Appellate Tribunal or, as the case may be, the court, the interest payable thereon under sub-section (1) shall be on such increased amount.

2.25.9 Provisional attachment to protect revenue in certain cases [Section 11DDA]

(1) Where, during the pendency of any proceedings under section 11A or section 11D, the Central Excise Officer is of the opinion that for the purpose of protecting the interest of revenue, it is necessary so to do, he may, with the previous approval of the Principal Commissioner or Commissioner of Central Excise, by order in writing, attach provisionally any property belonging to the person on whom notice is served under sub-section (1) of section 11A or sub-section (2) of section 11D, as the case may be, in accordance with the rules made in this behalf under section 142 of the Customs Act, 1962.

(2) Every such provisional attachment shall cease to have effect after the expiry of a period of six months from the date of the order made:

Provided that the Principal Chief Commissioner or Chief Commissioner of Central Excise may, for reasons to be recorded in writing, extend the aforesaid period by such further period or periods as he thinks fit, so, however, that the total period of extension shall not in any case exceed two years:

Provided further that where an application for settlement of case under section 32E is made to the Settlement Commission, the period commencing from the date on which such application is made and ending with the date on which an order under sub-section (1) of section 32F is made shall be excluded from the period specified in the preceding proviso.

2.25.10 Adjudication Powers:

Authority	**Remission of duty (upto ₹)**	**Demand of Duty (upto ₹)**
The Superintendent	10,000	1,00,000
The Deputy/Assistant Commissioner	1,00,000	5,00,000
The Joint/Additional Commissioner	5,00,000	50,00,000
Principal Commissioner or Commissioner	without any upper limit	without any upper limit

Note :

1. Demand of duty or differential duty may be relating to * determination of valuation and / or classification or * Cenvat credit cases or * duty short paid or not paid or erroneously refunded for any reason. Such demand may or may not contain for allegation of fraud, suppression of facts etc. (in other words, whether or not there is allegation of fraud/suppression of facts etc., the monetary limit of adjudication remains same.

2. As per CBE&C circular No. 809/6/2005-CX dated 1-3-2005, in case of refund claim, AC/ DC can pass order without any monetary limit. However, claims of ₹ 5 lakhs and above will be subject to pre-audit at level of jurisdictional Principal Commissioner or Commissioner

3. It has been clarified that value of goods/conveyance, plants, machinery, land, building etc. liable to confiscation will not alter the powers of adjudication as the powers solely depend upon the amount of duty/Cenvat credit involved on the offending goods.

   Who can issue show cause notice - Show cause notice should be approved and signed by officer empowered to adjudicate the case.

2.26 POWER OF OFFICER

Powers of Central Excise Officers:

(i) Power to access registered premises: As per Rule 22(1) of Central Excise Rules, 2002, an officer empowered by the Principal Commissioner or Commissioner in this behalf shall have access to any premises registered under these rules for the purpose of carrying out any scrutiny, verification and checks as may be necessary to safeguard the interest of revenue.

(ii) Power to stop and search: As per Rule 23 of Central Excise Rules, 2002, any Central Excise Office, may search any conveyance carrying excisable goods in respect of which he has reason to believe that the goods are being carried with the intention of evading duty.

(iii) Power to detain or seize gods: As per Rule 24 of Central Excise Rules, 2002, if a Central Excise Officer, has reason to believe that any goods, which are liable to excise duty but no duty has been paid thereon or the said goods were removed with the intention of evading the duty payable thereon, the Central Excise Officer may detain or seize such goods.

(iv) Powers of to delegate authority: As per Section 12E(1) of Central Excise Act, 1944, a Central Excise Officer may exercise the powers and discharge the duties conferred or imposed under this Act on any other Central Excise Officer who is subordinate to him.

Notwithstanding anything contained in sub-section (1), the Commissioner of Central Excise (Appeals) shall not exercise the powers and discharge the duties conferred or imposed on a Central Excise Officer other than those specified in section 14.

(v) Power to arrest: As per Section 13 of the Central Excise Act, 1944, Central Excise Officer not below the rank of Inspector of Central Excise may, with prior approval of the Principal Commissioner or Commissioner of Central Excise, arrest any person whom he has reason to believe to be liable to punishment under this Act or the rules made thereunder.

Note: provisions of arrest are not applicable to service tax matters.

(vi) Power to summon persons to give evidence and produce documents in inquiries under this Act:

As per Section 14 of the Central Excise Act, 1944,

(a) Any Central Excise Officer duly empowered by the Central Government in this behalf, shall have power to summon any person whose attendance he considers necessary either to give evidence or to produce a document or any other thing in any inquiry which such officer is making for any of the purposes of this Act. A summons to produce documents or other things may be for the production of certain specified documents or things or for the production of all documents or things of a certain description in the possession or under the control of the person summoned.

(b) All persons so summoned shall be bound to attend, either in person or by an authorised agent, as such officer may direct; and all persons so summoned shall be bound to state the truth upon any subject respecting which they are examined or make statements and to produce such documents and other things as may be required:

Provided that the exemptions under Sections 132 and 133 of the Code of Civil Procedure, 1908 (5 of 1908) shall be applicable to requisitions for attendance under this section.

(c) Every such inquiry as aforesaid shall be deemed to be a "judicial proceeding" within the meaning of Section 193 and Section 228 of the Indian Penal Code, 1860.

2.27 APPEALS UNDER EXCISE

Appeals under Excise

Appeals to Commissioner (Appeals) [Section 35]

(1) Any person aggrieved by any decision or order passed under this Act by a Central Excise Officer, lower in rank than a Principal Commissioner or Commissioner of Central Excise , may appeal to the Commissioner of Central Excise (Appeals) hereafter in this Chapter referred to as the Commissioner (Appeals) within sixty days from the date of the communication to him of such decision or order.

Provided that the Commissioner (Appeals) may, if he is satisfied that the appellant was prevented by sufficient cause from presenting the appeal within the aforesaid period of sixty days, allow it to be presented within a further period of thirty days.

(1A) The Commissioner (Appeals) may, if sufficient cause is shown at any stage of hearing of an appeal, grant time, from time to time, to the parties or any of them and adjourn the hearing of the appeal for reasons to be recorded in writing.

Provided that no such adjournment shall be granted more than three times to a party during hearing of the appeal.

(2) Every appeal under this section shall be in the prescribed form and shall be verified in the prescribed manner.

Procedure in appeal [Section 35A]

(1) The Commissioner (Appeals) shall give an opportunity to the appellant to be heard, if he so desires.

(2) The Commissioner (Appeals) may, at the hearing of an appeal, allow an appellant to go into any ground of appeal not specified in the grounds of appeal, if the Commissioner (Appeals) is satisfied that the omission of that ground from the grounds of appeal was not willful or unreasonable.

(3) The Commissioner (Appeals) shall, after making such further inquiry as may be necessary, pass such order, as he thinks just and proper, confirming, modifying or annulling the decision or order appealed against.

Provided that an order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value or reducing the amount of refund shall not be passed unless the appellant has been given a reasonable opportunity of showing cause against the proposed order:

Provided further that where the Commissioner (Appeals) is of opinion that any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, no order requiring the appellant to pay any duty not levied or paid, short-levied or short-paid or erroneously refunded shall be passed unless the appellant is given notice within the time-limit specified in section 11A to show cause against the proposed order.

(4) The order of the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision.

(5) The Commissioner (Appeals) shall, where it is possible to do so, hear and decide every appeal within a period of six months from the date on which it is filed.

(6) On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the appellant, the adjudicating authority, the Principal Chief Commissioner or Chief

Commissioner of Central Excise and the Principal Commissioner or Commissioner of Central Excise.

Appeals to the Appellate Tribunal [Section 35B]

(1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order —

(a) a decision or order passed by the Principal Commissioner or Commissioner of Central Excise as an adjudicating authority;

(b) an order passed by the Commissioner (Appeals) under section 35A;

(c) an order passed by the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 (hereafter in this Chapter referred to as the Board or the Appellate Commissioner of Central Excise under section 35, as it stood immediately before the appointed day;

(d) an order passed by the Board or the Principal Commissioner or Commissioner of Central Excise , either before or after the appointed day, under section 35A, as it stood immediately before that day.

Provided that no appeal shall lie to the Appellate Tribunal and the Appellate Tribunal shall not have jurisdiction to decide any appeal in respect of any order referred to in clause (b) if such order relates to, —

(a) a case of loss of goods, where the loss occurs in transit from a factory to a warehouse or to another factory, or from one warehouse to another, or during the course of processing of the goods in a warehouse or in storage, whether in a factory or in a warehouse;

(b) a rebate of duty of excise on goods exported to any country or territory outside India or on excisable materials used in the manufacture of goods which are exported to any country or territory outside India;

(c) goods exported outside India (except to Nepal or Bhutan) without payment of duty ;

(d) credit of any duty allowed to be utilised towards payment of excise duty on final products under the provisions of this Act or the rules made thereunder and such order is passed by the Commissioner (Appeals) on or after the date appointed under section 109 of the Finance (No. 2) Act, 1998.

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or clause (d) where —

(i) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; o

(ii) the amount of fine or penalty determined by such order, does not exceed two lakh rupees;

(1A) Every appeal against any order of the nature referred to in the first proviso to sub-section (1), which is pending immediately before the commencement of Section 47 of the Finance Act, 1984, before the Appellate Tribunal and any matter arising out of, or connected with, such appeal and which is so pending shall stand transferred on such commencement to the Central Government, and the Central Government shall deal with such appeal or matter under section 35EE as if such appeal or matter were an application or a matter arising out of an application made to it under that section.

(1B) (i) The Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 may, by order, constitute such Committees as may be necessary for the purposes of this Act.

(ii) Every Committee constituted under clause (i) shall consist of two Principal Commissioner or Chief Commissioners of Central Excise or two Principal Commissioner or Commissioners of Central Excise, as the case may be.

(2) The Committee of Principal Commissioner or Commissioners of Central Excise may, if it is of opinion that an order passed by the Appellate Commissioner of Central Excise under section 35, as it stood immediately before the appointed day, or the Commissioner (Appeals) under section 35A, is not legal or proper, direct any Central Excise Officer authorised by him in this behalf (hereafter in this Chapter referred to as the authorisedofficer) to appeal on its behalf to the Appellate Tribunal against such order.

Provided that where the committee of Principal Commissioner or Commissioners of Central Excise differs in its opinion regarding the appeal against the order of the Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Principal Chief Commissioner or Chief Commissioner of Central Excise who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct any Central Excise Officer to appeal to the Appellate Tribunal against such order.

Explanation- For the purposes of this sub section, "Jurisdiction Principal Chief Commissioner or Chief Commissioner" means the Principal Chief Commissioner or Chief Commissioner of Central Excise having jurisdiction over the adjudicating authority in the matter.

(3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Principal Commissioner or Commissioner of Central Excise, or, as the case may be, the other party preferring the appeal.

(4) On receipt of notice that an appeal has been preferred under this section, the party against whom the appeal has been preferred may, notwithstanding that he may not have appealed against such order or any part thereof, file, within forty-five days of the receipt of the notice, a memorandum of cross-objections verified in the prescribed manner against any part of the order appealed against and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in sub-section (3).

(5) The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period referred to in sub-section (3) or sub-section (4), if it is satisfied that there was sufficient cause for not presenting it within that period.

(6) An appeal to the Appellate Tribunal shall be in the prescribed form and shall be verified in the prescribed manner and shall, irrespective of the date of demand of duty and interest or of levy of penalty in relation to which the appeal is made, be accompanied by a fee of, —

(a) where the amount of duty and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is five lakh rupees or less, one thousand rupees;

(b) where the amount of duty and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is more than five lakh rupees but not exceeding fifty lakhrupees, five thousand rupees;

(c) where the amount of duty and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is more than fifty lakh rupees, ten thousand rupees:

Provided that no such fee shall be payable in the case of an appeal referred to in sub-section (2) or a memorandum of cross-objections referred to in sub-section (4).

(7) Every application made before the Appellate Tribunal —

(a) in an appeal for grant of stay or for rectification of mistake or for any other purpose; or

(b) for restoration of an appeal or an application,shall be accompanied by a fee of five hundred rupees.

Provided that no such fee shall be payable in the case of an application filed by or on behalf of the Principal Commissioner or Commissioner of Central Excise under this sub-section.

Orders of Appellate Tribunal [Section 35C]

(1) The Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or annulling the decision or order appealed against or may refer the case back to the authority which passed such decision or order with such directions as the Appellate Tribunal may think fit, for a fresh adjudication or decision, as the case may be, after taking additional evidence, if necessary.

(1A) The Appellate Tribunal may, if sufficient cause is shown, at any stage of hearing of an appeal, grant time, from time to time, to the parties or any of them and adjourn the hearing of the appeal for reasons to be recorded in writing:

Provided that no such adjournment shall be granted more than three times to a party during hearing of the appeal.

(2) The Appellate Tribunal may, at any time within six months from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it under sub-section (1) and shall make such amendments if the mistake is brought to its notice by the Principal Commissioner or Commissioner of Central Excise or the other party to the appeal:

Provided that an amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the other party, shall not be made under this sub-section, unless the Appellate Tribunal has given notice to him of its intention to do so and has allowed him a reasonable opportunity of being heard.

(2A) The Appellate Tribunal shall, where it is possible to do so, hear and decide every appeal within a period of three years from the date on which such appeal is filed:

(3) The Appellate Tribunal shall send a copy of every order passed under this section to the Principal Commissioner or Commissioner of Central Excise and the other party to the appeal.

(4) Save as provided in section 35G or section 35L, orders passed by the Appellate Tribunal on appeal shall be final.

Procedure of Appellate Tribunal [Section 35D]

(1) The provisions of sub-sections (1), (2), (5) and (6) of section 129C of the Customs Act, 1962 (52 of 1962), shall apply to the Appellate Tribunal in the discharge of its functions under this Act as they apply to it in the discharge of its functions under the Customs Act, 1962.

(2) **Omitted**

(3) The President or any other member of the Appellate Tribunal authorised in this behalf by the President may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member where —

(a) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or

(b) the amount of fine or penalty involved, does not exceed fifty lakh rupees.

Powers of Committee of Principal Chief Commissioner or Chief Commissioners of Central Excise or Principal Commissioner or Commissioner of Central Excise to pass certain orders [Section 35E]

(1) The Committee of Principal Chief Commissioner or Chief Commissioners of Central Excise may, of its own motion, call for and examine the record of any proceeding in which a Principal Commissioner or Commissioner of Central Excise as an adjudicating authority has passed any decision or order under this Act for the purpose of satisfying itself as to the legality or propriety of any such decision or order and may, by order, direct such Principal Commissioner or Commissioner or any other Principal Commissioner or Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order as may be specified by the Committee of Principal Chief Commissioner or Chief Commissioners of Central Excise in its order.

Provided that where the Committee of Principal Chief Commissioner or Chief Commissioners of Central Excise differs in its opinion as to the legality or propriety of the decision or order of the Principal Commissioner or Commissioner of Central Excise, it shall state the point or points on which it differs and make a reference to the Board which, after considering the facts of the decision or order, if is of the opinion that the decision or order passed by the Principal Commissioner or Commissioner of Central Excise is not legal or proper, may, by order, direct such Principal Commissioner or Commissioner or any other Principal Commissioner or Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order, as may be specified in its order.

(2) The Principal Commissioner or Commissioner of Central Excise may, of his own motion, call for and examine the record of any proceeding in which an adjudicating authority subordinate to him has passed any decision or order under this Act for the purpose of satisfying himself as to the legality or propriety of any such decision or order and may, by order, direct such authority or any Central Excise Officer subordinate to him to apply to the Commissioner (Appeals) for the determination of such points arising out of the decision or order as may be specified by the Principal Commissioner or Commissioner of Central Excise in his order.

(3) Every order under sub-section (1) or sub-section (2), as the case may be, shall be made within a period of three months from the date of communication of the decision or order of the adjudicating authority.

Provided that the Board may, on sufficient cause shown, extend the said period by another thirty days.

(4) Where in pursuance of an order under sub-section (1) or sub-section (2) the adjudicating authority or the authorised officer makes an application to the Appellate Tribunal or the Commissioner (Appeals) within a period of one month from the date of communication of the order under sub-section (1) or sub-section (2) to the adjudicating authority, such application shall be heard by the Appellate Tribunal or the Commissioner (Appeals), as the case may be, as if such application were an appeal made against the decision or order of the adjudicating authority and the provisions of this Act regarding appeals, including the provisions of sub-section (4) of section 35B shall, so far as may be, apply to such application.

(5) Omitted

SECTION 35EA. Omitted

Revision by Central Government [Section 35EE]

(1) The Central Government may, on the application of any person aggrieved by any order passed under section 35A, where the order is of the nature referred to in the first proviso to sub-section (1) of section 35B, annul or modify such order :

Provided that the Central Government may in its discretion, refuse to admit an application in respect of an order where the amount of duty or fine or penalty, determined by such order does not exceed five thousand rupees.

Explanation. — For the purposes of this sub-section, "order passed under section 35A" includes an order passed under that section before the commencement of section 47 of the Finance Act, 1984 against which an appeal has not been preferred before such commencement and could have been, if the said section had not come into force, preferred after such commencement, to the Appellate Tribunal.

(1A) The Principal Commissioner or Commissioner of Central Excise may, if he is of the opinion that an order passed by the Commissioner (Appeals) under section 35A is not legal or proper, direct the proper officer to make an application on his behalf to the Central Government for revision of such order.

(2) An application under sub-section (1) shall be made within three months from the date of the communication to the applicant of the order against which the application is being made:

Provided that the Central Government may, if it is satisfied that the applicant was prevented by sufficient cause from presenting the application within the aforesaid period of three months, allow it to be presented within a further period of three months.

(3) An application under sub-section (1) shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf and shall be accompanied by a fee of, -

(a) two hundred rupees, where the amount of duty and interest demanded, fine or penalty levied by any Central Excise officer in the case to which the application relates is one lakh rupees or less;

(b) one thousand rupees, where the amount of duty and interest demanded, fine or penalty levied by any Central Excise officer in the case to which the application relates is more than one lakh rupees :

Provided that no such fee shall be payable in the case of an application referred to in sub-section (1A).

(4) The Central Government may, of its own motion, annul or modify any order referred to in sub-section (1).

(5) No order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value shall be passed under this section, —

(a) in any case in which an order passed under section 35A has enhanced any penalty or fine in lieu of confiscation or has confiscated goods of greater value; and

(b) in any other case, unless the person affected by the proposed order has been given notice to show cause against it within one year from the date of the order sought to be annulled or modified.

(6) Where the Central Government is of opinion that any duty of excise has not been levied or has been short-levied, no order levying or enhancing the duty shall be made under this section unless the person affected by the proposed order is given notice to show cause against it within the time-limit specified in section 11A.

SECTION 35F. Deposit of certain percentage of duty demanded or penalty imposed before filling appeal

The Tribunal or the Commissioner (Appeals), as the case may be, shall not entertain any appeal,—

(i) under sub-section (1) of section 35, unless the appellant has deposited seven and a half per cent, of the duty demanded or penalty imposed or both, in pursuance of a decision or an order passed by an officer of Central Excise lower in rank than the Commissioner of Central Excise;

(ii) against the decision or order referred to in clause (a) of sub-section (1) of section 35B, unless the appellant has deposited seven and a half per cent, of the duty demanded or penalty imposed or both, in pursuance of the decision or order appealed against;

(iii) against the decision or order referred to in clause (b) of sub-section (1) of section 35B, unless the appellant has deposited ten per cent, of the duty demanded or penalty imposed or both, in pursuance of the decision or order appealed against:

Provided that the amount required to be deposited under this section shall not exceed rupees ten crores:

Provided further that the provisions of this section shall not apply to the stay applications and appeals pending before any appellate authority prior to the commencement of the Finance (No.2) Act, 2014.

Explanation.— For the purposes of this section "duty demanded" shall include,—

(i) amount determined under section 11D;

(ii) amount of erroneous Cenvat credit taken;

(iii) amount payable under rule 6 of the Cenvat Credit Rules, 2001 or the Cenvat Credit Rules, 2002 or the Cenvat Credit Rules, 2004.

Interest on delayed refund of amount deposited under the proviso to Section 35F [Section 35FF]

Where an amount deposited by the appellant in pursuance of an order passed by the Commissioner (Appeals) or the Appellate Tribunal (hereinafter referred to as the appellate authority), under the first proviso to section 35F, is required to be refunded consequent upon the order of the appellate authority and such amount is not refunded within three months from the date of communication of such order to the adjudicating authority, unless the operation of the order of the appellate authority is stayed by a superior court or tribunal, there shall be paid to the appellant interest at the rate specified in section 11BB after the expiry of three months from the date of communication of the order of the appellate authority, till the date of refund of such amount.

SECTION 35G. Appeal to High Court

(1) An appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal on or after the 1st day of July, 2003 (not being an order relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment), if the High Court is satisfied that the case involves a substantial question of law.

(2) The Principal Commissioner or Commissioner of Central Excise or the other party aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court and such appeal under this sub-section shall be -

(a) filed within one hundred and eighty days from the date on which the order appealed against is received by the Principal Commissioner or Commissioner of Central Excise or the other party;

(b) accompanied by a fee of two hundred rupees where such appeal is filed by the other party;

(c) in the form of a memorandum of appeal precisely stating therein the substantial question of law involved.

(2A) The High Court may admit an appeal after the expiry of the period of one hundred and eighty days referred to in clause (a) of sub-section (2), if it is satisfied that there was sufficient cause for not filing the same within that period.

(3) Where the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate that question.

(4) The appeal shall be heard only on the question so formulated, and the respondents shall, at the hearing of the appeal, be allowed to argue that the case does not involve such question:

Provided that nothing in this sub-section shall be deemed to take away or abridge the power of the Court to hear, for reasons to be recorded, the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.

(5) The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the grounds on which such decision is founded and may award such cost as it deems fit.

(6) The High Court may determine any issue which -

(a) has not been determined by the Appellate Tribunal; or

(b) has been wrongly determined by the Appellate Tribunal, by reason of a decision on such question of law as is referred to in sub-section (1).

(7) When an appeal has been filed before the High Court, it shall be heard by a bench of not less than two Judges of the High Court, and shall be decided in accordance with the opinion of such Judges or of the majority, if any, of such Judges.

(8) Where there is no such majority, the Judges shall state the point of law upon which they differ and the case shall, then, be heard upon that point only by one or more of the other Judges of the High Court and such point shall be decided according to the opinion of the majority of the Judges who have heard the case including those who first heard it.

(9) Save as otherwise provided in this Act, the provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the High Court shall, as far as may be, apply in the case of appeals under this section.

Application to High Court [Section 35H]

(1) The Principal Commissioner or Commissioner of Central Excise or the other party may, within one hundred and eighty days of the date upon which he is served with notice of an order under section 35C passed before the 1st day of July, 2003 (not being an order relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment), by application in the prescribed form, accompanied, where the application is made by the other party, by a fee of two hundred rupees, apply to the High Court to direct the Appellate Tribunal to refer to the High Court any question of law arising from such order of the Tribunal.

(2) The Principal Commissioner or Commissioner of Central Excise or the other party applying to the High Court under sub-section (1) shall clearly state the question of law which he seeks to be referred to the High Court and shall also specify the paragraph in the order of the Appellate Tribunal relevant to the question sought to be referred.

(3) On receipt of notice that an application has been made under sub-section (1), the person against whom such application has been made, may, notwithstanding that he may not have filed such application, file, within forty-five days of the receipt of the notice, a memorandum of cross-objections verified in the prescribed manner against any part of the order in relation to which an application for reference has been made and such memorandum shall be disposed of by the High Court as if it were an application presented within the time specified in sub-section (1).

(3A) The High Court may admit an application or permit the filing of a memorandum of cross objections after the expiry of the relevant period referred to in sub-section (1) or sub-section (3), if it is satisfied that there was sufficient cause for not filing the same within that period.

(4) If, on an application made under sub-section (1), the High Court directs the Appellate Tribunal to refer the question of law raised in the application, the Appellate Tribunal shall, within one hundred and twenty days of the receipt of such direction, draw up a statement of the case and refer it to the High Court.

Power of High Court or Supreme Court to require statement to be amended [Section 35-I]

If the High Court or the Supreme Court is not satisfied that the statements in a case referred to it are sufficient to enable it to determine the questions raised thereby, the Court may refer the case back to the Appellate Tribunal for the purpose of making such additions thereto or alterations therein as it may direct in that behalf.

Case before High Court to be heard by not less than two judges [Section 35J]

(1) When any case has been referred to the High Court [under section 35G or section 35H , it shall be heard by a Bench of not less than two judges of the High Court and shall be decided in accordance with the opinion of such judges or of the majority, if any, of such judges.

(2) Where there is no such majority, the judges shall state the point of law upon which they differ and the case shall then be heard upon that point only by one or more of the other judges of the High Court, and such point shall be decided according to the opinion of the majority of the judges who have heard the case including those who first heard it.

Decision of High Court or Supreme Court on the case stated [Section 35K]

(1) The High Court or the Supreme Court hearing any such case shall decide the question of law raised therein and shall deliver its judgment thereon containing the grounds on which such decision is founded and a copy of the judgment shall be sent under the seal of the Court and the signature of the Registrar to the Appellate Tribunal which shall pass such orders as are necessary to dispose of the case in conformity with such judgment.

(1A) Where the High Court delivers a judgment in an appeal filed before it under section 35G, effect shall be given to the order passed on the appeal by the concerned Central Excise Officer on the basis of a certified copy of the judgment.

(2) The costs of any reference to the High Court or an appeal to the High Court or the Supreme Court, as the case may be which shall not include the fee for making the reference, shall be in the discretion of the Court.

Appeal to the Supreme Court [Section 35L]

(1) An appeal shall lie to the Supreme Court from —

(a) any judgment of the High Court delivered -

(i) in an appeal made under section 35G; or

(ii) on a reference made under section 35G by the Appellate Tribunal before the 1st day of July, 2003;

(iii) on a reference made under section 35H,

in any case which, on its own motion or on an oral application made by or on behalf of the party aggrieved, immediately after passing of the judgment, the High Court certifies to be a fit one for appeal to the Supreme Court; or

(b) any order passed before the establishment of the National Tax Tribunal by the Appellate Tribunal relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment.

(2) For the purpose of this chapter, the determination of any question having a relation to the rate of duty shall include the determination of taxability or excisability of goods for the purpose of assessment.

Hearing before Supreme Court [Section 35M]

(1) The provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the Supreme Court shall, so far as may be, apply in the case of appeals under section 35L as they apply in the case of appeals from decrees of a High Court :

Provided that nothing in this sub-section shall be deemed to affect the provisions of sub-section (1) of section 35K or section 35N.

(2) The costs of the appeal shall be in the discretion of the Supreme Court.

(3) Where the judgment of the High Court is varied or reversed in the appeal, effect shall be given to the order of the Supreme Court in the manner provided in section 35K in the case of a judgment of the High Court.

Sums due to be paid notwithstanding reference, etc. [Section 35N]

Notwithstanding that a reference has been made to the High Court or the Supreme Court or an appeal has been preferred to the Supreme Court, under this Act before the commencement of the National Tax Tribunal Act, 2005 sums due to the Government as a result of an order passed under sub-section (1) of section 35C shall be payable in accordance with the order so passed.

Exclusion of time taken for copy [Section 35-O]

In computing the period of limitation prescribed for an appeal or application under this Chapter, the day on which the order complained of was served, and if the party preferring the appeal or making the application was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order shall be excluded.

Transfer of certain pending proceedings and transitional provisions [Section 35P]

(1) Every appeal which is pending immediately before the appointed day before the Board under section 35, as it stood immediately before that day, and any matter arising out of or connected with such appeal and which is so pending shall stand transferred on that day to the Appellate Tribunal and the Appellate Tribunal may proceed with such appeal or matter from the stage at which it was on that day.

Provided that the appellant may demand that before proceeding further with that appeal or matter, he may be re-heard.

(2) Every proceeding which is pending immediately before the appointed day before the Central Government under section 36, as it stood immediately before that day, and any matter arising out of or connected with such proceeding and which is so pending shall stand transferred on that day to the Appellate Tribunal and the Appellate Tribunal may proceed with such proceeding or matter from the stage at which it was on that day as if such proceeding or matter were an appeal filed before it.

Provided that if any such proceeding or matter relates to an order where —

(a) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or

(b) the amount of fine or penalty determined by such order,

does not exceed ten thousand rupees, such proceeding or matter shall continue to be dealt with by the Central Government as if the said section 36 had not been substituted.

Provided further that the applicant or the other party may make a demand to the Appellate Tribunal that before proceeding further with that proceeding or matter, he may be re-heard.

(3) Every proceeding which is pending immediately before the appointed day before the Board or the Principal Commissioner or Commissioner of Central Excise under section 35A, as it stood immediately before that day, and any matter arising out of or connected with such proceeding and which is so pending shall continue to be dealt with by the Board or the Principal Commissioner or Commissioner of Central Excise , as the case may be, as if the said section had not been substituted.

(4) Any person who immediately before the appointed day was authorised to appear in any appeal or proceeding transferred under sub-section (1) or sub-section (2) shall, notwithstanding anything contained in section 35Q, have the right to appear before the Appellate Tribunal in relation to such appeal or proceeding.

Appearance by authorised representative [Section 35Q]

(1) Any person who is entitled or required to appear before a Central Excise Officer or the Appellate Tribunal in connection with any proceedings under this Act, otherwise than when required under this Act to appear personally for examination on oath or affirmation, may, subject to the other provisions of this section, appear by an authorised representative.

(2) For the purposes of this section, "authorized representative" means a person authorised by the person referred to in sub-section (1) to appear on his behalf, being —

(a) his relative or regular employee; or

(b) any legal practitioner who is entitled to practise in any civil court in India; or

(c) any person who has acquired such qualifications as the Central Government may prescribe for this purpose.

(3) Notwithstanding anything contained in this section, no person who was a member of the Indian Customs and Central Excise Service — Group A and has retired or resigned from such Service after having served for not less than three years in any capacity in that Service, shall be entitled to appear as an authorised representative in any proceedings before a Central Excise Officer for a period of two years from the date of his retirement or resignation, as the case may be.

(4) No person, —

(a) who has been dismissed or removed from Government service; or

(b) who is convicted of an offence connected with any proceeding under this Act, the Customs Act, 1962 or the Gold (Control) Act, 1968; or

(c) who has become an insolvent,

shall be qualified to represent any person under sub-section (1), for all times in the case of a person referred to in clause (a), and for such time as the Principal Commissioner or Commissioner of Central Excise or the competent authority under the Customs Act, 1962 or the Gold (Control) Act, 1968, as the case may be, may, by order, determine in the case of a person referred to in clause (b), and for the period during which the insolvency continues in the case of a person referred to in clause (c).

(5) If any person, —

(a) who is a legal practitioner, is found guilty of mis-conduct in his professional capacity by any authority entitled to institute proceedings against him, an order passed by that authority shall have effect in relation to his right to appear before a Central Excise Officer or the Appellate Tribunal as it has in relation to his right to practise as a legal practitioner;

(b) who is not a legal practitioner, is found guilty of mis-conduct in connection with any proceedings under this Act by the prescribed authority, the prescribed authority may direct that he shall thenceforth be disqualified to represent any person under sub-section (1).

(6) Any order or direction under clause (b) of sub-section (4) or clause (b) of sub-section (5) shall be subject to the following conditions, namely:—

(a) no such order or direction shall be made in respect of any person unless he has been given a reasonable opportunity of being heard;

(b) any person against whom any such order or direction is made may, within one month of the making of the order or direction, appeal to the Board to have the order or direction cancelled; and

(c) no such order or direction shall take effect until the expiration of one month from the making thereof, or, where an appeal has been preferred, until the disposal of the appeal.

Appeal not to be filed in certain cases [Section 35R]

(1) The Central Board of Excise and Customs may, from time to time, issue orders or instructions or directions fixing such monetary limits, as it may deem fit, for the purposes of regulating the filing of appeal, application, revision or reference by the Central Excise Officer under the provisions of this Chapter.

(2) Where, in pursuance of the orders or instructions or directions, issued under sub-section (1), the Central Excise Officer has not filed an appeal, application, revision or reference against any decision or order passed under the provisions of this Act, it shall not preclude such Central Excise Officer from filing appeal, application, revision or reference in any other case involving the same or similar issues or questions of law.

(3) Notwithstanding the fact that no appeal, application, revision or reference has been filed by the Central Excise Officer pursuant to the orders or instructions or directions issued under sub-section (1), no person, being a party in appeal, application, revision or reference shall contend that the Central Excise Officer has acquiesced in the decision on the disputed issue by not filing appeal, application, revision or reference.

(4) The Commissioner (Appeals) or the Appellate Tribunal or Court hearing such appeal, application, revision or reference shall have regard to the circumstances under which appeal, application, revision or reference was not filed by the Central Excise Officer in pursuance of the orders or instructions or directions issued under sub-section (1).

(5) Every order or instruction or direction issued by the Central Board of Excise and Customs on or after the 20th day of October, 2010, but before the date on which the Finance Bill, 2011 receives the assent of the President, fixing monetary limits for filing of appeal, application, revision or reference shall be deemed to have been issued under sub-section (1) and the provisions of sub-sections (2), (3) and (4) shall apply accordingly.

Definitions [Section 36]

In this Chapter —

(a) "appointed day" means the date of coming into force of the amendments to this Act specified in Part II of the Fifth Schedule to the Finance (No. 2) Act, 1980;

(b) "High Court" means, —

  (i) in relation to any State, the High Court for that State;

  (ii) in relation to a Union Territory to which the jurisdiction of the High Court of a State has been extended by law, that High Court;

  (iii) in relation to the Union Territories of Dadra and Nagar Haveli and Daman and Diu, the High Court at Bombay;

  (iv) in relation to any other Union Territory, the highest court of civil appeal for that territory other than the Supreme Court of India;

(c) "President" means the President of the Appellate Tribunal.

PRACTICAL PROBLEMS

Example 68: M/s XYZ. are in the business of supplying "Turbo-alternators" to various customers. They manufacture steam turbines in the factory, which are removed to the customer's site on payment of Central Excise Duty. They purchase duty paid alternators from the market which are delivered at the customer's site. M/s XYZ assemble both the items and fix them permanently on a platform at the site. Department demands central excise duty payable on "Turbo-alternator" when it comes into existence after being assembled on the platform embedded to the earth. Is the view taken by the department correct. Discuss with the help of case laws, if any.

Answer:

In the present case two issues are involved

(i) Whether assembly of steam turbines and duty paid alternators amounts to manufacture of turbo alternators, and

(ii) Whether such assembly results in manufacture of excisable goods.

The facts of the case are similar to the case of *Triveni Engineering and Industries Ltd. v C. CEX, 2000* (120) El,T 273 (SC)

In the present case, the Appellants were, according to specified designs, combining steam turbine and alternator by fixing them on a platform and aligning them. As a result of this activity of the Appellants, an new product, turbo alternator, came into existence, which has a distinctive name and use different from its components. Therefore, the process involved in fixing steam turbine and alternator and in coupling and aligning them in a specified manner to form a turbo alternator, a new commodity, is nothing but a manufacturing process.

Though the process of assembling results into a new commodity and therefore is a process amounting to manufacture, yet the turbo alternator set (known in the market as such) comes into existence only when a steam turbine and alternator with all their accessories are fixed at the site. Further, in order to be brought in the market the turbo would not remain turbo alternator. Thus, its is obvious that without fixing to the ground the turbo alternator does not come into being. The installation or erection of turbo alternator on the platform specially constructed on the land cannot be treated as a common base, therefore, such alternator would be immovable property. Accordingly, such activity could not be considered as 'excisable goods'.

Example 69: Snow White Ltd. Manufactures paper and in the course of such manufacture, "waste paper" is produced (paper being the main product and dutiable goods). The Central Excise Tariff Act, 1985 (CET) was amended w.e.f. 1-3-1995, so as to include waste paper. White Ltd. was issued a show cause notice by the Central Excise Officer, demanding duty of ₹ 2 lakhs on waste paper produced during October, 1994 to February, 1995, but cleared during April-May, 1995. A reply is due to be filed immediately to the notice. As Counsel of Snow White Ltd. you we required to advise the company about –

(i) The legality and validity of the proposed levy and collection of duty on waste paper for the period prior to 1-3-1995; and

(ii) State (with the help of decided cases) the reasons for your advice/opinion.

Answer:

The issue involve in the given case is determination of taxable event for the purpose of levy of excise duty.

As per section 3 of the Central Excise Act, 1944, the taxable event for levy of Central Excise is "manufacture of excisable goods". The date for determination for rate of duty and tariff valuation is the date of actual removal of the goods from the factory or warehouse.

However, there must be a levy of duty of excise at the time of manufacture and only then, the duty can be collected at the time of removal as has already been held in Vazir Sultan Tobacco Industry's case 1996 (83) ELT 3(SC).

Therefore, the waste paper produced prior to the levy will not be chargeable to duty of excise even though it has been cleared after such levy and the proposed show cause notice demanding ₹ 2 lakhs of excise duty on such waste paper is invalid and illegal and liable to be quashed.

Example 70: Kagaz Karkhana Ltd., manufactures paper in the year 2012-13, it embarked on a major expansion programme, and for the purpose, fabricated at site, 75% of the portion of papermaking machine and procured (paying excise duty) the remaining parts of the papermaking machine from other suppliers. Having done so, it assembled all the parts together into a paper-making machine at site. The erection and installation was completed during November, 2012 and the machine was firmly fastened to the earth, with the help of bolts, nuts and grouting material on a concrete bed, to prevent rattling and ensure wobble-free operation and presently the machine is functional and operating. During July, 2015, the Central Excise authorities served the company a show cause demanding excise duty of ₹ 5 crores, on the paper-making machine, alleging that the activity resulted in manufacture of excisable goods, falling under chapter 84 of CETA. The company engages you as 'counsel' to represent them and desires to contest the case on the grounds :

(i) That the activity of erection and installation was not manufacture,

(ii) That the activity resulted in "immovable property" emanating at site and

(iii) That the demand is time-barred

You are required to discuss the tenability or otherwise of the contentions of the notice client and advice them drawing support from the judicial decision.

Answer:

There are three issues involved in the present case:

(i) Whether the activity of erection and installation was not manufacture,

(ii) Whether the activity resulted in "immovable property" emanating at site and

(iii) Whether the demand is time-barred

In respect of the first issue, it is to be noted that the excise duty is levied on the excisable goods manufactured in India, and hence it will not be attracted where goods are not produced from the manufacturing process.

A commodity is said to be manufactured if by application of the process its identity is changed and it is known in the market as a separate and distinct commodity having separate name, character and use.

The assembly of parts results in paper-making machine which has distinct identity, name and character and use and hence such assembly amounts to manufacture.

The second issue is whether erection and installation of such machine on a concrete base results in a immovable property. The Supreme Court, in Sirpur Paper Mills v C.C.Ex., Hyderabad 1998(97) ELT 3 (SC), has held that papermaking machine if assembled and erected at site and embedded in concrete base to ensure wobble free operation will not become an immovable property. The machine can be dismantled from its base and sold in parts. Hence, the assessee's first two contentions are untenable and incorrect as the activity has resulted in the manufacture of goods and there is no immovable property brought into existence and assembly operations are liable to duty of excise.

The third issue is whether the demand notice is time barred. Under section 11A of the Central Excise Act, 1944, the extended period of limitation can be invoked only when there is a fraud, collusion, willful misstatement, suppression of facts or contravention of the provisions of the Act with an intent to evade the payment of duty of excise. If the manufacturing activity of paper-making machine was known to the department then the department cannot invoke the extended period of limitation. Hence, the contention of the assessee is an arguable point and the same is legally tenable.

Example 71: Regarding the applicability of excise duty, Computers are covered under Heading no 84.71 of the First schedule to the Central Excise Tariff Act, 1985 which describes computers as automatic data processing machines. XYZ Ltd. has undertaken upgradation of its computers both in terms of storage capacity and processing speed by increasing the hard disc capacity, RAM, changing of processor chip from 386 to 486 and in certain cases from Pentium III to Pentium IV. The Department's contention is that new goods with a different name character and use have come into existence and the upgraded products are chargeable to excise duty. Discuss in the light of provision of section 2(f) of the Central Excise Act, 1944 relating to "manufacture" whether this stand of the Department is justified.

Answer:

The computers covered under heading No. 84.71 of the Schedule to the Central Excise Tariff Act, 1985 are described as automatic data processing machines. An automatic data processing machine will be known by this name, irrespective of its capacity of storage and processing, which may be enhanced by increasing the hard disk capacity. RAM or by changing the mother board or the processor chip. However, it cannot be said that new goods with a different name, character and use have come into existence, which can be subjected to duty again.

Accordingly, upgrading of old and used computer systems would not amount to manufacture, in so far as the upgradation does not bring into existence goods with a distinct new name, character and use.

Example 72: Full exemption is granted by exercising Central Excise Notification which e xplains all products of printing industry including newspapers and printed periodicals." A manufacturer, who is manufacturing cardboard cartons and subsequently doing varied printing on them, claims benefit of the said exemption notification on the ground that every material on which printing is done becomes a product of the printing industry. Is the claim of the manufacturer justified? Give reasons for your view.

Answer:

The cited Central Excise exemption notification grants full exemption to – "all products of printing industry including newspapers and printed periodicals". The products in respect of which exemption is claimed are cardboard, cartons although subsequently varied printing is done on them. These products relate to the packaging industry. The mere fact that printing is done on these products will not render these products as the products of the printing industry.

Accordingly, the products of the packaging industry shall not be entitled to the exemption granted to "all products of printing industry including newspapers and printed periodicals".The case in support is *Rollatainiers Ltd. v UOI* (1994) 72 ELT 793(SC).

Example 73: How would you arrive at the assessable value for the purpose of levy of excise duty from the following particulars-Cum-Duty selling price exclusive of sales Tax ₹ 10,000, Rate of excise duty applicable to the product - 12.5% (including education cess), Trade discount allowed – ₹ 1,200, Freight ₹ 750 from factory to buyer place.

Answer:

In computation of assessable value for the purpose of levy of excise duty, trade discount and freight are allowed as deductions.

Thus,

Net price	=	Selling Price – (Trade Discount + Freight)
	=	₹ 10,000 – (1,200 + 750)
	=	₹ 8,050

Since the price is inclusive of excise duty @12.5%,

Therefore,—

Assessable Value	=	₹ 8,050 x 100/112.5
	=	₹ 7,156
Excise Duty will be ₹ 8,050 – ₹ 7,156	=	₹ 894

Check : 12.5% of ₹ 7,156 is ₹ 894

Example 74: X Ltd. is engaged in the manufacture of 'paracetamol' tablets that has an MRP of ₹ 9 per strip. The company cleared 1,00,000 tablets and distributed as physician's samples. The goods are not covered by MRP, but the MRP includes 12.5% Excise Duty and 2% CST. If the cost of production of the tablet is 40 paise per tablet, determine the total duty payable.

Answer:

If the product is not covered under MRP provisions, valuation provisions under section 4A do not apply. In that case, valuation is required to be done as per Central Excise Valuation Rules.

As per the CBEC's circular, any physicians samples or other samples distributed free of cost are to be valued under Rule 11 read with Rule 8 of Central Excise Valuation Rules, 2000.

As per Rule 8, such samples are to be valued at 110% of cost of production or manufacture. The given cost of production is 40 Paise, Assessable Value will be 44 Paise. Therefore, duty payable @ 12.5% on 44 paise = 12.5% × 0.44 = 0.055 paise per tablet.

Example 75: M/s. A.U.L. avail of CENVAT credit of the duty paid on the inputs namely, steel sheets. The scrap generated during the manufacture of their final product was cleared by them without payment of duty. Subsequently the Department raised a demand of Excise duty on waste and scrap. M/s. A.U.L. accepted the duty liability, but contended that the price at which waste and scrap had been sold should be considered to be cum-duty price and assessable value should be determined after deducting the element of excise duty. The contention of the Department is that as no central Excise duty was paid by them while clearing the scrap, no deduction on account of excise duty is available to M/s. A.U.L.

Answer:

The facts of the given case are similar to those decided by the Supreme Court in *C.C.Ex. v Maruti Udyog Ltd.* (2002) 141 ELT 3 (SC) in the said case, the department raised duty demand on waste and scrap and the price realized by the assessee was taken as the assessable value. The assessee contended that the price of such waste and scrap was includive of excise duty. The Supreme Court decided the issue in favour of the assessee. Accordingly, in the given case, as the Department has raised duty demand on waste and scrap, the price collected by M/s. A.U.L. will be considered as the Cum-Duty price and it shall be deemed that the element of excise duty is already included in such price. The manufacturer will therefore be entitled for deduction on account of such price. Thus the assessable value will be worker out as under –

$$\text{Assessable value} = \frac{(\text{Cum-Duty Price} - \text{Permissible Deduction}) \times 100}{100 + \text{Rate of Duty}}$$

Example 76: State whether the following elements are to be included or not as part of the 'Transaction value' under section 4 of the Central Excise Act, 1944.

(i) Erection and commissioning charges

(ii) System software etched in the computer system

(iii) Cylinder holding charges

(iv) After-sales warranty charges

Answer:

(i) Any payment made by buyer to assessee is includible in assessable value only if it is in 'connection' with sale. In case of erection and commissioning charges for erecting machinery at site, these are incurred after goods are removed from the factory. These may be in 'relation' to sales but are not in 'connection' with sales as there is no 'cause and effect' relationship between the two. Hence these are not includable in assessable value. This is also confirmed *vide* CBE&C Circular No. 643/34/2002-CX, dated 1-7-2002.

(ii) A computer manufacturer loads bought out computer software on computer while selling. Thus, the system software is loaded on computer while computer is cleared from the factory. Computer software as such is exempt from duty. Department had earlier clarified that value of computer software etched or loaded on computer will be includible. However, if computer software is supplied separately on floppy disc or tapes, its value will not be includible. [However, as per CBE&C circular dated 28-2-2003, value of computer software will not be includible in assessable value of computer].

(iii) In case of durable and returnable containers, the container is returnable after the gas or other material inside is used. Often, manufacturing companies take some deposit and charge some rent for the container. These are 'cylinder holding charges'. CBE&C, *vide* its Circular No. 643/34/2002-CX, dated 1-7-2002, has clarified that rental charges or cost of maintenance of reusable metal containers like cylinders etc. are to be included in assessable value. This view is correct as such rental charges and the sale of gas are so intrinsically connected that there can be no sale without such charges.

(iv) Compulsory after sales warranty charges are includible as the sale goods and such charges are inseparable. However, optional service charges are not includable as there is no connection between the sale of goods and the optional service charges.

Example 77: A Ltd., a manufacturer to tyres was extending a warranty discount on any tyres that, were defective. The scheme of warranty discount operated thus, the customers lodged their claim with regard to any defects in the tyres. Such claims were then scrutinized by a Technical Committee of A Ltd., which would decide the amount of refund due to the customer on the basis of the reduction in the normal life of tyre attributable to the defect. This refund was to be given by the Technical Committee. This practice was being followed by A Ltd. for the last 15 years. A Ltd. claimed the 'warranty discount' as a Trade discount which is deductible in computing the assessable value of the tyres. Is this correct? Discuss in the light of the provisions under Section 4 of the Central Excise Act, 1944.

Answer:

According to section 4 of the Central Excise Act, 1944, regarding discounts, transaction value does not make a direct reference. Now actually the excise duty is paid/payable on the net price of the goods after deduction of discounts. If in any transaction discount is allowed in accordance with normal practice of trade and it is passed on to the buyer, stile inclusion of such discount is not justified. However, the said amount to be allowed as deduction must be in the nature of discount.

From the facts of the above case, the manufacturer was extending warranty discount on any tyres that were defective. Though this was known as discounts, but it was only a compensation for defects in tyres, which was given to the customers. Hence, it will not be allowed as deduction from the transaction value as was held in *GOI v MRF* (1995) 77 ELT 433(SC).

Example 78: How would you arrive at the assessable value for the purpose of levy of excise duty from the following particulars :

i. Cum-duty selling price exclusive of sales tax ₹ 20,000

ii. Rate of excise duty applicable to the product 12.5%

iii. Trade discount allowed ₹ 2,400

iv. Freight ₹ 1,500

Answer:

Trade discount of ₹ 2,400 and freight of ₹ 1,500 are allowed as deductions. Hence, net price will be ₹ 16,100 [₹ 20,000 – ₹ 2,400 – ₹ 1,500].

Since the price is inclusive of excise duty of 12.5%, Excise Duty will be ₹ 1,788.89 (₹ 16,100 × 12.5)/112.5) and Assessable Value will be ₹14,311.11 [₹16,100 – ₹1,788.89]

Example 79: M/s U.T.A. manufacture welding electrodes which are put first in Polythene bags and then packed together in cardboard cartons. They sell electrodes at the factory gate packed in cardboard cartons whereas such electrodes are also packed in wooden boxes when sold to their customers located at outstations. Is the department justified to include the cost of wooden boxes in the assessable value of the welding electrodes? Discuss with the help of case laws, if any.

Answer:

The new Section 4 of the Central Excise Act, 1944, does not make any specific reference to packing charges. In normal commercial transactions the price of goods charged includes the cost of packing charges. The charges that are recovered on account of packing are obviously the charges in relation to sale of goods under assessment and will form the part of transaction value. Whatever be the nature of packing that is whether the packing is primary or secondary or special or packing for the purpose of transportation, the cost of such packing shall be includible.

In light of the new Section 4, the earlier case laws hold no significance now.

Example 80: A1 Ltd., manufactures three soft drinks namely Coke, Pep, and Maaza. Coke was sold only to A2 Ltd., a subsidiary company of A1 Ltd. Pep was sold to A3 Ltd., where the Managing Director of A1 Ltd., is a Manager. Maaza was sold to A Ltd, who is sole distributor of A1 Ltd., and was coming under same management of A1 Ltd.

Determine the assessable value of the three products in the hands of A1 Ltd. on the basis of the following information:

Price of A1 Ltd to A2 Ltd. is	₹ 1,00,000
Price of A1 Ltd. to A3 Ltd. is	₹ 50,000
Price of A1 Ltd. to A Ltd. is	₹ 20,000
Price of A2 Ltd. to Consumer is	₹ 1,20,000
Price of A3 Ltd. to Consumer is	₹ 60,000
Price of A Ltd. to consumer is	₹ 30,000

Note: sale prices are exclusive of duties and taxes.

Answer: (Rule 10)

Statement showing computation of Assessable value for A1Ltd.

Particulars	**Assessable value (₹)**	**Relation ship**	**Applicable Rule**	**Remarks**
Coke sold to A2 Ltd.	1,20,000	Relative	Rule 10 of the Valuation Rules, 2000	Price at which relative buyer, sells goods in the open market to non relative buyer
Pep sold to A3 Ltd.	50,000	Non relative	--	Relation ship will come into exist only when there is holding and subsidiary concept persist.
Maaza sold to A Ltd.	20,000	Non relative	--	Relation ship will come into exist only when there is holding and subsidiary concept persist.
Total	1,90,000			

Example 81: M/s R.M.T. Industries manufactures cigarettes which are sold in wholesale, exfactory, at cum-duty price to wholesale dealers. The price charged to all the dealers from the cigarettes is the same. However, the dealers who purchase on credit are required to deposit interest free security with M/s R.M.T. The department has demanded duty from M/s R.M.T. contending that they had earned notional interest in the security deposit received from the dealers which should be included in the assessable value of the cigarettes being the additional consideration. Duty on cigarettes is being charged on advalorem basis. Discuss the stand taken by the department with decided case laws, if any.

Answer:

The facts of this case are similar to the case of *VST Industries Ltd. v C.C.Ex.* (1998) 97 ELT 395 (SC).

In the instant case the interest free deposit scheme was introduced by the assessee because of commercial consideration of covering the risk of credit sales, no special consideration flowing form the assessee to the buyer keeping tile deposit, the Supreme Court held that the notional interest cannot be included in the assessable value.

Example 82: Determine the value on which Excise duty is payable in the following instances. Quote the relevant section/rules of Central Excise Law.

(a) A. Ltd. sold goods to B Ltd., at a value of ₹ 100 per unit in turn, B Ltd. sold the same to C Ltd. at a value of ₹ 110 per unit. A Ltd. and B Ltd. are related, whereas B Ltd. and C Ltd. are unrelated.

(b) A Ltd. and B. Ltd. are inter-connected undertakings, under section 2(g) of MRTP Act. A Ltd. sells goods to B Ltd. at a value of ₹ 100 per unit and to C Ltd. at ₹ 110 per unit, who is an independent buyer.

(c) A Ltd. sells goods to B Ltd. at a value of ₹ 100 per unit. The said goods are captively consumed by B Ltd. in its factory. A Ltd. and B Ltd. are unrelated. The cost of production of the goods to A Ltd. is ₹ 120 per unit.

(d) A Ltd. sells motor spirit to B Ltd. at a value of ₹ 31 per litre. But motor spirit has administered price of ₹ 30 per litre, fixed by the Central Government.

(e) A Ltd. sells to B Ltd. at a value of ₹ 100 per unit. B Ltd. sells the goods in retail market at a value of ₹ 120 per unit. The sale price of ₹ 100 per unit is wholesale price of A Ltd. Also, A Ltd. and B Ltd. are related.

(f) Depot price of a company are -

Place of removal	Price at depot on 1-1-2016	Price at depot on 31-1-2016	Actual sale price at depot on 1-2-2016
Amritsar Depot	₹ 110 per unit	₹ 105 per unit	₹ 115 per unit
Bhopal Depot	₹ 120 per unit	₹ 115 per unit	₹ 125 per unit
Cuttack Depot	₹ 130 per unit	₹ 125 per unit	₹ 135 per unit

Additional information : (i) Quantity cleared to Amritsar Depot – 100 units, (ii) Quantity cleared to Bhopal Depot – 200 units, (iii) Quantity cleared to Cuttack Depot – 200 units, (iv) The goods were cleared to respective depots on 1-1-2016 and actually sold at the depots on 1-2-2016.

Answer:

(a) Transaction value ₹ 110 per unit (Rule 9 of Valuation value Rules). [Sale to unrelated party].

(b) Transaction value ₹ 100 per unit for sale to B and ₹ 110 for sale to C – Rule 10 read with Rule 4 [Note that inter connected undertaking will be treated as 'related persons' for purpose of excise valuation only if they are 'holding and subsidiary' or are 'related person' as per any other part of the definition of 'related person'. Note that A is selling directly to C as per the question, and not through B Ltd].

(c) Transaction value will be ₹ 100. – section 4(1)—Incase of sale to unrelated person, question of cost of production does not arise.

(d) Transaction value ₹ 31. – section 4. – Since the goods are actually sold at this price, administered price is not considered.

(e) Transaction value ₹ 120 per unit – Rule 9 read with section 4 of Central Excise Act. Sale to an unrelated buyer. [Under new rules, there is no concept of 'wholesale price and retail price']

(f) Under Rule 7, the price prevailing at the Depot on the date of clearance from the factory will be the relevant value to pay Excise duty.

Therefore –

(i) Clearance to Amritsar depot will attract duty based on the price as on 1-1-2016. Transaction value ₹ 110x 100 units = ₹ 11,000

(ii) Clearance to Bhopal depot, so depot price on 1-1-2016. Therefore, transaction value ₹120 × 200 units = ₹ 24,000

(iii) Clearance to Cuttack Depot, depot price on 1-1-2016. Transaction value ₹ 130x120 units = ₹ 26,000. Note the relevant date is 1-1-2016, since the goods were cleared to the depots on that date. No additional duty is payable even if goods are later sold from depot at higher price.

Example 83: Having regard to the provisions of section 4 of the Central Excise Act, 1944, compute/derive the assessable value of excisable goods, for levy of duty of excise, given the following information :

Cum-duty wholesale price including sales tax of ₹ 2,500	₹ 15,000
Normal secondary packing cost	₹ 1,000
Cost of special secondary packing	₹ 1,500
Cost of durable and returnable packing	₹ 1,500
Freight	₹ 1,250
Insurance on freight	₹ 200
Trade discount (normal practice)	₹ 1,500
Rate of C.E. duty as per C.E. Tariff	12.5% Advalorem

State in the footnote to your answer, reasons for the admissibility or otherwise of the Deductions.

Answer:

The assessable value from cum-duty price can be worked out by the under-mentioned formula

$$\text{Assessable Value} = \frac{(\text{Cum-Duty Price} - \text{Permissible Deduction}) \times 100}{100 + \text{Rate of Duty}}$$

Computation of Assessable Value

	₹	₹
Cum-duty price		15,000
Less : Deductions (See Notes)		
Sales tax	2,500	
Durable & returnable-packing	1,500	
Freight	1,250	
Insurance	200	
Trade-Discount	1,500	6,950
		8,050
Less: Central Excise Duty thereon @ 12.5%		
8,050 × 12.5/112.5		894.44
Assessable value		**7,155.56**

Notes :

1. The transaction value does not include Excise duty, Sales tax and other taxes.
2. The Excise duty is to be charged on the net price, hence trade discount is allowed as deduction.
3. With regards to packing, all kinds of packing except durable and returnable packing is included in the assessable value. The durable and returnable packing is not included as the such packing is not sold and is durable in nature.
4. Freight and insurance on freight will be allowed as deduction only if the amount charged is actual and it is shown separately in the invoice as per Rule 5 of the Central Excise Valuation Rules, 2000.

Example 84: Explain whether the following items can be included in/excluded from the transaction value under section 4 of the Central Excise Act, 1944.

(1) Collection expenses incurred in respect of empty bottles for filling aerated waters from the premises of buyers to the manufacturers.

(2) Delivery and collection charges of gas cylinders and collection of empty cylinders.

(3) Interest notional or real accruing on deposits for sale/return of gas cylinders as well as rentals.

(4) Cash discount known at the time of clearance of goods but not availed by the customer.

(5) Value of system software in case of computers.

Answer:

(1) Transaction value includes any amount charged in addition to the price of the goods by reason of or in connection with the sale. Since collection expenses are incurred by reason of or in connection with the sale, it would be included in the transaction value.

(2) CBEC has vide Circular No. 643/34/2002, dated 1-7-2002 clarified that delivery and collection charges of gas cylinders are by reason of or in connection with the sale of goods and therefore, the same would be included in the transaction value.

(3) The interest on advances taken from the customers would not be included in the assessable value, unless the receipt of such advance had no effect of depressing the wholesale price.

In *VST Industries Ltd. v C.C.Ex, Hyderabad* 1998 (97) ELT 395(SC), where interest free deposits were taken because of commercial consideration of covering the risk of credit sales, no special consideration flowing from the assessee to the buyer keeping the deposit was found and the Supreme Court held that notional interest cannot be included in the assessable value.

(4) However, in such case, the burden of proof lies on the Department to prove a nexus between the fact of advance taken and the depression in the value.

(5) The transaction value is the price actually paid or payable for the goods. In the given situation, as the case of cash discount has not been passed on to tile customer, it will not be allowed as deduction.

As per tile CBEC & Circular No. 644/35/2002-CX, dated 12-7-2002 the Software can be of the following types – *Systems software/Operating software* – which is designed to control the operation of the computer system.

Application software – Which is developed for specific applications only.

Valuation of goods is done in the form in which it is cleared. Therefore, computer *systems* will be valued by including the value of the software loaded on the hard disc. No distinction is to be made between an 'operating software' and an 'application software'.

Example 85: Thunder TV Ltd is engaged in the manufacture of colour television sets having its factories at Bangalore and Pune. At Bangalore the company manufactures picture tube; which are stock transferred to Pune factory where it is consumed to produce television sets. Determine the Excise duty liability of the captively consumed picture tubes from the following information:

Direct material cost (per unit)	₹	600
Indirect material	₹	50
Direct Labour	₹	100
Indirect Labour	₹	50
Direct Expenses	₹	100
Indirect Expenses	₹	50
Administrative overheads	₹	50
Selling and Distribution overheads	₹	100

Additional Information:

Profit margin as per the Annual Report for the company for 2014-2015 was 15% before income tax.

(i) Material cost includes Excise duty paid ₹ 100.

(ii) Excise duty rate applicable is 12.5%.

Answer:

As per Rule 8 of The Central Excise Valuation (Determination of Price of Excisable Goods) Rules, 2000, the valuation of captively consumed goods is 110% of the cost of production. The cost of production of goods would include cost of material, labour cost and overheads including administration cost and depreciation etc.

The cost of material would be net of excise duty if CENVAT credit is availed in respect of such inputs.

Accordingly, the assessable value will be determined as follows :

Raw materials Cost (net of excise duty)	₹	500
Indirect material	₹	50
Direct Labour	₹	100
Indirect Labour	₹	50
Direct Expenses	₹	100
Indirect Expenses	₹	50
Administrative overheads (assumed related to production activity)	₹	50
Total cost of production	₹	900
Assessable value	₹	990
(i.e. 110% of the cost of production)		

Total Duty Liability = ₹ 990 x 12.5/100 = ₹ 123.75

The raw material cost has been taken at ₹ 500 after deducting the duty element assuming that the CENVAT credit has been availed.

Example 86: Mrs. E fails to pay Excise Duty of ₹ 60,000 on the goods cleared in February by 5th March of 2015. The assessee, Mrs. E, is owner of a SSI unit. What is the interest payable under Rule 8 of Central Excise Rules, 2002 if the duty was actually paid on 10th May of 2015?

Answer:

Interest = ₹ 60,000 x 18/100 x 40 days /365 days = ₹ 1,184

Note: w.e.f. 1-4-2011 rate of interest is @18% p.a. simple interest.

Example 87: From the following data, determine the CENVAT allowable if the goods are produced or manufactured in a FTZ or by a 100% EOU and used in any other place in India.

Assessable value : ₹ 770 per unit,

Quantity cleared 77,770 units,

BCD — 10%,

CVD — 12.5%

Answer:

As per Rule 3 of CENVAT Credit Rules, 2002 the following formula is to be used if a unit in DTA purchases goods from EOU –

Assessable value	= ₹ 770	
Add: 50% on BCD 10%	= ₹ 38.50	(10% x 50%= 5% on ₹ 770)
Balance	= ₹ 808.5	
Add: CVD 12.5%	= ₹ 101.06	(12.5% on ₹ 808.50)

CENVAT Credit allowed to the extent of CVD. Therefore, ₹ 101.06 per unit for 77,770 units is ₹ 78,59,436.

Example 88: X Ltd. purchased a Boring-Drilling machine at a cum-duty price of ₹ 37,27,360. The Excise duty rate charged on the said machine was @12.36%. The machine was purchased on 1.4.2013 and disposed of on 30.6.2015 for a price of ₹ 12,00,000 in working condition as second hand machinery (Excise duty @12.5%). The company was claiming depreciation @25% following Straight Line Method on the value of machine. Using the said information, answer the following questions:

What is the excise duty paid on the machine?

What is the CENVAT credit allowable under CENVAT Credit Rules?

What is the amount of CENVAT credit reversible or duty payable at the time of clearance of the said machinery?

Answer:

(a) Excise duty is ₹ 4,10,023 (i.e.₹ 37,27,360 × 12.36/112.36)

(b) Upto 50% allowed as CENVAT credit in the year 2013-14 on 1-4-2013 and balance CENVAT credit in the year 2014-15 on 1-4-2014.

(c)

Year	**No. of quarter**	**Workings**
2013	3	April – December
2014	4	January – December
2015	2	January – June
Total	9	

Particulars	**Amount (₹)**	**Workings**
Cenvat credit on capital goods	4,10,023	
Less: Reduction	(46,128)	₹ 2,05,012 × 2.5% × 9 qtrs.
	(25,627)	₹ 2,05,012 × 2.5% × 5 qtrs.
Amount to be paid	3,38,268	
Or		
Excise duy on transaction value	1,50,000	₹ 12 lakhs × 12.5%
Amount to be paid	3,38,268	Whichever is higher

Example 89: Prepare a Cenvat account in the books of A Ltd., and determine the balance as on 30-9-2015 from the following data :

Opening balance as on 1-4-2015 ₹ 47,000.

Inputs received on 04-04-2015 involving excise duty paid ₹ 14,747

Purchased a lathe for ₹ 1,16,000-cum duty price @ excise duty rate of 12.5% on 5-4-2015 and received the lathe into the factory on 5-12-2015.

On 6-4-2015 paid excise duty on final products @12.5% through Cenvat A/c (cum duty price of the goods ₹ 2,32,000).

Inputs cleared as such to a job worker on 1-4-2015 not returned in 180 days, quantity 1,000 Kgs; Asssessable value ₹ 2 lacs; ED @ 12.5% of the above, 50% of the inputs were received on 1-10-2015.

Common inputs were used in a product, which was exempted from payment of duty cleared at a price of ₹ 100/unit, which included taxes of ₹ 20/unit ; quantity cleared 1,000 units.

On 7-4-2015 duty paid on inputs amounting to ₹ 17,867 was taken credit for in the Cenvat A/c as ₹ 17,687.

Answer:

CENVAT Credit Receivable Account in the Books of A Ltd., as on 30-9-2015

Date	Particulars	Debit (₹)	Credit (₹)
1-4-2015	To Opening Balance	47,000	
4-4-2015	To Sundry Creditors	14,747	
6-4-2015	By Excise duty paid on Final product [(₹2,32,000 ÷112.5)×12.5]		27,778
7-4-2015	To Sundry Creditors	17,687	
30-9-2015	To Sundry Creditors (Credit short taken on 7-4-2015)	180	
30-9-2015	By Reversal of Cenvat Account (6% Amount on Exempted goods)		6,180
30-9-2015	By Reversal of Cenvat Account (Amount equal to duty on inputs not return within 180 days)		24,720
	By Balance Carry Forward		22,936

Notes :

(i) Since capital goods (lathe) was received only on 5-12-2015, the credit is permissible only on 5-12-2015 and not before that date.

When 50% of inputs are received on 1-10-2015 (sent on job work), the credit is allowable for 50% only on 1-10-2015.

(iii) Where goods are exempted, an 'amount' is payable @ 6% on sale price less taxes.

(iv) For wrong amount of credit, rectification entry is passed.

(v) The 'amount' paid on 30-9-2015 is reversal of Cenvat credit. It is not 'excise duty'. Hence, a separate account 'Reversal of Cenvat Account' or "Payment of 'Amount' under Central Excise Rules" may be opened. At the year end, the balance may be transferred to expenses account. Strictly legally, it is not 'excise duty' paid.

Example 90: A manufacturer brings some inputs valued at ₹ 25,000 on which duty of ₹ 5,000 has been paid @ 20%. Subsequently, the manufacturer sold the input as such, which goods he sold for ₹ 30,000. What is the duty payable by the manufacturer if –

1. Rate of duty on the date of clearance on inputs was 25%.
2. Rate of duty on the date of clearance on input was 10%.

Answer:

Rule 3(5) of the CENVAT Credit Rules, 2004, provides that when inputs are removed as such from the factory, the amount of duty payable shall be equivalent to the credit availed in respect of such inputs. The sale price has no bearing on the duty payable if the inputs are cleared as such from the factory.

Hence, different rate of excise duty on different date is not relevant in this case.

Therefore, excise duty liability should be ₹5,000.

Example 91: ABC and Co. are manufacturing the products specified below from excise duty paid high density polyethylene granules. Part of the goods are captively consumed and other part of the goods cleared for home consumption in India and for export to Bhutan and United Kingdom. The effective rate of duty, and the value of clearances during the preceding year 2014-15, and the current assessment period 2015-2016 are as follows –

1. Rate of duty —

Product 'A' – 12.50%. Product 'B' – 12.50%. Product 'C' (Waste & Scrap)- Exempt from duty.

2. Value clearances in 2014-15 –

Product 'A'–

(a) Clearance for home consumption – ₹ 130 Lakhs.

(b) For captive consumption in the manufacture of excisable goods –₹ 135 lakhs.

(c) Exports to Bhutan – ₹ 35 lakhs

(d) Exports to UK under bond – ₹ 100 lakhs

Product 'B'—

(a) Clearance for home consumption – ₹ 80 lakhs

(b) For captive consumption in the manufacture of excisable goods – Nil

(c) Exports to Bhutan – ₹ 50 lakhs.

(d) Exports to UK under bond – ₹ 200 lakhs.

Product 'C'–

(a) Clearance for home consumption – ₹ 40 lakhs

(b) For captive consumption in the manufacture of excisable goods – ₹ 20 lakhs

(c) Exports to Bhutan – Nil

(d) Exports to UK – Nil

3. Value of clearances during current year *i.e.* 2015-16 —

Product 'A'–

(a) Clearance for home consumption – ₹ 50 lakhs.

(b) For captive consumption in the manufacture of excisable goods – ₹ 40 lakhs

(c) exports to Bhutan – Nil

(d) Exports to UK under bond ₹ 50 lakhs.

Product 'B'–

(a) Clearance for home consumption – ₹ 80 lakhs

(b) For captive consumption in the manufacture of excisable goods- Nil

(c) Exports to Bhutan – ₹ 50 lakhs.

(d) Exports to UK under bond – ₹ 100 lakhs.

Product 'C'–

(a) Clearance for home consumption – ₹ 50 lakhs.

(b) For captive consumption in the manufacture of excisable goods- Nil

(c) Exports to Bhutan – ₹ 50 lakhs.

(d) Exports to UK under bond – ₹ 100 lakhs.

Advise the manufacturers as to whether they are entitled to small scale exemption and the amount of excise duty payable for their clearances during 2015-16, if the assessee intends to avail Cenvat credit.

Answer:

Turnover in 2014-15 for purpose of considering SSI exemption limit is as follows –

Product A – ₹ 165 lakhs [130 + 35]

Product B – ₹ 130 lakhs [80 + 50]

Product C – ₹ 40 lakhs.

If final product is exempt from duty, the goods used for captive consumption are liable to duty. Therefore, total turnover during 2014-15 is ₹ 335 lakhs.

Since total turnover does not exceeds ₹ 400 lakhs, the assessee is entitled to exemption in 2015-16 and has to pay normal duty @ 12.50% on ₹ 130 lakhs (₹ 280 lakhs - ₹ 150 lakhs)= ₹ 16.25 lakhs

If assessee avails cenvat credit, duty payable will be = 12.50% of ₹ 280 lakhs = ₹ 35 lakhs

Example 92: The value of excisable goods viz. Iron and Steel articles manufactured by M/s. Alpha Ltd., was ₹ 170 lakhs during the financial year 2015-16. The goods attract 12.50% ad valorem duty. Determine the excise duty liability when the assessee opts for 'CENVAT' and 'opts for not to avail CENVAT' under SSI exemption notifications respectively.

Answer:

If the assessee does not avail Cenvat, duty payable will be ₹ 2.50 lakhs. [Nil for first 150 lakhs and ₹2.50 lakhs for subsequent ₹ 20 lakhs]. If assessee avails Cenvat credit, duty payable will be ₹ 21.25 lakhs i.e. (170 × 12.50%).

Example 93: M/s NML, a unit registered as a small scale unit, manufactures coloured television sets under the brand name "SONY" in India, which brand name is owned by a Foreign Company. M/s NML has the exclusive right to use the Brand name "SONY" in India.

Explain briefly with reference to Notifications governing Small Scale Industrial Undertakings under the Central Excise Act, 1944 and the Rules, whether the manufacturer in this case M/s NML is entitled to the benefit of the exemption as applicable to small scale industrial undertakings.

Answer:

The benefit of SSI exemption is not applicable incase an SSI unit is manufacturing under the brand name or trade name of another person whether registered or not.

In the present case, since NML is manufacturing the TV sets under the brand name of "Sony", it will not be entitled for the benefit of SSI exemption.

Case in support is *Namtech Systems Ltd. v C.C.Ex, (Tribunal)*.

Example 94: An assessee has factory in Kolkata. As a sales policy, he has fixed uniform price of ₹ 2,000 per piece (excluding taxes) for sale anywhere in India. Freight is not shown separately in his invoice. During F.Y. 2014-15, he made following sales: (i) Sale at factory gate in Kolkata – 1,200 pieces – no transport charges; (ii) Sale to buyers in Gujarat – 600 pieces, actual transport charges incurred ₹ 28,000; (iii) Sale to buyers in Bihar – 400 pieces, actual transport charges incurred – ₹ 18,000, (iv) Sale to buyers in Kerala – 1,000 pieces, actual transport charges ₹ 54,800. Find assessable value.

Answer:

The total pieces sold are 3,200 (1,200 + 600 + 400 + 1000). The actual total transport charges incurred are ₹ 1,00,800 (Nil + 28,000 + 18,000 + 54,800). Thus, equalized (averaged) transport charges per piece are ₹ 31.50. Hence assessable value will be ₹ 1968.50 (₹ 2,000 – ₹ 31.50). This will apply to all 3,200 pieces sold by the manufacture.

Study Note - 3

CENVAT CREDIT

This Study Note includes

3.1 BACKGROUND OF CENVAT CREDIT

Excise and Service tax are central taxes, expected to be consumption based taxes to the extent practicable. Till the goods or service is finally consumed, the burden of excise duty and service tax is passed on to next buyer, who gets credit of the tax and excise duty paid by the supplier/ service provider. Thus, effectively, tax is paid on value added at each stage, as illustrated in following example. It means to say that CENVAT Credit eliminates cascading effect of tax.

Cascading effect of tax: it means goods suffered tax suffering again and again in addition to tax on taxes, whereas CENVAT Credit eliminates the cascading effect of tax.

Example 1:

	Transaction without VAT		Transaction With VAT	
Details	A (₹)	B (₹)	A (₹)	B (₹)
Purchases	–	110	–	100
Value Added	100	40	100	40
Sub–Total	100	150	100	140
Add Tax 10%	10	15	10	14
Total	110	165	110	154

'B' is purchasing goods from 'A'. In second case i.e. under Vat, his purchase price is ₹ 100 as he is entitled to Cenvat credit of ₹ 10 i.e. tax paid on purchases. His invoice shows tax paid as ₹ 14. However, since he has got credit of ₹ 10, effectively he is paying only ₹ 4 as tax, which is 10% of ₹ 40, i.e. 10% of 'value added' by him. Cenvat (Central Value Added Tax) scheme is used to achieve the aim of levying tax only on 'value added' at each stage.

Example 2:

Particulars	Value ₹
Goods Purchased by Mr. Y by paying ₹ 224 from Mr. X out of which ₹ 24 towards excise duty which is not considered as cost	200.00
Add: Value Addition	80.00
Taxable Turnover	280.00
Add: CENVAT @12.5%	35.00
Sales Inclusive of Excise Duty	315.00

Total excise duty payable = ₹ 35.00

Less: CENVAT Credit = ₹ 24.00

Net excise duty payable = ₹ 11.00

Value Added Tax is ₹ 11.00

3.2 HIGHLIGHTS OF CENVAT CREDIT SCHEME

CENVAT Credit is an integration of excise duty and service tax. It means while paying excise duty service tax can claim as Cenvat credit and while paying service tax excise duty can claim as Cenvat credit. The same has been explained in the following example:

Example 3:

M/s X Ltd. (not a SSI unit) is a manufacturer produced dutiable finished goods in the month of December 2015 for ₹ 20,00,000, exclusive of excise duty payable is @12.5%. Input goods (i.e. raw material) purchased for ₹ 5,61,800 inclusive of excise duty @ 12.5%. Capital goods purchased in the same month for ₹ 10,00,0000 (exclusive of excise duty 12.5%). Input services used from a consultant for ₹ 2,00,000 (exclusive of service tax 14.5%). Finished goods removed from the factory in the month of December 2015. Find the net excise duty payable by M/s X Ltd., and due date of payment of excise duty?

Answer:

(Amount in ₹)

Particulars	Excise Duty (₹)	Workings
Finished Goods	2,50,000	₹ 20 L × 12.5%
Less: CENVAT CREDIT on input goods	(62,422)	5,61,800 × 12.5/112.5 = ₹ 62,422
Less: CENVAT CREDIT on capital goods	(62,500)	₹ 10,00,000 × 12.5% = ₹1,25,000 Up to 50% allowed as CENVAT credit in the first year of receipt of capital goods and balance allowed in the subsequent year or years
Less: CENVAT CREDIT on input services	(29,000)	₹ 2,00,000 × 14.5% = ₹ 29,000
Net excise duty payable	96,078	Due date of payment of excise duty is on or before 6th January 2016

3.2.1 Cenvat Credit Rules, 2004

Rule 1: Title, extent and commencement:

These rules called as CENVAT Credit Rules, 2004. They extended to the whole of India. However, these rules not applicable to the State of Jammu and Kashmir with regard to availment and utilization of credit of service tax.

Definitions under Cenvat Credit Rules, 2004

Rule 2: Definitions:

Rule 2(a): **capital goods:**

The term "Capital goods" under CENVAT Rules is Different from capital goods as understood in accounting or in income-tax. Items like spare parts, tools, dies, tubes fittings etc. are never capitalized in accounts for income-tax purposes but are defined as capital goods for CENVAT.

(A) Capital goods are —

(i) All goods falling under Chapters 82, 84, 85, 90, heading number 6805, grinding wheels and the like parts thereof falling under heading 6804 of the First Schedule to Central Excise Tariff Act, 1 985.Tools, hand tools

Chapter 82: Tools, Implements, Cutlery etc.

Chapter 84: Nuclear Reactors, Boilers, Machinery and Mechanical appliances parts thereof

Chapter 85: Electrical Machinery & Equipment & parts thereof, sound recorders, and parts and accessories of such articles

Chapter 90: Optical, photographic, medical & surgical instruments and apparatus parts and accessories thereof.

(ia) Outside the factory of the manufacturer of the final products for generation of electricity for captive use within the factory;

(ii) Pollution control equipment;

(iii) Components, spares and accessories of goods specified at (i) and (ii) above;

(iv) Moulds and dies, jigs and fixtures;

(v) Refractories and refractory materials;

(vi) Tubes, pipes and fittings thereof, used in the factory;

(vii) Storage tank and

(viii) Motor vehicles other than those falling under tariff heading 8702, 8703, 8704, 8711 and their chassis, (but including dumpers and trippers)

Used—

(1) in the factory of the manufacturer of the final products, but does not include any equipment or appliance used in an office; or

(2) For providing output service;

(B) Motor vehicle designed for transportation of goods including their chassis registered in the name of the service provider, when used for

(i) providing an output service of renting of such motor vehicle; or

(ii) transportation of inputs and capital goods used for providing an output service; or

(iii) providing an output service of courier agency

(C) Motor vehicle designed to carry passengers including their chassis, registered in the name of the provider of service, when used for providing output service of

(i) transportation of passengers; or

(ii) renting of such motor vehicle; or

(iii) imparting motor driving skills.

(D) components, spares and accessories of motor vehicles which are capital goods for the assessee;

Rule 2(b): Customs Tariff Act means the Customs Tariff Act, 1975;

Rule 2(c): Excise Act means Central Excise Act, 1944;

Rule2(d): As per Rule 2(d) of Cenvat Credit Rules, 2004, exempted goods (i.e. non-dutiable goods) means goods which is exempt from whole of duty of excise leviable thereon, and includes goods which are chargeable to 'Nil' rate of duty goods in respect of which the benefit of an exemption under Notification No. 1/2011-CE dated 1-3-2011 or under entries at serial numbers 67 and 128 of Notification No. 12/2012–CE, dated the 17th March, 2012 is availed.

Rule 2(e): As per Rule 2(e) of Cenvat Credit Rules, 2004, exempted services means taxable services which is exempt from the whole of the service tax leviable thereon, or includes services on which no service tax is leviable under section 66B of the Finance Act, 1994 or taxable services whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken. For removal of doubts, it is hereby clarified that exempted services' includes trading (w.e.f. 1-4-2011).

Trading goods: A manufacturer or service provider may also be trading in goods. For example authorized service station of automobiles is also selling spare parts of motor car. For the purpose of valuation, the value of exempted service shall be the difference between the sale price and the cost of goods sold (determined as per the generally accepted accounting principles without including the expenses incurred towards the purchases) or 10%of the cost of goods sold, whichever is higher (vide

— Notification No. 13/201 1-CE dated 3 1-3-2011).

Taxable service whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken, but shall not include a service which is exported in terms of rule 6A of the Service Tax Rules, 1994.

Rule 2(f): Excise Tariff Act means the Central Excise Tariff Act, 1985

Rule 2(g): Finance Act means the Finance Act, 1994

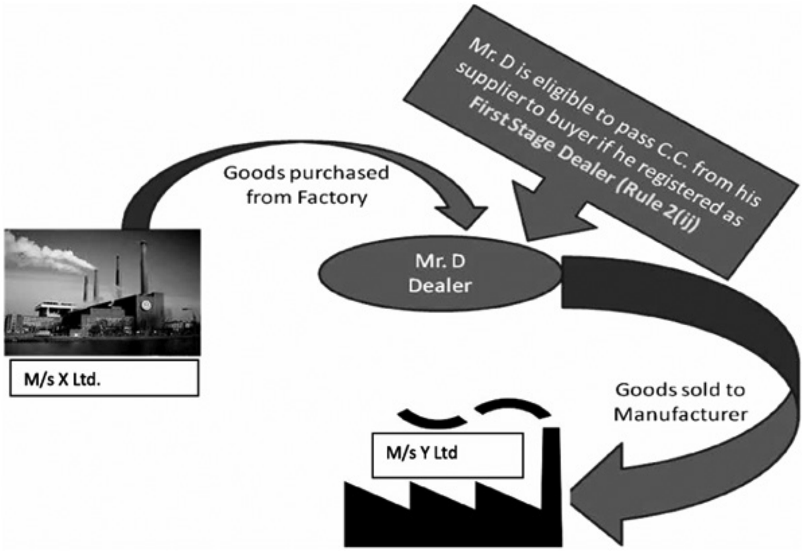
Rule 2(h): Rule 2(h) of CENVAT Credit Rules defines **final products** under Central Excise to mean those goods that are excisable and have come into existence from manufacturing activity making use of inputs or by using input services. Here final products mean only excisable goods i.e. those goods which are liable for excise duty which may be at nil rate or a rate higher than zero. Assessees are generally under the misconceived notion that only goods which suffer duty at a rate higher than zero percent are excisable goods whereas that is not the case. This definition of exempted goods is vital as there are certain restrictions as to availability of CENVAT credit. However the goods against which there is no rate prescribed in the CET may not be said to be excisable goods.

Rule 2(ij): First stage dealer means –

(i) A dealer, who purchases the goods directly from the manufacturer under the cover of an invoice in terms of the provisions of Central Excise Rules, 2002 or from the depot of the said manufacturer, or from premises of the consignment agent of the said manufacturer, or from any other premises from where the goods are sold by or on behalf of the said manufacturer, under cover of an invoice; or

(ii) An importer who sells goods imported by him under the cover of an invoice on which CENVAT credit may be taken and such invoice shall include an invoice issued from his depot or the premises of his consignment agent;

Example 4: Mr. D purchased dutiable goods from M/s X Ltd by paying excise duty and the same sold to M/s Y Ltd. In the given case Mr. D (registered under Central Excise as registered dealer) is competent to pass the excise duty as CENVAT Credit from M/s X Ltd to M/s Y Ltd. The same has been explained in the following diagram:



C.C. = CENVAT CREDIT

Rule 2(k): "input" means—

(i) all goods used in the factory by the manufacturer of the final product; or

(ii) any goods including accessories, cleared along with the final product, the value of which is included in the value of the final product and goods used for providing free warranty for final products; or

(iii) all goods used for generation of electricity or steam for captive use; or

(iv) all goods used for providing any output service;

but excludes—

(A) light diesel oil, high speed diesel oil or motor spirit, commonly known as petrol;

(B) any goods used for—

(a) construction or execution of works contract of a building or a civil structure or a part thereof; or

(b) laying of foundation or making of structures for support of capital goods,

except for the provision of service portion in the execution of a works contract or construction service as listed under clause (b) of section 66E of the Act;

(C) capital goods except when used as parts or components in the manufacture of a final product;

(D) Motor vehicles;

(E) any goods, such as food items, goods used in a guesthouse, residential colony, club or a recreation facility and clinical establishment, when such goods are used primarily for personal use or consumption of any employee; and

(F) any goods which have no relationship whatsoever with the manufacture of a final product.

Explanation:- For the purpose of this clause, "free warranty" means a warranty provided by the manufacturer, the value of which is included in the price of the final product and is not charged separately from the customer;

What is Input

Any input

- which is used "in the manufacture" or
- which is used "in relation to manufacture"
- which is not defined as capital goods will be eligible as inputs.

All goods (except High Speed Diesel, Light Diesel Oil and Petrol) used in or in relation to the manufacture of the final product, directly or indirectly and whether contained in the final product or not, and includes (i) Lubricating oils, (ii) Greases, (iii) cutting oils, (iv) accessories of the final products, (v) goods used as paints, as packing material, as fuel or for generation of electricity or steam used for manufacture of final products are eligible for CENVAT.

Example 5: X Ltd. removed cookers along with packing material from factory but used for packing at depot had to be considered as have been used in or in relation to the manufacture of final products and credit of duty paid on such master cartons (i.e. packing material) could not have been denied. The entire packing material is to be considered as has been used in or in relation to the manufacture of the final product. Accordingly they are entitled to avail the credit of duty paid on the packing material *Hawkins Cookers Ltd. (2010) (HC)*.

Construction service is not an 'input service to any manufacturer or service provider w.e.f. 1-4-2011

Example 6: Laboratory, test or quality check is always in relation to the manufacture of finished goods. It is immaterial whether or not the input is physically present in the final finished product as such; therefore, the laboratory test in relation to the manufacture of final product is a part of manufacture. Hence Cenvat Credit is available on raw material destroyed in laboratory test. *Tata Engineering & Locomotive Co. Ltd. 2010 (HC)*.

What is not input?

(a) Any input which is used as "facilitation to the manufacture" is not considered as an eligible Input.

(b) Input like steel, cement, angles, channels, CTD (Cold Twisted Deformed) or TMT (thermo mechanically treated) bar, other material used for following purpose is not eligible for credit

- Construction of building or civil structure or part thereof
- Laying of foundation or making of structures for support of Capital goods

Conditions one should satisfy to avail CENVAT Credit:

Cenvat Credit can be claimed only in respect of eligible inputs subject to the following conditions.

Condition 1: The input should be used in factory (Material sent for job work is acceptable provided these are brought back within 180 days from the date of dispatch). This condition is not applicable to the service provider.

Condition 2: Central Excise duty should be paid on inputs (Actual payment of duty by the buyer cum- manufacturer may not be required)

Condition 3: Final product must be dutiable goods.

Rule 2(l): input service (w.e.f. 1-4-2011), "input service" means any service,—

(i) used by a provider of output service for providing an output service; or

(ii) used by the manufacturer, whether directly or indirectly, in or in relation to the manufacture of final products and clearance of final products, upto the place of removal, and includes

    (a) services used in relation to modernization, renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises,

(b) advertisement or sales promotion,

(c) market research,

(d) storage upto the place of removal,

(e) procurement of inputs,

(f) accounting,

(g) auditing,

(h) financing,

(i) recruitment and quality control,

(j) coaching and training,

(k) computer networking,

(l) credit rating,

(m) share registry,

(n) security,

(o) business exhibition,

(p) legal services,

(q) inward transportation of inputs or capital goods and

(r) outward transportation upto the place of removal;

but excludes

(A) Service portion in the execution of a works contract and construction services including service listed under clause (b) of section 66E of the Finance Act (hereinafter referred as specified services) in so far as they used for

a. Construction or execution of works contract of a building or a civil structure or a part thereof; or

b. Laying of foundation or making of structures for support of capital goods,

except for the provision of one or more of the specified services; or

(B) Services provided by way of renting of a motor cycle in so far as they relate to a motor vehicle which is not a capital goods; or

(BA) service of general insurance business, servicing, repair and maintenance, in so far as they relate to a motor vehicle which is not a capital goods, except when used by-

(a) a manufacturer of a motor vehicle in respect of a motor vehicle manufactured by such person; or

(b) an insurance company in respect of a motor vehicle insured or reinsured by a such person; or

(C) such as those provided in relation to outdoor catering, beauty treatment, health services, cosmetic and plastic surgery, membership of a club, health and fitness centre, life insurance, health insurance and travel benefits extended to employees on vacation such as Leave or Home Travel Concession, when such services are used primarily for personal use or consumption of any employee.

Rule 2(m): "input service distributor" means an office of the manufacturer or producer of final products or provider of output service, which receives invoices issued under rule 4A of the Service Tax Rules, 1994 towards purchases of input services and issues invoice, bill or, as the case may be, challan for the purposes of distributing the credit of service tax paid on the said services to such manufacturer or producer or provider, as the case may be;

Rule 2(n): "job work" means processing or working upon of raw material or semi-finished goods supplied to the job worker, so as to complete a part or whole of the process resulting in the manufacture or finishing of an article or any operation which is essential for aforesaid process and the expression "job worker" shall be construed accordingly.

Rule 2(na): "large taxpayer" shall have the meaning assigned to it in the Central Excise Rules, 2002;

Rule 2(naa): "manufacturer or producer" –

(i) in relation to articles of jewellery or other articles of precious metals falling under heading 7113 or 7114, as the case may be, of the First Schedule to the Excise Tariff Act, includes a person who is liable to pay duty of excise leviable on such goods under sub-rule (1) of rule 12AA of the Central Excise Rules, 2002;

(ii) in relation to goods falling under Chapter 61, 62 or 63 of the First Schedule to the Excise Tariff Act, includes a person who is liable to pay duty of excise leviable on such goods under sub-rule (1A) of rule 4 of the Central Excise Rules, 2002.

Rule 2(o): "notification" means the notification published in the Official Gazette;

Rule 2(p): "output service" means any service provided by a provider of service located in the taxable territory but shall not include a service –

(i) specified in section 66D of the Finance Act, or

(ii) where the whole of service tax is liable to be paid by the recipient of service.

Rule 2(q): "person liable for paying service tax" has the meaning as assigned to it in clause (d) of sub-rule (1) of rule 2 of the Service Tax Rules, 1994.

Rule 2(qa): "place of removal" means –

(i) a factory or any other place or premises of production or manufacture of the excisable goods;

(ii) a warehouse or any other place or premises wherein the excisable goods have been permitted to be deposited without payment of duty;

(iii) a depot, premises of a consignment agent or any other place or premises from where the excisable goods are to be sold after their clearance from the factory,

from where such goods are removed;

Rule 2(r): "provider of taxable service" include a person liable for paying service tax.

Rule 2(s): "second stage dealer" means a dealer who purchases the goods from a first stage dealer.

Rule 2(t): words and expressions used in these rules and not defined but defined in the Excise Act or the Finance Act shall have the meaning respectively assigned to them in those Acts.

Clarifications from the CBE&C (Circular No. 943/04/201 1-CX, dated 29-4-2011) with regard to input and input services

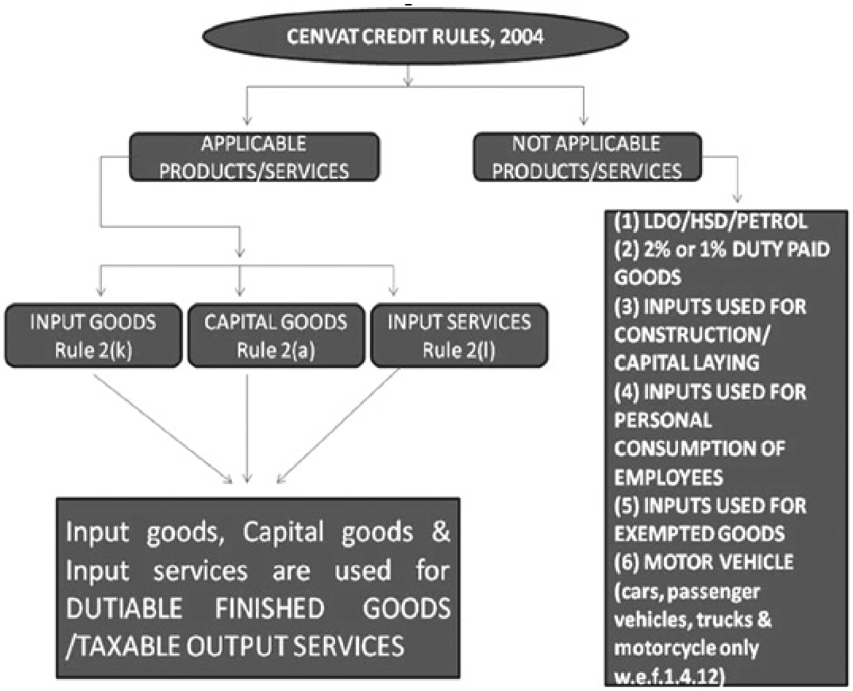
Since, definition of 'input', and 'input service' has been changed w.e.f. 1-4-2011, the Central Board of Excise and Customs has been issued clarifications in this regard *vide* CBE&C No. 943/04/2011 -CX., dated 29-4-2011, the same were explained with the help of examples;

Sl. No.	Issue	Clarification	Examples
1	Can credit of capital goods be availed of when used in manufacture of dutiable goods on which benefit under Notification 1/2011- CE is availed or in provision of a service whose part of value is exempted on the condition that no credit of inputs and input services is taken?	As per Rule 6(4) of the CENVAT credit Rules, 2004, no credit can be availed on capital goods used exclusively in manufacture of exempted goods or in providing exempted service. Goods in respect of which the benefit of an exemption (i.e. Excise duty @1% is paid) under notification No. 1/2011-CE, dated the 1st March, 2011(or excise duty 2% w.e.f 17-3-2012) is availed are exempted goods [Rule 2(d)]. Taxable services, whose part of value is exempted on the condition that no credit of inputs and input services, used for providing such taxable service, shall be taken, are exempted services [Rule 2(e)]. Hence credit of capital goods used exclusively in manufacture of such goods or in providing such service is not allowed.	(1) M/s. X Ltd. is a manufacturer of Mathematical boxes, geometry boxes and colour boxes, pencil sharpeners. These goods are subject to excise duty @2% (w.e.f. 1-4-2012. Machinery purchased for ₹ 1,12,360 (inclusive of excise duty @12.36%) to produce aforesaid final products. Hence, M/s. X Ltd. is not eligible to claim CENVAT credit of duty paid on capital goods. (2) M/s. CDS Builders provided construction of commercial contract services. While executing construction contract, service provider purchased Drilling Machine (i.e. Capital Goods) for ₹ 2,24,720 (inclusive of excise duty @12.36%). Service tax was paid by service provider after claiming abatement @67%. Hence, M/s. CDS Builders are not eligible to claim CENVAT credit of duty paid on capital goods.
2	Is the credit of only specified goods and services listed in the definition of inputs and input services not allowed such as goods used in a club, outdoor catering etc, or is the list only illustrative?	The list is only illustrative. The principle is that cenvat credit is not allowed when any goods and services are used primarily for personal use or consumption of employees. **Illustrative list :** • Outdoor catering, • Beauty treatment, • Health services, • Cosmetic and plastic surgery, • Membership of a club, • Health and fitness centre, • Life insurance, • Health insurance and travel benefits extended to employees on vacation such as Leave or Home Travel Concession etc.	M/s. A Ltd. is a manufacturing company regularly providing lunch to their employees. For this purpose M/s. A Ltd. received outdoor catering service from Mr. B. Since, this service meant primarily for the personal use or consumption of employees will not constitute an input service. Therefore, service tax paid on outdoor catering service is not allowed as CENVAT credit. *However, outdoor catering service should be considered as input service if used for sales promotion, training, auditing (i.e. lunch to auditors), legal services, security or to directors who are not employees.*

Sl. No.	Issue	Clarification	Examples
3	How is the *"no relationship whatsoever with the manufacture of a final product"* to be determined?	Credit of all goods used in the factory is allowed except in so far as it is specifically denied. The expression *"no relationship whatsoever with the manufacture of a final product"* must be interpreted and applied strictly and not loosely. The expression does not include any goods used in or in relation to the manufacture of final products whether directly or indirectly and whether contained in the final product or not. Only credit of goods used in the factory but having absolutely no relationship with the manufacture of final product is not allowed.	(1) M/s. Ram Ltd. purchased Steel, cement and other material used for construction of factory building is not eligible as input goods. (2) Part of inputs goes in process loss, may not be reflected in final product. However, CENVAT credit is available on entire quantity of inputs. Since, inputs are used in the manufacture of final product. (3) *Goods such as furniture and stationary used in an office within the factory are goods used in the factory and are used in relation to the manufacturing business and hence the credit of same is allowed.*
4	Is the credit of input services used for repair or renovation of factory or office available?	*Credit of input services used for repair or renovation of factory or office is allowed.* Services used in relation to renovation or repairs of a factory, premises of provider of output service or an office relating to such factory or premises, are specifically provided for in the inclusive part of the definition of input services.	M/s. X Ltd. paid ₹1,10,300 (inclusive of service tax @12.36%) to a provider of taxable services towards renovation of factory and office relating to such factory. M/s. X Ltd. is allowed to claim CENVAT credit on input services (i.e. renovation and repairs of a factory) as per Rule 2(l) of CEVNAT Credit Rules, 2004 (w.e.f. 1-4-2011).
5	Is the credit of Business Auxiliary Service (BAS) on account of sales commission now disallowed after the deletion of expression "activities related to business"?	The definition of input services allows all credit on services used for clearance of final products upto the place of removal as per the Rule 2(1)(ii) of the CENVAT Credit Rules, 2004 (w.e.f. 1-4-2011). Moreover activity of sale promotion is specifically allowed and on many occasions the remuneration for same is linked to actual sale. Reading the provisions harmoniously it is clarified that credit is admissible on the services of sale of dutiable goods on commission basis.	Mr. X is a commission agent of M/s Y Ltd., manufacturer of furniture. A sum of ₹ 11,030 (inclusive of service tax) has been paid by M/s Y Ltd., towards commission to Mr. X. Service tax paid on input service (Business Auxiliary Service) is allowed as CENVAT credit.

Sl. No.	Issue	Clarification	Examples
6	Can the credit of input or input services used exclusively in trading, be availed?	Trading is an exempted service. Hence the credit of any inputs or input services used exclusively in trading cannot be availed.	An assessee is a dealer of Air Condition Machines. These goods are purchased from a manufacturer by paying value of goods as well as excise duty. However, excise duty is not allowed as CENVAT credit.
7	Are the taxes and year end discounts to be included in the sale price and cost of goods sold while calculating the value of trading?	Generally accepted accounting principles need to be followed in this regard. All taxes for which set off or credit is available or are refundable/ refunded may not be included. Discounts are to be included.	**Value of trading:** selling price of a product is ₹ 250 and the purchase price is ₹ 200, the difference is ₹ 50 or ₹ 20 (i.e. ₹ 200 x 10%) whichever is higher will be considered as value of exempted service for the purpose of payment of amount @6% or for proportionate reversal of credit. *Selling price includes discounts but excludes taxes and duties for which credit is allowed.*
8	Does the expression "in or in relation" used in Rule 6 override the definition of "input" under Rule 2(k) for determining the eligibility of Cenvat credit?	The definition of "input" is given in Rule 2(k) and Rule 6 only intends to segregate the credits of inputs used towards dutiable goods and exempted goods. While applying Rule 6, the expression "in or in relation" must be read harmoniously with the definition of "inputs".	
9	Sub-rules 3B and 3C of rule 6 apply to whole entity or independently in respect of each registration?	The sub-rules 6(3B) and 6(3C) impose obligation on the entities providing banking and financial services (in case of a bank and a financial institution including a non-banking financial company) or life insurance services or management of investment under ULIP service. The obligation is applicable independently in respect of each registration. When such a concern is exclusively rendering any other service from a registered premise, the said rules do not apply. In addition to BoFS and life insurance services if any other service is rendered from the same registered premises, the said rules will apply and due reversals need to be done.	
10	Is the credit available on services received before 1.4.11 on which credit is not allowed now?	The credit on such service shall be available if its provision had been completed before 1.4.2011.	rent-a-cab service

For easy understanding we have presented the entire concept so far explained in the following diagram:



Types of CENVAT Credit

In terms of Rule 3 of CENVAT Credit Rules, credit is available to the manufacturer of excisable goods which either may be dutiable or non dutiable and the provider of taxable service. CENVAT credit is not available to the dealer as the dealer does not engage himself in any processing amounting to manufacture as defined under law which would entitle him to CENVAT credits and therefore, merely passes on the CENVAT benefit which is equal to the duty per unit of the final product, paid by the manufacturer on clearances effected by him. The following duties paid on inputs are eligible as CENVAT Credit for the manufacturer of Excisable goods:

(i) Basic duty of excise specified under First Schedule to Central Excise Tariff Act.

(ii) Special duty of excise specified under Second Schedule to Central Excise Tariff Act.

(iii) The additional duty of excise under Section 3 of Additional duties of excise (Textile and Textile Articles) Act, 1978 and wherein restrictions are provided as to utilization i.e. it can be utilized only towards payment of excise duty leviable under additional duties of excise (T & TA) Act 1978.

(iv) The additional duty of excise leviable under section 3 of Additional duties of excise (Goods of special importance) Act, 1957 (58 of 1957) and it can be utilized towards payment of either basic or special excise duty.

(v) The National Calamity Contingent duty leviable under section 136 of Finance Act, 2001 (14 of 2001) and this duty can be utilized for payment of NCCD.

(vi) Education Cess on excisable goods or on taxable services leviable under section 91 read with section 93 of Finance Act, 2004 and this is to be utilized only towards the payment of education cess either on goods or taxable output services.

(vii) Secondary and Higher education cess on inputs and input services leviable under section 136 read with section 138 of Finance Act. 2007 and it can be utilized only towards payment of secondary and higher education cess either on excisable goods or on taxable output service.

(viii) The additional duty leviable under section 3(5) of the Customs Tariff Act, No restrictions are provided for its utilization but however the duty leviable under this section cannot be availed by service providers.

(ix) The additional duty of excise leviable under section 157 of the Finance Act and this can be utilized towards payment of additional duty of excise under section 157.

(x) Additional duty of excise equivalent to duty of excise leviable under section 3 of Customs Tariff Act to offset the effect of Central Excise Duty on locally manufactured goods. This is known as CVD

(xi) Service tax leviable under section 66, 66A (import of services under erstwhile service tax law) or Section 66B (charging section under negative list based taxation). No restrictions as to utilization is provided and this credit can be utilized towards payment of either excise duty or for paying service tax.

(xii) Additional duty of excise leviable under section 85 of the Finance Act and this is to be utilized towards payment of additional duty of excise leviable under section 85 of the Finance Act.

However duty paid at the rate of 1% in terms of Notification No. 1/2011-CE dated 1-3-201 1 cannot be availed as Credit. It is also set out in proviso to Rule 3(I)(v/7) that credits upto 85% of additional duty of Customs under section 3(1) of Customs Tariff Act, 1975, on ships, boats and other structures for breaking up can be allowed.

CENVAT Credit is available either to the manufacturer or producer of excisable products or provider of taxable services on:

(a) Inputs received in the factory of manufacture of final products on or after 10th September 2004.

(b) Capital goods received in the factory of manufacture of final products (except in case capital goods installed outside the factory for generation of electricity for captive use) on or after 10th September, 2004.

(c) Input services received by the manufacturer of final product on or after 10th September, 2004.

(d) Any inputs or input services used in the manufacture of intermediate products by a job worker and received by the manufacturer for further use in relation to manufacture.

Transitional Credit

Rule 3(2) provides for availment of credit on inputs when the assessee enters into the tax net for the first time, as in the normal course the manufacturer would have stock in hand (raw materials, consumables, packing materials) as on that date. The removals from that date would suffer duty; therefore credit on the inputs contained in finished goods and work in progress is available and on the other hand any assessee who opts out of CENVAT scheme should also reverse the credit contained in the raw material, finished goods and work in progress. For availing the transitional credit, the inputs must satisfy all the conditions as to definition of inputs under Central Excise Law. This provision is mainly invoked by SME units availing the benefit of Notification No. 8/2003-CE as they are required to pay duty on crossing ₹ 150 lacs and avail credit while at the end of the year they are required to reverse the credit on excising the option available under Notification No. 8/2003-CE.

3.3 UTILIZATION OF CENVAT CREDIT

Rule 3: Cenvat Credit allowed or may be utilized for various types of duties and taxes explained under the sub rules of rule 3.

Cenvat Credit allowed or may be utilized for various types of duties and taxes explained under the sub rules of rule 3.

As per Rule 3(4) of CENVAT Credit Rules 2004, credit may be utilized for payment of

(a) any duty of excise on any final products or

(b) an amount equal to CENVAT credit taken on inputs if such inputs are removed as such or after being partially processed; or

(c) an amount equal to the CENVAT credit taken on capital goods if such capital goods are removed as such; or

an amount under sub-rule (2) of rule 16 of Central Excise Rules, 2002 (it means if the process to which the goods are subjected before being removed does not amount to manufacture, the manufacturer shall pay an amount equal to the CENVAT credit taken) service tax on any output service.

The following table will provide clear picture in respect of claiming of credit.

Particulars	**BED**	**Remarks**
Finished Goods	XXXX	
OUTPUT SERVICE	XXXX	
AMOUNT	XX	AMOUNT DOES NOT ATTRACT CESS
LESS: C.C. ON I.G.	(XX)	
LESS: C.C. ON I.S.	(XX)	
LESS: C.C. ON C.G.	(XX)	UPTO 50% 1ST YEAR
LESS: C.V.D.	(XX)	Equal to B.E.D.
LESS: SPL. CVD	(XX)	Equal to VAT / CST
NET PAYABLE	XX	

C.C. ON I.G = cenvat credit on input goods

C.C. ON I.S = cenvat credit on input services

C.C. ON C.G = cenvat credit on capital goods

C.V.D. = countervailing duty (also called as additional customs duty)

SPL. CVD = special countervailing duty (also called as special additional customs duty)

Rule 3(1)(i): *Additional Customs Duty (i.e. CVD) Imported Goods*

Ships, boats and other structures imported for breaking up which will attract excise duty falling under 8909 00 00, because various items like washing machine, furniture, air condition machine and so on will come out. Therefore, CVD paid on account of import of ships, boats allowed as cenvat credit only to the extent of 85% (w.e.f 1.3.2011) while paying excise duty on products extracted from ships, boats or other structures.

Rule 3(2):Ceases to be exempted

Manufacture is allowed to take cenvat credit lying in stock or in process (work in progress) or inputs contained in the final goods lying as stock on the date on which any goods manufactured by the said manufacturer ceases to be exempted goods (i.e. goods become dutiable). The same provision is also applicable for service provider rule 3(3).

3.4 REVERSAL OF CENVAT CREDIT

Rule 3(5) Removal of Goods as such

When inputs or capital goods, on which CENVAT credit has been taken, are removed as such from the factory, or premises of the provider of output service, the manufacturer of the final products or provider of output service, as the case may be, shall pay an amount equal to the credit availed in respect of such inputs or capital goods and such removal shall be made under the cover of an invoice referred to in rule 9 of the Cenvat Credit Rules, 2004.

It is provided that if the manufacturer of goods or the provide of output service fails to pay the amount payable under sub-rules (5), (5A) and (5B) of Rule 3 (Payment on removal of Inputs/Capital goods as such or after use and write off of Inputs/Capital goods), it shall be recovered, in the manner as provided in rule 14, for recovery of CENVAT Credit wrongly taken.

Exceptions:

(a) Cenvat credit not required to be reversed if input goods or capital goods removed outside the premises of the provider of output service for providing the output service;

(b) Cenvat credit shall not be required to be reversed where any inputs are removed outside the factory for providing free warranty for final products.

Rule 3(5A) Removal of Capital goods after use (w.e.f. 1-4 -2012)

If the capital goods, on which CENVAT credit has been taken, are removed after being used, whether as capital goods or as scrap or waste, the manufacturer or provider of output services, shall pay

(a) an amount equal to the CENVAT Credit taken on the said capital goods reduce by the percentage points calculated by straight line method as specified below for each quarter of a year or part thereof from the date of taking the CENVAT Credit, namely:–

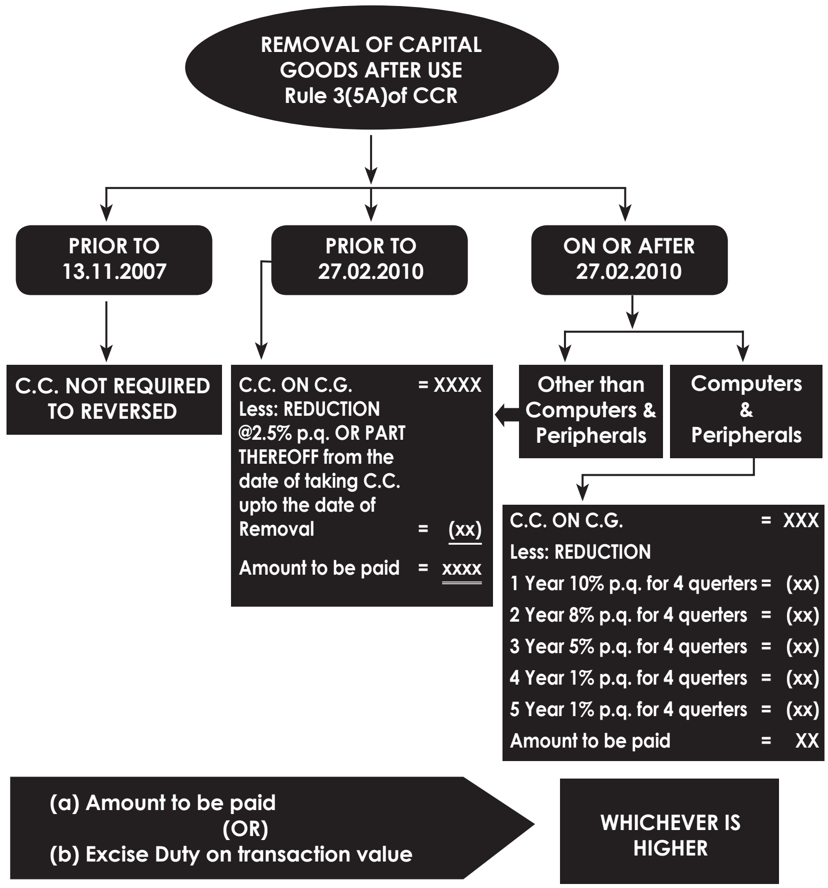
  (i) for computer and computer peripherals:

  - for each quarter in the first year @10%
  - for each quarter in the second year @ 8%
  - for each quarter in the third year @ 5%
  - for each quarter in the fourth and fifth year @1%

  (ii) for capital goods, other than computers and computer peripherals @ 2.5% for each quarter.

  Provided that if the amount so calculated is less than the amount equal to the duty leviable on transaction value, the amount to be paid shall be equal to the duty leviable on transaction value.

(b) If the capital goods are cleared as waste and scrap, the manufacturer shall pay an amount equal to the duty leviable on transaction value.



Rule 3(6): Cenvat credit available of the amount paid under sub-rule 5 & 5A

The amount paid under sub-rule (5) and sub-rule (5A) shall be eligible as CENVAT credit as if it was a duty paid by the person who removed such goods under sub-rule(5) and sub-rule (5A).

Rule 3(5B): CENVAT credit to be reversed/paid

Any inputs or capital goods before being put to use, on which CENVAT Credit has been taken is written off fully or partially or any provision is made in books of account to write off fully or partially, the manufacturer or service provider is required to pay an amount equal to CENVAT credit taken in respect of such inputs or capital goods (w.e.f. 1-3-2011).

Provided that if the said inputs or capital goods is subsequently used in the manufacture of final products or the provision of output services, the manufacturer or output service provider, as the case may be, shall be entitled to take the credit of the amount equivalent to the CENVAT credit paid earlier subject to the other provisions of these rules.

Rule 3(5C): Damage/Destruction of Finished goods

Where on any goods manufactured or produced by an assessee, the payment of duty is ordered to be remitted under rule 21 of the Central Excise Rules, 2002, the CENVAT credit taken on the inputs used in the manufacture or production of said goods and the CENVAT credit taken on inputs services used in or in relation to the manufacture or production of said goods shall be reversed.

Explanation 1- The amount payable under sub-rules (5), (5A), (5B) and (5C), unless specified otherwise, shall be paid by the manufacturer of goods or the provider of output service by debiting the CENVAT credit or otherwise on or before the 5th or 6th day of the following month except for the month of March, where such payment shall be made on or before the 31st day of the month of March.

Explanation 2- If the manufacturer of goods or the provider of output service fails to pay the amount payable under sub-rules (5), (5A), (5B) and (5C), it shall be recovered, in the manner as provided in rule 14, for recovery of CENVAT credit wrongly taken and utilized.

Example 7: Y Ltd. manufactured cars which have been destroyed by fire within the factory. If Y Ltd. obtained remission of duty on finished goods, then duty on input goods had availed as CENVAT credit should be reversed.

Rule 3(7): CENVAT Credit on purchases from EOU/EHTP/STP

Goods removed from a 100% Export Oriented Unit or from a unit in an Electronic Hardware Technology park or from a Software Technology Park to Domestic Tariff Area are liable to pay excise duty. As per Rule 17 of Central Excise Rules, 2002 goods shall be removed from a 100% Export Oriented Unit to Domestic Tariff Area under an invoice by following the procedure specified in rule 11 of CENVAT Credit Rules, 2004, and the duty leviable on such goods shall be paid by utilizing the CENVAT credit or by crediting the duty payable to the account of the Central Government in the manner specified in rule 8 of the Central Excise Rules, 2002 *[CCEx. & Cus.* **v** *Suresh Synthetics* (2007) (SC)].

As per present law, duty on clearances of goods to DTA from 100% EOU will be equal to 50% of basic customs duty, countervailing duty under section 3(1) of the Customs Tariff Act, 1975 plus special additional duty under section 3(5) of Customs Tariff Act, 1975, if applicable (i.e. VAT exempted), and cess as applicable.

Example 8 : M/s X Ltd (a unit of 100% EOU) sold goods to M/s A Ltd. for ₹ 20 lac. BCD @10%, CVD 12.5% and Spl. CVD @4% (VAT exempted) are applicable.

Find the total duty of excise. How much Cenvat Credit allowed to M/s A Ltd.

Answer:

Particulars	**Value in ₹**	**Workings**
Assessable value	20,00,000	
Add: Basic Customs Duty 10%	1,00,000	20,00,000 × 10% × 50%
Balance	21,00,000	
Add: CVD @12.5%	2,62,500	21,00,000 × 12.5%
Balance	23,62,500	
Add: 2% CESS on (₹ 1,00,000 + ₹ 2,62,500)	7,250	3,62,500 × 2%
Add: 1% SAH CESS on (₹ 1,00,000 + ₹ 2,62,500)	3,625	3,62,500 × 1%
Balance	23,73,375	
Add: SPL. CVD 4%	94,935	23,73,375 × 4%
Value of import	24,68,310	

Cenvat Credit allowed is ₹ 3,57,435 (i.e. CVD + Spl. CVD)

Rule 4: Conditions for allowing CENVAT Credit

In all taxation laws, the benefit is always available with some Conditions and the conditions for utilizing the CENVAT credits are provided in Rule 4 of CENVAT Credit Rules 2004:

1. The CENVAT Credit in respect of inputs may be taken immediately on receipt of the inputs in the factory of the manufacture or in the premises of the provider of output service. In respect of final products falling under chapter 7113, the CENVAT on inputs may be taken immediately on receipt of inputs in the registered premises of the person who gets the final products manufactured on his behalf on job work basis subject to the condition that inputs are used by the job worker for manufacturing such final product.

Further CENVAT credit in respect of inputs may be taken by the provider of output service when the inputs are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the inputs.

Provided also that the manufacturer or the provider of output service shall not take CENVAT credit after six months of the date of issue of any of the documents specified in sub-rule (1) of rule 9.

2. The CENVAT Credit in respect of capital goods received in a factory at any point in a given financial year shall be taken only to the extent of 50% of the duty paid. [Manufacturer eligible for SSI exemption would be eligible to avail 100% in the 1st year]

Further CENVAT credit in respect of capital goods may be taken by the provider of output service when the capital goods are delivered to such provider, subject to maintenance of documentary evidence of delivery and location of the capital goods.

3. Rule 4(2)(a)) which provides for availing credits on receipt of capital goods into factory, is amended w.e.f. 1-4-2011, to state that the CENVAT credit would be allowed even on capital goods which is received outside the factory and used for generation of electricity for captive used in factory.

4. However if the capital goods are cleared as such in the same financial year, whole of the duty paid shall be taken as CENVAT. Availment of Credit upto 50% in the year of receipt is not applicable to additional duty of excise levied under section 3(5) of Customs Tariff Act. Similar to what is stated in the aforesaid clause, physical receipt is important for availment of CENVAT credit. Facility has been provided to SSI units that are eligible to avail the benefit of Notification No. 8/2003-CE to take the full CENVAT credit on capital goods in one installment in the year of receipt of goods.

5. The balance of CENVAT credit may be taken in any financial year subsequently only if the capital goods are in the possession of the manufacturer and in case the manufacturer has not availed duty of excise in the year of procurement, then entire credit would be available in the next year. This requirement as to possession in the subsequent year would not apply to components, spares and accessories, moulds, tools and dies and refractories and refractory materials.

6. The manufacturer is not expected to own the capital goods for the purpose of availment, relaxations are provided in Rule 4(3) allowing credit in respect of capital goods even if the capital goods are acquired either on lease, hire or loan agreement from a financing company.

7. Rule 4(4) provides that CENVAT credit in respect of capital goods shall not be allowed on such value of capital goods representing duty when the manufacturer has claimed depreciation under section 32 of Income Tax Act on the said amount of duty. In other words, the manufacturer or the service provider cannot claim CENVAT credit and again include the CENVAT amount in the cost of the capital goods for the purpose of claiming depreciation.

8. Rule *4(5)(b)* has been amended during 2010 budget changes to provide that CENVAT credit shall be allowed in respect of jigs, fixtures, moulds and dies sent by a manufacturer of final products to another manufacturer for production of goods or to a job worker for the production of goods on his behalf. Therefore, these items can also be sent to another manufacturer for manufacture of goods as per his specifications.

Rule 4(7): CENVAT credit in respect of Input service

The CENVAT credit in respect of input service shall be allowed, on or after the day on which the invoice, bill or, as the case may be, challan referred to in rule 9 is received.

Provided that in respect of input service where whole of the service tax is liable to be paid by the recipient of service, credit shall be allowed after the service tax is paid.

Provided further that in respect of an input service, where the service recipient is liable to pay a part of service tax and the service provider is liable to pay the remaining part, the CENVAT credit in respect of such input service shall be allowed on or after the day on which payment is made of the value of input service and the service tax paid or payable as indicated in invoice, bill or, as the case may be, challan referred to in rule 9.

Provided also that in case the payment of the value of input service and the service tax paid or payable as indicated in the invoice, bill or, as the case may be, challan referred to in rule 9, except in respect of input service where the whole of the service tax is liable to be paid by the recipient of service, is not made within three months of the date of the invoice, bill or, as the case may be, challan, the manufacturer or the service provider who has taken credit on such input service, shall pay an amount equal to the CENVAT credit availed on such input service and in case the said payment is made, the manufacturer or output service provider, as the case may be, shall be entitled to take the credit of the amount equivalent to the CENVAT credit paid earlier subject to the other provisions of these rules.

Provided also that if any payment or part thereof, made towards an input service is refunded or a credit note is received by the manufacturer or the service provider who has taken credit on such input service, he shall pay an amount equal to the CENVAT credit availed in respect of the amount so refunded or credited.

Provided also that CENVAT credit in respect of an invoice, bill or, as the case may be, challan referred to in rule 9, issued before the 1st day of April, 2011 shall be allowed, on or after the day on which payment is made of the value of input service and the service tax paid or payable as indicated in invoice, bill or, as the case may be, challan referred to in rule 9.

Provided also that the manufacturer or the provider of output service shall not take CENVAT credit after one year of the date of issue of any of the documents specified in sub-rule (1) of rule 9.

3.5 REFUND OF CENVAT CREDIT

Rule 5: Refund of Cenvat Credit

Following the amendment in Rule 5, the Government has issued a fresh Notification No. 27/2012 –CE (N.T.) dated 18 June 2012 (the Notification) which has superseded earlier Notification in this regard i.e. Notification No. 5/2006 – CE (N.T.) dated 14 March 2006. The Notification prescribes new procedures, safeguards, conditions and limitations with respect to the manner in which the refund would be claimed by the exporter of goods / services.

The key changes are as under:

(a) In case of person exporting goods and services simultaneously, option has been provided to submit two refund claims, one in respect of export of goods and the other in respect of export of services;

(b) Option to submit monthly claims under certain circumstances has been withdrawn. Therefore, every person will now have to file the refund claim on a quarterly basis;

(c) In addition to the maximum cap provided in Rule 5 (to the extent of export turnover / total turnover), the Notification further provides for a restriction, wherein the amount of refund claim can neither exceed the closing balance of credit lying at the end of quarter to which the refund claim relates nor the balance of credit lying at the time of filing of refund claim;

(d) The amount of refund would have to be debited to CENVAT credit amount at the time of filing of such claim. However, if the sanctioned amount of refund is less than the amount of refund filed, the difference may be taken back as credit by the claimant;

(e) Credit is being allowed on motor vehicles (except those of heading nos. 8702, 8703, 8704, 8711 and their chassis).

The Credit of tax paid on the supply of such vehicles on rent, insurance and repair shall also be allowed;

(f) Credit of insurance and service station service is being allowed to –

(i) Insurance companies in respect of motor vehicles insured and re-insured by them; and

(ii) Manufacturers in respect of motor vehicles manufactured by them.

(g) At present, credit on goods can be taken only after they are brought to the premises of the service provider. Rule 4(1) and 4(2) are being amended to allow a service provider to take credit of inputs or capital goods whenever the goods are delivered to him, subject to specified conditions.

(h) Rule 7 for input service distributors is being amended to provide that credit of service tax attributable to service used wholly in a unit shall be distributed only to that unit and that the credit of service tax attributable to service used in more than one unit shall be distributed prorate on the basis of the turnover of the concerned unit to the sum total of the turnover of all the units to which the service relates.

(i) Rule 9(1) (e) is being amended to allow availment of credit on the tax payment challan in case of payment of service tax by the receiver on reverse charge basis.

W.e.f 1.4.2012 Simplified scheme introduced for exporter and service providers who are exported goods and services.

$$\text{REFUND AMOUNT} = \frac{\text{EXPORT TURNOVER OF GOODS \& SERVICE}}{\text{TOTAL TURNOVER}} \times \text{Net CENVAT CREDIT}$$

EXPORT TURNOVER	VALUE (₹)
DUTIABLE F.G. EXPORTED DURING THE RELEVANT PERIOD	XXXX
INTERMEDIATE PRODUCTS CLEARED FOR EXPORT DURING RELEVANT PERIOD	XXXX
TOTAL	XXXX

EXEMPTED GOODS EXPORTED REMAINS CALLED AS EXEMPTED GOODS ONLY

Export Turnover of Service	**Value (₹)**
Payments received during the relevant period for export service	XXXX
Export services whose provision has been completed for which payment had been received in advance	XXXX
Less: Advance received for export of services for which services not completed during the relevant period	XXXX
Total	**XXXX**

Total Turnover	**Amount (₹)**
Dutiable goods cleared during relevant period for export as well as for D.T.A	XXXX
Exempted goods cleared during relevant period for export as well as for D.T.A	XXXX
Export of services and services provided in D.T.A	XXXX

Input goods and capital goods removed as such against an invoice for the relevant period - rule 3(5)	XXXX
Total	**XXXX**

Net Cenvat Credit	**Amount (₹)**
Total cenvat credit on input goods and input services	XXXX
Less: Amount reversed for the relevant period as per rule 3(5c) of CCR	(XXX)
Total	**XXXX**

Example 9: Export of dutiable goods = ₹ 60,000

Domestic turnover = ₹ 30,000

Cenvat Credit = ₹ 4,500

Excise duty Liability = ₹ 3,708

Answer:

Refund is ₹ 792

(₹ 60,000/ ₹ 90,000) x ₹ 4,500 = ₹ 3,000

Or

Cenvat Credit balance = ₹ 792 (i.e. 4500 – 3708)

Whichever is less.

Refund claim should be after paying excise duty liability.

Note: Time limit for claiming refund is ONE year from the date of provision of the services.

Rule 5B: Refund of CENVAT credit to service providers providing services taxed on reverse charge basis. - A provider of service providing services notified under sub-section (2) of section 68 of the Finance Act and being unable to utilise the CENVAT credit availed on inputs and input services for payment of service tax on such output services, shall be allowed refund of such unutilised CENVAT credit subject to procedure, safeguards, conditions and limitations, as may be specified by the Board by notification in the Official Gazette.

Example 10: Mr. A is service provider and service tax on services provided by him is payable on partial reverse charge. 40% of service tax on services provided by Mr. A is payable by service recipient and balance tax is paid by him. The total service tax on services provided by him is ₹2,00,000 out of which his liability is ₹ 1,20,000. He receives inputs and input services on which credit of ₹ 2,20,000 is available. Discuss whether he can claim refund under Rule 5B ? What will be your answer, if 100% of the service tax is payable by the receiver of service.

Answer:

The two situations are discussed below –

Case I - Partial Reverse charge: If Mr. A is liable to pay 60% of service tax, which amounts to ₹1,20,000, then, such service will amount to output service and, hence, he can taken credit of ₹2,20,000; utilise it for payment of service tax of ₹1,20,000 and balance ₹1,00,000 of credit can be claimed as refund under Rule 5B.

Case II - 100% reverse charge: If whole of service tax on services provided by Mr. A is payable by recipient of services, then, such service is not output service under Rule 2(p) for Mr. A. Hence, he cannot take credit. When credit cannot be taken, there is no question of refund under Rule 5B.

As per Notification No.12/2014 dated 3rd March, 2014, the refund of CENVAT credit shall be allowed to a provider of services notified under sub-section (2) of section 68 of the Finance Act,1994, subject to the procedures, safeguards, conditions and limitations, as specified below, namely:-

1. Safeguards, conditions and limitations. –

   (a) the refund shall be claimed of unutilised CENVAT credit taken on inputs and input services during the half year for which refund is claimed, for providing following output services namely:-

      (i) renting of a motor vehicle designed to carry passengers on non abated value, to any person who is not engaged in a similar business;

      (iii) service portion in the execution of a works contract; (hereinafter the above mentioned services will be termed as partial reverse charge services).

   Explanation:- For the purpose of this notification,-

   Unutilised CENVAT credit taken on inputs and input services during the half year for providing partial reverse charge services = (A) – (B)

   Where,

$$A = \text{CENVAT credit taken on inputs and input services during the half year} \times \frac{\text{Turnover of output service under partial reverse charge during the half year}}{\text{Total turnover of goods and services during the half year}}$$

B = Service tax paid by the service provider for such partial reverse charge services during the half year;

   (b) the refund of unutilised CENVAT credit shall not exceed an amount of service tax liability paid or payable by the recipient of service with respect to the partial reverse charge services provided during the period of half year for which refund is claimed;

   (c) the amount claimed as refund shall be debited by the claimant from his CENVAT credit account at the time of making the claim;

   (d) in case the amount of refund sanctioned is less than the amount of refund claimed, then the claimant may take back the credit of the difference between the amount claimed and the amount sanctioned;

   (e) the claimant shall submit not more than one claim of refund under this notification for every half year;

   (f) the refund claim shall be filed after filing of service tax return as prescribed under rule 7 of the Service Tax Rules for the period for which refund is claimed;

   (g) no refund shall be admissible for the CENVAT credit taken on input or input services received prior to the 1st day of July,2012;

   ***Explanation.* –** For the purposes of this notification, half year means a period of six consecutive months with the first half year beginning from the 1st day of April every year and second half year from the 1st day of October of every year.

2. **Procedure for filing the refund claim. –**

(a) the provider of output service, shall submit an application in *Form A* annexed hereto, along with the documents and enclosures specified therein, to the jurisdictional Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, as the case may be, before the expiry of one year from the due date of filing of return for the half year:

Provided that the last date of filing of application in Form A, for the period starting from the 1st day of July, 2012 to the 30th day of September,2012, shall be the 30th day of June,2014;

(b) if more than one return is required to be filed for the half year, then the time limit of one year shall be calculated from the due date of filing of the return for the later period;

(c) the applicant shall file the refund claim along with copies of the return (s) filed for the half year for which the refund is claimed;

(d) the Assistant Commissioner or Deputy Commissioner to whom the application for refund is made may call for any document in case he has reason to believe that information provided in the refund claim is incorrect or insufficient and further enquiry needs to be caused before the sanction of refund claim;

(e) at the time of sanctioning the refund claim, the Assistant Commissioner or Deputy Commissioner shall satisfy himself or herself in respect of the correctness of the refund claim and that the refund claim is complete in every respect.

3.6 OBLIGATION OF A MANUFACTURER OR PRODUCER OF FINAL PRODUCTS AND A PROVIDER OF TAXABLE SERVICES

Rule 6: Obligation of a manufacturer or producer of final products and a provider of taxable service
Option 1: As per rule 6(2) of the CENVAT Credit Rules, 2004 (w.e.f. 1-4-2011).

If separate accounts maintained for the receipt, consumption and inventory of inputs, then the assessee shall take CENVAT credit on inputs which are used:-

in or in relation to the manufacture of dutiable final products excluding exempted goods; and for the provision of output services excluding exempted services.

If separate accounts maintained for the receipt and use of input services, then the assessee shall take CENVAT credit on input services which are used:-

- in or in relation to the manufacture of dutiable final products, excluding exempted goods, and their clearance upto the place of removal; and
- for the provision of output services excluding exempted services

If the capital goods used by the manufacturer or service provided for dutiable as well as non-dutiable goods and for taxable services as well as exempted services then the available Cenvat Credit can be claimed fully (i.e. upto 50% in the first year of receipt and the balance in the subsequent years).

Cenvat reversal of non-excisable goods under Rule 6 of the Cenvat Credit Rules, 2004 [Explanation 1] [w.e.f 01.03.2015]: For the purpose of this rule, exempted goods or final products shall include non-excisable goods cleared for a consideration from the factory.

Valuation of non-excisable goods [Explanation 2]: Value of non-excisable goods –

- Invoice value;
- if invoice value is not available, such value shall be determined by using reasonable means consistent with the principles of valuation contained in the Excise Act and the rules made thereunder.

If separate accounts are not maintained

In this case the manufacturer or service provider has following three options:

Option 2: As per rule 6(3)(i) of the Cenvat Credit Rules, 2004, *pay an amount*:

The manufacturer of goods shall pay an amount equal to 6% of '*value*' of exempted goods (w.e.f. 1-4-2012) and the provider of output services shall pay an amount equal to 7% (w.e.f. 01-06-2015) of '*value*' of the exempted services [notification no. 14/2015 - Central Excise (N.T.)].

(Or)

Option 3: As per rule 6(3) (ii) of the Cenvat Credit Rules, 2004, pay an amount proportionately attributable to CENVAT credit utilized for exempted final product and exempted output services as provided in rule 6(3A) of the Cenvat Credit Rules, 2004.

Option 4: As per rule 6(3)(iii) of the Cenvat Credit Rules, 2004, maintain separate account for inputs and pay 'amount' as determined under rule 6(3A) in respect of input services (w.e.f. 1-4-2011).

Goods Exported under bond are not exempted goods: Final products (dutiable goods) are exported under bond without payment of duty. They are not exempted goods. Hence, an amount @6% is not required to be paid. At the same time proportionate reversal of CENVAT credit is also not required as per rule 6(6)(v) of the Cenvat Credit Rules, 2004. Exported goods are considered as dutiable goods for the purpose of calculation of formulae as per rule 6(3A).

Rule 6(6A): the provisions of rule 6(1), 6(2), 6(3) and 6(4) shall not be applicable in case the taxable services are provided, without payment of service tax, to a unit in a Special Economic Zone or to a Developer of a Special Economic Zone for their authorized operations.

Important points with regard to Rule 6:

(i) Pay an *Amount'* to the department without charging Education Cess and Secondary and Higher Education Cess.

(ii) The buyer of exempted product is not eligible to get the CENVAT credit. Hence, the buyer of such exempted goods will not be eligible to avail CENVAT credit of 'amount' paid to the manufacturer or service provider (CBE & C circular No. 870/08/2008-C.Ex., dated 16-5-2008).

(iii) At the end of the year, assessee should calculate the ratios on actual basis and make fresh calculations and pay difference if any on or before 30th June. If any excess is paid, such an excess amount can be adjusted in CENVAT credit.

(iv) Delay in payment of shortfall amount will attract interest @ 24% per annum after the due date (i.e. 30^{th} June.) till the date of payment of short amount.

(v) If assessee opts to pay 'amount' on exempted services under 6(3)(i) of Cenvat credit Rules, 2004, the amount will be calculated on the value so exempted under abatement scheme. For example Mr. Raj provider of commercial construction services opted abatement 67%. Gross value of contract is ₹ 100 lakhs. Exempted services are ₹ 67 lakhs and taxable services are ₹ 33 lakhs. Hence, he is liable to pay service tax on ₹ 33 lakhs and 'amount' @7% on ₹ 67 lakhs.

(vi) **Value for purpose of Rule 6(3) and 6(3A) of the Cenvat Credit Rules, 2004 (w.e.f, 1-4-2011):** Assessee has to either pay 'amount' on value of exempted goods or services as per rule 6(3) or opt for proportionate reversal of credit as per rule 6(3A). As per rule 6(3D) of the Cenvat Credit Rules, 2004, ₹ Value' in both the cases will be as follows:

(a) Gross amount of works contract is ₹ 1,00,000 were service provider opted for composition scheme (i.e. @4.8%). Service tax will be ₹ 4,800. Hence, value of exempted services is ₹ 40,000 (i.e. 1: 4,800 x 100/12).

(b) Provider of commercial construction services opted abatement 67%. Gross value of contract is ₹ 100 lakhs. Exempted services are ₹ 67 lakhs and taxable services are ₹ 33 lakhs. Hence, he is liable to pay service tax on ₹ 33 lakhs and 'amount' @7% on ₹ 67 lakhs. That is value of exempted services is ₹ 67 lakhs.

(c) In case of trading goods, selling price of a product is ₹ 250 and the purchase price is ₹ 200, the difference is ₹ 50 or ₹ 20 (i.e. ₹ 200 x 10%) whichever is higher will be considered as value of exempted service for the purpose of payment of amount @7% or for proportionate reversal of credit.

Rule 6(3B): Bank or NBFC services

A substantial part of the income of a bank is from investment or by way of interest in which a number of inputs and input services are used (i.e. exempted as well as taxable). Hence, a banking company or a financial institution including NBFC, providing banking and financial services are being obligated to pay an amount equal to 50% of the credit availed on inputs and input services as per rule 6(3B) of the Cenvat Credit Rules, 2004, w.e.f. 1-4-2011. Therefore, other options of payment of amount under Rule 6 shall not be available for this service provider.

Rule 6(3C): Insurance Company services: A substantial part of the income of an insurance company is from investment or by way of interest in which a number of inputs and input services are used (i.e. exempted as well as taxable), Therefore, general insurance services and life insurance services or management of ULIPs, amount payable is equal to 20% of Cenvat credit availed on inputs and input services in the month as per rule 6(3C) of the Cenvat Credit Rules, 2004, w.e.f, 1-4-2011. Therefore, other options of payment of amount under Rule 6 shall not be available for this service provider. However, Rule 6(30 has been withdrawn w.e f 1.4.2012. It means Insurance companies now can avail full cenvat credit.

Rule 6(4): No CENVAT credit shall be allowed on capital goods which are used exclusively in the manufacture of exempted goods or in providing exempted services, other than the final products which are exempt from the whole of the duty of excise leviable thereon under Notification No, 8/2003 namely SMALL SCALE UNIT's exemption notification.

Rule 6(6): Goods sold to EOU, SEZ, EHTP, STP, UN Agencies: Dutiable goods removed without payment of duty to Export Oriented Units (EOUs), Special Economic Zone (SEZ units), Electronic Hardware Technology Park (EHTP), Software Technology Park (STP), United Nations (UN) agencies as per rule 6(6) of Cenvat Credit Rules, 2004, then the Cenvat credit on inputs/capital goods / input services used in the manufacture of such final products shall be allowed. It means CENVAT Credit need not required to be reversed or pay an 'amount'. It means these goods are not 'exempted goods'.

Exempted goods cannot be exported under bond & benefit of rule 6(6) of Cenvat Credit Rules, 2004 is not available. i.e. Manufacturer is not eligible to take Cenvat credit of Inputs/capital goods/input services used in such goods. It means these good are to be considered as exempted goods only.

Rule 6(8): A service provided or agreed to be provided shall not be an exempted service when:-

(a) the service satisfies the conditions specified under rule 6A of the Service Tax Rules, 1994 and the payment for the service is to be received in convertible foreign currency; and

(b) such payment has not been received for a period of six months or such extended period as may be allowed from time-to-time by the Reserve Bank of India, from the date of provision.

Provided that if such payment is received after the specified or extended period allowed by the Reserve Bank of India but within one year from such period, the service provider shall be entitled to take the credit of the amount equivalent to the CENVAT credit paid earlier in terms of sub-rule (3) to the extent it relates to such payment, on the basis of documentary evidence of the payment so received.

3.7 INPUT SERVICE DISTRIBUTOR

Rule 7: Manner of distribution of credit by input service distributor (w.e.f. 1-4-2012):

The input service distributor may distribute the CENVAT CREDIT in respect of the service tax paid on the input service to its manufacturing units or units providing output service, subject to the following conditions, namely:-

(a) The Input service distributor must ensure that such a distribution should not exceed the service tax paid.

(b) In case an input service is attributable to service use by one or more units exclusively engaged in manufacture of exempted goods or exempted services, then such credit of service tax shall not be distributed.

(c) Credit of service tax attributable to service used wholly by a unit shall be distributed only to that unit; and

(d) Credit of service tax attributable to service used by more than one unit shall be distributed prorata on the basis of the turnover of such unit to the total of the turnover of all the units, which are operational in the current year, during the said relevant period.

Rule 7A: Distribution of credit on inputs by the office or any other premises of output service provider:

Cenvat credit on input goods and capital goods can be distributed by the service provider only if such person registered as first stage dealer or a second stage dealer.

Rule 8: Storage of input outside the factory of the manufacturer: In exceptional cases, AC/DC may permit the manufacturer considering the nature of goods and shortage of space to store the inputs on which CENVAT credit has been availed, outside the factory premises. Condition may be prescribed to safeguard revenue. This relaxation is available only to inputs and not capital goods.

3.8 DOCUMENTS AND ACCOUNTS

Rule 9: Documents and accounts:

CENVAT Credit can be taken based on the following any documents:

- invoice
- supplementary invoice
- bill of entry
- invoice, bill or challan

The above documents if does not contain full information then deputy commissoiner or the assistant commissioner of central excise is satisfied that the said goods have been accounted for in the books of the assessee he may allow the Cenvat credit.

Rule 9(4): Purchases from first stage or second stage dealer

Rule 9(4) provides that CENVAT credit in respect of inputs and capital goods shall be allowed only if the dealer has maintained proper records and should indicate that the goods are cleared from the duty paid stock. CENVAT Credit shall be allowed only if the duty portion is expressly provided on the invoice *i.e.* on pro rata basis. The dealer should ensure that he has proper stock records to take care of this issue.

Rule 9(5): Admissibility of CENVAT Credit

Rule 9(5) of CENVAT Credit Rules provides that it is the duty of the manufacturer to prove the admissibility of credit and the manufacturer shall maintain proper records for receipt, disposal, consumption and inventory of input and capital goods. The manufacturer shall also' maintain a statement presenting the information as to value, availment and utilization of CENVAT credit and the name of the manufacturer or dealer from whom the inputs or capital goods were procured. In short the burden of proving the admissibility is on the person availing the CENVAT.

Return of CENVAT Credit

The manufacturers availing CENVAT benefits are required to file a CENVAT credit return along with monthly return within ten days' from the close of the month. The due date for filing of quarterly returns for SSI units is changed wherein it has to be filed within 10 days from the end of the quarter instead of

20 days from the end of the quarter. The dates are aligned with the date for Non-SSI units so that all the returns are required to be filed by 10th of the month following the said month for non SSI's and 10th of the month following the quarter for SSI units.

Rule 9A: Information in respect of Principal Inputs

The information that is required to be furnished under Rule 9A is:

- The Central Government has notified manufacturers who have remitted excise duty of more than one hundred lakhs during the preceding financial year to furnish the declaration in form ER 5 and monthly return in for ER 6.
- The manufacturer shall file a declaration in form ER 5 containing the information as to the excisable goods manufactured or to be manufactured and also the quantity of principal inputs required for manufacture of one unit of finished goods. The said declaration is to be made annually and filed within 30th April. If there is any alteration to the information already provided in ER 5, then the manufacturer shall within 15 days of such change, inform the superintendent of central excise.
- The manufacturer shall file a return in form ER 6 within 10 days from the end of month containing the details as to the quantity of finished goods manufactured and information relating to receipt and consumption of each principal input.
- Explanation to Rule 9A was provided to explain principal inputs to mean any input which is used in the manufacture of final product and the cost of such input is not less than 10% of the total cost of raw material for the manufacture of unit quantity of a given final product.

Rule 10: Transfer of CENVAT Credit

In terms of Rule 10 of CENVAT Credit Rules, relaxations in the form of transfer of credit is available to manufacturer of final products when the manufacturer shifts his factory to another location or transfers his business on account of change in ownership or on sale, merger, amalgamation, lease or transfers his property to a joint venture with the specific provision for transfer of liabilities, and only then the manufacturer shall be allowed to transfer the unutilized CENVAT credit to the transferee.

The transfer of unutilized credit is allowable only if the stock of inputs or inputs in process or capital goods is also transferred along with the factory and it should be duly accounted to the satisfaction of ACCE or DCCE.

Rule 10A: Inter-unit transfer of Additional CVD

A new Rule 10A is introduced wherein if manufacturer has more than one registered premises, it provides for transfer of CENVAT Credit of additional CVD (additional duty leviable under sub-section (5) of section 3 of the Customs Tariff Act) from one unit to another unit, such credit lying in balance at the end of quarter.—

The credit can be transferred as follows:

(i) making an entry for such transfer in the documents maintained for CENVAT Credit;

(ii) issuing a transfer challan containing registration number, name and address of the registered premises transferring the credit and receiving such credit, the amount of credit transferred and the particulars of such entry as mentioned in clause (/) above,

(iii) based on such transfer challan, the recipient premises may take CENVAT credit

The above benefit is restricted if the transferring unit is the benefit of following notification:

(a) 32/99- CE -Goods produced in specified areas like north-east, J&K, Uttarakhand, Himachal Pradesh, Sikkim and Kutch (Gujarat)

(b) 33/99-CE specified goods of factories in North-East (Assam, Tripura, Meghalaya, Meghalaya, Mizoram, Manipur, Nagaland or Arunachal Pradesh)

(c) 39/2001-CE - Exemption to excisable goods cleared from units in Kutch (Gujarat)

(d) 56/2002-CE - Exemption to all goods produced (except cigars, tobacco and its products, soft drinks and their concentrates) produced in Jammu & Kashmir by units located in Industrial Growth Centre, IIDC, EPIP or industrial Estate.

(e) 57/2002-CE - exemption to specified goods produced by units in Jammu & Kashmir

(f) 56/2003-CE - exemption to specified goods cleared from new units in Sikkim

(g) 71/2003-CE - Exemption to all goods produced(except cigars, tobacco and its products, Specified Carry bags, mineral oils, branded aerated beverages, pollution causing paper and paper products) Cleared from specified areas of Sikkim by unit in Industrial Growth Centre, IIDC, EPIP or industrial Estate from excise duty other than duty paid on account of Cenvat credit

(h) 20/2007-CE Exemption to north East including Sikkim on all goods (except as specified) cleared from Assam, Tripura, Meghalaya, Mizoram, Manipur, Nagaland or Arunachal Pradesh or Sikkim from duty Paid other than by utilization of Cenvat credit.

(i) 1/2010-CE - exemption to all goods except cigarettes, cigars, tobacco products and soft drinks or their concentrates cleared from new units (established/expanded after 6-2-2010) in J&K.

3.9 OTHER PROVISIONS

Rule 11: Transitional provision:

Final product fully exempted from Excise Duty due to any one of the following reasons:

(a) As per Rule 11(2) of the CENVAT Credit Rules, 2004, a manufacturer claiming CENVAT credit on inputs or input services, subsequently opt for full exemption from excise duty under Notification No. 8/2003 (i.e. Small Scale Industrial (SSI) exemption).

(b) As per Rule 11(3) of the CENVAT Credit Rules, 2004, a manufacturer of final product opts for full exemption from excise duty, if the said final products are exempted absolutely under section 5A of the Central Excise Act, 1944.

(c) As per Rule 11(4) of the CENVAT Credit Rules, 2004, a service provider opts for full exemption from payment of tax on his output service.

In such cases, an '*amount*' is payable equivalent to CENVAT credit taken on such —

- inputs lying in stock or
- inputs lying in process or
- inputs contained in final products or
- input services.

The said '*amount*' can be paid by utilizing the CENVAT credit receivable account. The balance CENVAT credit, if any, receivable will lapse.

Rule 12: Special Dispensation in respect of inputs manufactured in factories located in specified areas of North East region, Kutch district of Gujarat, State of Jammu & Kashmir and State of Sikkim where a manufacturer has cleared any inputs or capital goods, in terms of notifications of the Govt. of India, the cenvat credit on such inputs or capital goods shall be admissible as if no portion of the duty paid on such inputs or capital goods was exempted under any of the said notifications.

Rule 12A: Large Tax payer Unit (LTU) — Special Enabling provisions

Large tax payer means any person, engaged in the manufacture or production of goods, except the goods falling under chapter 24 or Pan Masala falling under chapter 21 of the First schedule of the Central Excise Tariff Act, 1985 and has remitted during the financial year preceding the year under consideration:

(i) Duties of excise of more than rupees five hundred lakhs in cash or through account current; or

(ii) Advance tax of more than rupees ten hundred lakhs, under the Income Tax Act, 1961.

Rule 12A facilitates the large tax payer to remove CENVATABLE inputs or capital goods except petrol, diesel and LDO without payment of duty under CENVAT Credit Rules either under the cover of an invoice or challan to another premise for further use in the manufacture of final products in the recipient premises provided that:

- The goods are manufactured using the said transferred inputs and are cleared on payment of duty or exported under bond or letter of undertaking within a time span of six months from the receipt of such inputs.
- Any other conditions that are prescribed by the Principal Commissioner or Commissioner of Central Excise would have to be followed.
- Explanation is provided prescribing the requirements that the transfer challan shall be serially numbered containing registration number, name, address of the transferor unit, description, classification, time and date of removal, mode of transport and vehicle registration number, quantity of goods and registration number and name of the consignee.

If default is made in following the above mentioned procedure or conditions stipulated by the Principal Commissioner or Commissioner of Central Excise or the inputs are cleared as such, then the large tax payer shall pay an amount equal to the credit taken in respect of such inputs along with interest specified under Rule 14 of the CENVAT Credit Rules.

Yet another proviso is added to recover CENVAT credit availed on capital goods by the LTU, when the capital goods are exclusively used in manufacture of exempted goods or such goods are cleared from recipient premises. However in this case too recovery is made from the recipient's premises along with interest specified under Rule 14 of CENVAT Credit Rules.

The above conditions shall not be applicable if the recipient is availing either the benefits under Notifications provided below or the unit is an export oriented unit or a unit located in electronic hardware technology park (EHTP) or software technology park (STP).

No 32/99, dt. 8-7-1999	33/99 dt. 8-7-1999	39/2001 dt. 31-7-2001
56/2002, dt. 14-11-2002	57/2002 dt. 14-11-2002	56/2003 dt. 25-6-2003
71/2003, dt. 9-9-2003	20/2007 dt. 25-4-2007	01/2010-CE dt. 6-2-2010

The other salient features of this Rule are provided below:

- The first recipient premise may avail the benefit of CENVAT credit of the amount paid under the proviso discussed above as if the duty is discharged by the sender premises and the document should expressly provide duty details.
- The CENVAT credit of any specified duties availed under Rule 3 of CENVAT Credit Rules shall neither be denied or varied in respect of input or capital goods if removed as such under Rule 12(1) and cannot be treated as removed without payment of duty under Rule 3(5) of the CENVAT Credit Rules or the said inputs or capital goods arc used in the manufacture of intermediate goods which are removed without payment of duty under Rule 12BB of Central Excise Rules.
- The large tax payer unit (LTU) shall submit a monthly return for each of the registered premises.

Rule 12A (4): Transfer of Credits within units

A large taxpayer may transfer, CENVAT credit taken on or before the 10th July, 2014, by one of his registered manufacturing premises or premises providing taxable service to his other such registered premises by

(i) making an entry for such transfer in the record maintained under rule 9;

(ii) issuing a transfer challan containing registration number, name and address of the registered premises transferring the credit as well as receiving such credit, the amount of credit transferred and the particulars of such entry as mentioned in clause (i), and such recipient premises can take CENVAT credit on the basis of such transfer challan as mentioned in clause (ii),

Provided that such transfer or utilization of CENVAT credit shall be subject to the limitations prescribed under clause (b) of sub-rule (7) of rule 3.

Rule 12AAA: Power to impose restrictions in certain types of cases

Where the Central Government, having regard to the extent of misuse of CENVAT credit, nature and type of such misuse and such other factors as may be relevant, is of the opinion that in order to prevent the misuse of the provision of CENVAT credit as specified in these rules, it is necessary in the public interest to provide for certain measures including restrictions on a manufacturer, first stage and second stage dealer, provider of taxable service or an exporter or a registered importer may by notification in the Official Gazette specify the nature of restrictions on utilization of CENVAT credit and suspension of registration in case of a dealer and type of facilities to be withdrawn and procedure for issue of such order by the Chief Commissioner of Central Excise.

Notification No. 16/2014 dated 21st March, 2014:

In pursuance of rule 12CCC of the Central Excise Rules, 2002, and rule 12AAA of the CENVAT Credit Rules, 2004 and in supersession of the notification of the Government of India in the Ministry of Finance, Department of Revenue, No. 05/2012-Central Excise (N.T.), dated the 12th March, 2012, published in the Gazette of India, Extraordinary, Part II, Section 3, Sub-section (i) vide number G.S.R. 140(E), dated the 12th March, 2012, except as respects things done or omitted to be done before such supersession, the Central Government hereby declares that where a manufacturer, first stage or second stage dealer, or an exporter including a merchant exporter or a registered importer is prima facie found to be knowingly involved in any of the following :-

(a) removal of goods without the cover of an invoice and without payment of duty;

(b) removal of goods without declaring the correct value for payment of duty, where a portion of sale price, in excess of invoice price, is received by him or on his behalf but not accounted for in the books of account;

(c) taking of CENVAT Credit without the receipt of goods specified in the document based on which the said credit has been taken;

(d) taking of CENVAT Credit on invoices or other documents which a person has reasons to believe as not genuine;

(e) issuing duty of excise invoice without delivery of goods specified in the said invoice;

(f) claiming of refund or rebate based on the duty of excise paid invoice or other documents which a person has reason to believe as not genuine;

(g) removal of inputs as such on which Cenvat credit has been taken, without paying an amount equal to credit availed on such inputs in terms of sub-rule (5) of rule 3 of the Cenvat Credit Rules, 2004, the Chief Commissioner of Central Excise may order for withdrawal of facilities or impose the restrictions as specified in para 2 of this notification.

2. Facilities to be withdrawn and imposition of restrictions.-

(1) Where a manufacturer is prima facie found to be knowingly involved in committing the offences specified in para 1, the Chief Commissioner of Central Excise may impose following restrictions on the facilities, namely:-

(i) the monthly payment of duty of excise may be withdrawn and the assessee shall be required to pay duty of excise for each consignment at the time of removal of goods;

(ii) payment of duty of excise by utilisation of CENVAT credit may be restricted and the assessee shall be required to pay duty of excise without utilising the CENVAT credit;

(iii) the assessee may be required to maintain records of receipt, disposal, consumption and inventory of the principal inputs on which CENVAT credit has not been taken;

(iv) the assessee may be required to intimate the Superintendent of Central Excise regarding receipt of principal inputs in the factory on which CENVAT credit has or has not been taken, within a period specified in the order and the said inputs shall be made available for verification upto the period specified in the order.

Provided that where a person is found to be knowingly involved in committing any one or more type of offences as specified in para 1 subsequently, every removal of goods from his factory may be ordered to be under an invoice which shall be countersigned by the Inspector of Central Excise or the Superintendent of Central Excise before the said goods are removed from the factory or warehouse.

Explanation.- For the purposes of this paragraph, it is clarified that-

(i) a person against whom the order under sub-para (2) of para 4 has been passed may continue to take CENVAT credit, however, he would not be able to utilize the credit for payment of duty during the period specified in the said order.

(ii) principal inputs means any input which is used in the manufacture of final products where the cost of such input constitutes not less than 10% of the total cost of raw materials for the manufacture of unit quantity of a given final product.

(iii) if the assessee commits any offence specified in para 1 for the first time, the period of imposition of restrictions may not be more than 6 months.

(iv) if the assessee commits any offence specified in para 1 subsequently, the period of imposition of restrictions shall not be more than 1 year.

(2) Where a first stage or second stage dealer is found to be knowingly involved in committing the type of offence specified at clauses (d) or (e) of para 1, the Chief Commissioner of Central Excise may order suspension of the registration granted under rule 9 of the Central Excise Rules, 2002 for a specified period.

(3) During the period of suspension, the said dealer shall not issue any Central Excise Invoice.

Provided that he may continue his business and issue sales invoices without showing duty of excise in the invoice and no CENVAT credit shall be admissible to the recipient of goods under such invoice.

(4) Where a merchant exporter is found to be knowingly involved in committing the type of offence specified in clause (f) of para 1, the Chief Commissioner of Central Excise may order withdrawal of the self sealing facility for export consignment and each export consignment shall be examined and sealed by the jurisdictional Central Excise Officer:

(5) If a manufacturer, first stage dealer or second stage dealer or an exporter or an registered importer does anything specified in clause (f) of para 1, the Chief Commissioner of Central Excise may order withdrawal of the other facility available to them.

3. Monetary limit.- The provisions of this notification shall be applicable only in a case where the duty of excise or CENVAT Credit alleged to be involved in anything specified in para 1 exceeds rupees ten lakhs.

4. Procedure.-

(1) The Commissioner of Central Excise or Additional Director General of Central Excise Intelligence, as the case may be, after examination of records and other evidence, and after

satisfying himself that the person has knowingly committed the offence as specified in para 1, may forward a proposal to the Chief Commissioner of Central Excise, to withdraw the facilities and impose restriction during or for such period, within 30 days of the detection of the case, as far as possible.

(2) The Chief Commissioner of Central Excise shall examine the said proposal and after satisfying himself that the records and evidence relied upon in the said proposal are sufficient to form a reasonable belief that the person has knowingly done or contravened anything specified in para 1, may issue an order specifying the type of facilities to be withdrawn or type of restrictions to be imposed, along with the period for which the said facilities will not be available or the period for which the restrictions shall be operative:

Provided that the Chief Commissioner of Central Excise, before issuing the order, shall give an opportunity of being heard to the person against whom the proceedings have been initiated and shall take into account any representation made by such person before he issues the order.

5. Proposals which are pending before the officer authorized by the Central Board of Excise and Customs or the Director General of Central Excise Intelligence in terms of notification no. 05/2012-Central Excise (N.T.), dated the 12th March, 2012, on the date of coming into force of this notification, shall be transferred to the Chief Commissioner of Central Excise, who shall decide the same in accordance with the procedure specified in paragraph 4 and the proposals pending before the Chief Commissioner of Central Excise shall also be decided accordingly.

Rule 13: Power of Central Government to notify goods for deemed CENVAT credit

The Central Govt. may, by notification, declare the input or input service on which the duties of excise, or additional duties of customs or service tax paid, shall be deemed to have been paid at such rate or equivalent to such amount as may be specified in that notification and allow CENVAT CREDIT of such duty or tax deemed to have been paid in such manner and subject to such conditions as may be specified in that notification even if, in the case of input, the declared input, or in the case of input service, the declared input service, as the case may be, by the provider of taxable service, declared in that notification, but contained in the said final products, or as the case may be, used in providing the taxable service.

Rule 14: Recovery of CENVAT credit wrongly taken or erroneously refunded (w.e.f 1-4-2012)

Where the CENVAT Credit has been taken and utilized wrongly or has been erroneously refunded, the same alone with interest shall be recovered from the manufacturer or the provider of the output service and the provisions of sections 11A and 11AA of the Excise Act, or section 73 and 75 of the Finance Act, shall apply mutatis mutandis for effecting such recoveries.

Rule 15: Confiscation and penalty in case of wrongly or in contravention of any provisions of these rules

If any person, takes or utilizes CENVAT Credit in respect of input or capital goods or input services, wrongly or in contravention of any of provisions of these rules, then, all such goods shall be liable to confiscation and such person shall be liable to a penalty: ₹ 2,000 or duty / service tax on such goods or services whichever is higher is the penalty.

Rule 15A: General penalty

Whoever contravenes the provisions of these rules for which no penalty has been provided in the rules, he shall be liable to a penalty which may extend to ₹ 5,000.

Rule 16: Supplementary provisions (i.e. any notification, circular, instruction, standing order, trade notices or other orders issued under the CENVAT Credit Rules, 2002 or the Service Tax Credit Rules, 2002 by the Central Govt., shall be deemed to be valid under CENVAT Credit Rules, 2004.

PRACTICAL PROBLEMS WITH ANSWERS

Payment of Excise Duty after Adjusting Cenvat Credit

Example 11: An assessee cleared various manufactured final products during June 2015. The duty payable for June 2015 on his final products was as follows:

Basic Excise duty ₹ 2,00,000.

During June he received various inputs on which total duty paid by suppliers of inputs was as follows:

Basic Excise Duty ₹ 50,000.

Excise duty paid on capital goods received during the month was as follows: Basic Excise Duty ₹ 12,000.

Service Tax paid on input services was as follows:

Service Tax ₹ 10,000.

Due date of payment of duty is 6th July 2015. He receives some inputs on 4th July, 2015 on which the excise duty paid is ₹ 1,000. Compute the amount of excise duty payable by him for the month of June 2015?

Answer :

Excise duty liability for the month of June 2015

Particulars	**BED** (₹)	**ST** (₹)
On final product:		
Duty payable	2, 00,000	
Input tax credit On other than capital goods On capital goods On input services	50,000 6,000 -	 - 10,000
CENVAT Credit	56,000	10,000
Net duty payable (₹)	1,34,000	

Note: Input tax credit ₹ 1,000 received during the month of July 2015 can be adjusted against the duty liability due as on 31st July, 2015.

Example 12: A manufacturer purchased certain inputs from Z. The, assessable value was ₹ 20,000 and the Central Excise duty was calculated at ₹ 3,296 making a total amount of invoice at ₹ 23,296. However, the buyer manufacturer paid only ₹ 20,800 to Z in full settlement of this bill. How much CENVAT credit can be availed by the manufacturer and why?

Answer :

CENVAT credit that can be availed by the manufacturer is ₹ 3,296.

CENVAT credit cannot be reversed just because the supplier of inputs has given some reduction in price after removal of goods or the buyer manufacturer paid only reduced amount than that of invoice [unless supplier of inputs claims and get refund of excise duty paid by him].

[*CCE* v *Trinetra Texturisers* 2004 (CESTAT].

Example 13: Prepare a CENVAT account in the books of A Ltd., and determine the balance as on 31.3.2016 from the following data:-

(i) Opening balance as on 1.8.2015 ₹ 47,000

(ii) Inputs received on 15.8.2015 involving excise duty paid ₹ 14,747

(iii) Purchased a Lathe for ₹ 1,10,300 (excise duty @10.30% inclusive) on 5.10.2015 and received the Lathe into factory on 1.4.2016.

(iv) On 6.10.2015 paid excise duty on final products @10.30% through CENVAT credit account (cum duty price of the goods ₹ 3,52,960).

(v) Inputs worth ₹ 2,00,000 (excise duty @16.48%) cleared as such to a job worker on 1.7.2015, these goods were received back on 1.4.2016.

(vi) Common inputs were used for manufacture of dutiable and exempted final products. Manufacturer opted to pay 6% as an amount on exempted final products. These goods (1,000 units) are cleared from the factory on 1.12.2015 at a price of ₹ 100 per unit inclusive of VAT ₹ 20 per unit.

(vii) On 15.3.2016 duty paid on input amounting to ₹ 1 7,867 was taken credit for in the CENVAT account as ₹ 17,687.

Answer :

In the books of A Ltd.

Dr. **CENVAT Credit Receivable Account for the Year 2015-16** **Cr.**

Date	Particulars	Amount (₹)	Date	Particulars	Amount (₹)
1.8.2015	To Opening bal. b/d	47,000	6.10.2015	By Excise duty payable	32,960
15.8.2015	To Bank	14,747	1.12.2015	By Profit and Loss A/c (6% on final goods exempted from duty)	4,800
15.3.2016	To Bank	17,687	28.12.2015	By Profit and Loss A/c (reversal of CENVAT credit on 181 days)	32,960
31.3.2016	To Bank	180	31.3.2016	By Balance c/d	8,894
	TOTAL	**79,614**		**TOTAL**	**79,614**
1.4.2016	To Opening bal. b/d	9,694			

Note:

(1) Purchased a lathe (i.e. Capital goods) for ₹ 1,10,300 (excise duty @10.30% inclusive) on 5.10.2015 and received the lathe into factory on 1.4.2016.

Excise duty = ₹ 10,300 (i.e. ₹ 1,10,300 x 10.30/110.30).

Up to 50% of ₹ 10,300 is allowed in the year of receipt of capital goods and balance will be allowed in the subsequent year or years. However, lathe received into factory on 1.4.2016, and hence, ₹ 5,150 can be allowed as CENVAT credit in the year 2016-17 and balance in the subsequent year. Thereby, no CENVAT credit is allowed for the year ended 31st March, 2016.

(2) On 6.10.2015 paid excise duty on final products @10.30% through CENVAT credit account (cum duty price of the goods ₹ 3,52,960).

Excise duty on final goods = ₹ 32,960 (i.e. ₹ 3,52,960 x 10.30 /110.30)

(3) Inputs worth ₹ 2,00,000 (excise duty @16.48%) cleared as such to a job worker on 1.7.2015, these goods were received back on 1.4.2016.

In case goods sent for job work are not returned within 180 days from the date of dispatch, then the input tax credit on those goods need to reverse or pay the amount equal to input tax credit availed. Therefore, on 28th Dec 2015 CENVAT credit of ₹ 32,960 has been reversed (i.e. on 181 day).

However, CENVAT credit is allowed only when these goods were returned to factory. In the given case these goods are returned into factory on 1.4.2016, and hence, the manufacturer is eligible to take credit on 1.4.2016.

(4) Common inputs were used for manufacture of dutiable and exempted final products. Manufacturer opted to pay 6% as an amount on exempted final products. These goods are cleared from the factory on 1.12.2015 at a price of ₹ 100 per unit inclusive of VAT ₹ 20 per unit.

Assessable value = ₹ 80 per unit (i.e.₹ 100 – ₹ 20)

An Amount = ₹ 4,800 (i.e. 1,000 units x ₹ 80 x 6%)

Example 13: M/s X & Co. Ltd. have cleared their goods manufactured final products during April, 2015 and the duty payable is ₹ 2,40,000 plus. Given below are the details of excise duty payable by them during the month at the time of purchase of goods.

		₹	
(i)	On inputs (RM)	1,00,000	(Invoice for excise duty of ₹ 20,000 paid was received by the assessee on 4.5.2015)
(ii)	On input service	20,000	
(iii)	On welding electrodes for repairs and maintenance of capital goods	5,000	
(iv)	Fuel (excluding HSD/Petrol)	6,000	
(v)	Storage tank	8,000	
(vi)	Tubes and Pipes (used in the factory)	14,000	
(vii)	Air Conditioner for the office of the Factory Manager	12,000	

Note: Find the total duty payable by the assessee for the month of April, 2015 after taking into account the Cenvat credit available.

Answer :

Cenvat Credit receivable as on 30th April 2015: (value in ₹)

Sl. No.	Particulars	Basic Excise Duty (₹)	Service Tax (₹)	Remarks	Workings
(i)	Input Goods	80,000	-	₹20,000 allowed as Cenvat credit in the month of May 2015.	₹ 1,00,000 - ₹ 20,000 = ₹ 80,000
(ii)	Input services		20,000	It is assumed that input service tax was paid	
(iii)	On welding electrodes for repairs and maintenance of capital goods	2,500		Considered as capital goods as per the Supreme Court judgment in case of *Hindustan Zinc Ltd.*	₹ 5,000 x 50% = 2,500
(iv)	Fuel (excluding HSD/ Petrol)	6,000		Considered as inputs	

(v)	Storage tank	4,000		Capital goods	₹ 8,000 x 50% = ₹ 4,000
(vi)	Tubes and Pipes (used in the factory)	7,000		Capital goods	₹ 14,000 x 50% = ₹ 7,000
(vii)	Air Conditioner for the office of the Factory Manager	—	—	Not considered as input goods	
	CENVAT Credit Receivable at the end of April 2014	99,500	20,000		

Excise duty payable for the month of April, 2015; **(Value in ₹)**

Sl. No.	Particulars	Basic Excise Duty (₹)	Service Tax (₹)	Remarks	Workings
(i)	Output	2,40,000	--		
	Total	2,40,000	--		

Statement showing total duty payable by the assessee for the month of April 2015: **(Value in ₹)**

Sl. No.	Particulars	Basic Excise Duty (₹)	Service Tax (₹)	Remarks	Workings
(i)	Output	2,40,000	--		
(ii)	CENVAT Credit Receivable	1,19,500	--		₹ 99500 + ₹ 20,000 = ₹ 1,19,500
	Excise Duty liability after CENVAT Credit.	1,20,500	--		

Eligibility of CENVAT Credit

Example 14: C Limited is engaged in manufacturing water pipes. Compute the CENVAT credit admissible to C Ltd. The excise duty paid at the time of purchase of following goods is:—

	(Value in ₹)
Raw Steel	12,000
Water pipe making machine	25,000
Lubricating oil	2,000
Equipments used in the office	10,000
Petrol	15,000
Pollution control equipment	22,000
Components, spares and accessories used in machinery	12,000

Answer :

Calculation of Cenvat Credit admissible to C Ltd.

Particulars	Nature of goods	Value (₹)	Eligibility	Cenvat Credit (₹)
Raw Steel	Other than capital goods	12,000	100%	12,000
Water pipe making machine	Capital goods	25,000	50%	12,500
Lubricating oil	Other than capital goods	2,000	100%	2,000
Equipment used in office	Capital goods	10,000	Not eligible	----
Petrol	Other than capital goods	15,000	Not eligible	----
Pollution control equipment	Capital goods	22,000	50%	11,000
Components, spares and accessories used in machinery capital goods	Capital goods	12,000	50%	6,000
Total Cenvat Credit admissible				43,500

Example 15: Following transactions took place in the factory of A Ltd.:

(i) An imported consignment of raw materials was received vide Bill of Entry dated 2.12.15 showing the following customs duty payments: Basic Customs duty ₹ 25,000; Additional duty (CVD) ₹ 20,000; Special Additional duty ₹ 5,800.

(ii) A consignment of 1,000 kgs of inputs was received. The Excise duty paid as per the invoice was ₹ 10,000. While the input was being unloaded 50 kgs were damaged and were found to be not usable.

(iii) A vehicle containing machinery was received. The machinery was purchased through a dealer and not from the manufacturer. The dealer's Invoice No. 925, dated 3.9.15 marked 'original for buyer' certified that the excise duty paid by the manufacturer of machinery was ₹ 24,000. The dealer is registered with the Central Excise Authorities.

(iv) Some inputs for final products were received. These were accompanied by a certified Xerox copy (photo copy) of Invoice No. 286 dated 15.1.2016 indicating that Excise duty of ₹ 6,400, has been paid on inputs. The original or duplicate copies of invoice are not traceable.

Indicate the eligibility of CENVAT Credit in each case under the CENVAT Credit Rules, 2004 with explanations where necessary.

Answer :

(i) CENVAT credit available for the following:

Additional duty (CVD) ₹ 20,000;

Special Additional duty ₹ 5, 800

(ii) CENVAT credit available for 950 Kgs

Eligible CENVAT credit = ₹ 10,000 x 950/1000 = ₹ 9,500.

(iii) CENVAT credit can be availed if the goods are purchased from a first or second stage dealer. The eligible CENVAT credit for the first year = ₹ 24,000 x 50% = ₹ 12,000.

The balance CENVAT credit for the second and subsequent years

(iv) CENVAT credit is not available based on the certified Xerox copy of invoice. CENVAT credit can be availed only when any one of the following invoices available:

(a) Original for buyer

(b) Duplicate for transporter

(c) Triplicate for seller.

However, It is pertinent to note that the High Court held that Cenvat Credit could be taken on the strength of private challans (i.e. other than prescribed documents) as the same were not found fake and there was proper certification that duty has been paid ***(CCEx.* v *Stelko Strips Ltd.* 2010 (255) E.L.T. 397 (P&H)).**

Therefore in the given case Xerox copy of invoice can be considered as a valid document for taking CENVAT credit.

Removal of Capital Goods after use

Example 16: X Ltd received capital goods on 15-12-2012 for ₹ 9,00,000 (Excise Duty @ 10.30%). The said machinery was sold for ₹ 5,50,000 from the factory after being used in the manufacture of dutiable goods on 1st July 2015. Excise duty attributable for said machine at the time of removal @12.5%. You are required to compute the amount of CENVAT credit to be reversed.

Answer :

Year	No. of quarters	Workings
2012	1	October to December
2013	4	January to December
2014	4	January to December
2015	3	January to September
Total	12	

Statement Showing CENVAT Credit to be Reversed:

Particulars	Amount (₹)	workings
Cenvat credit taken on capital goods	92,700	9,00,000 x 10.30%
Less: Reduction @2.5% per quarter or part thereof from the date of taking Cenvat credit up to the date of removal 46,350 x 2.5% x 12 quarters = ₹ 13,905 46,350 x 2.5% x 10 quarters = ₹ 11,588	(25,493)	Up to 50% taken on 15-12-2012 (2012-2013) Balance 50% taken on 1-4-2013 (2013-14)
Amount to be paid	67,207	
Or		
Excise duty on transaction value	68,750	5,50,000 × 12.5%
Amount payable or credit to be reversed under Rule 3(5A) of Cenvat Credit Rules, 2004.	68,750	Whichever is higher is required to pay as an 'AMOUNT'

Dutiable and non Dutiable Goods Manufactured

Example 17: Mr. A is manufacturing goods with other's brand name. Mr. A has manufactured goods of ₹ 90,00,000 in the FY 2015-16. Out of this, ₹ 70,00,000 are taxable final products and ₹ 20,00,000 are exempt final products.

Excise duty paid on his inputs is ₹ 10,00,000.

Rate of basic excise duty on final products is 12.5%.

Discuss the options available to Mr. A for availment of CENVAT credit, if he is not able to bifurcate inputs between those used for exempt goods and taxable final products. Calculate CENVAT credit available to him under different options and explain which option is beneficial to him.

Answer :

Option 1:

Maintain separate records for taxable and exempted goods and accordingly take the credit attributable for taxable final goods.

Option 2:

Excise duty on taxable goods	=	₹ 8,75,000	(i.e. ₹ 70,00,000 × 12.5%)
Less: CENVAT credit allowed	=	₹ (10,00,000)	
Excess Credit	=	₹ (1,25,000)	
Add: 6% amount payable on exempted goods	=	₹ 1,20,000	(i.e. ₹ 20,00,000 × 6%)
Net Excess credit	=	₹ 5,000	

Option 3:

Excise duty payable on taxable goods	=	₹ 8,75,000
Less: proportionate credit allowed		
(₹ 10,00,000 x ₹ 70 lacs /₹ 90 lacs)	=	₹ 7,77,778
Net Excise Duty payable by GAR -7 Challan	=	₹ 97,222

Option 2 is beneficial.

Study Note - 4

CUSTOMS LAW

This Study Note includes

4.1 INTRODUCTION

4.1.1 Customs duty is on imports into India and export out of India. The power to levy customs duty is derived from Entry 83 of Union List of the Seventh Schedule to the Constitution of India, which reads as, "Duty of Customs including export duties".

Thus, the power to make laws in respect of Customs duty vests with the Central Government. The tax receipts on account of customs duty-are solely enjoyed by the Union.

Section 12 of Customs Act, often called charging section, provides that duties of customs shall be levied at such rates as may be specified under 'The Customs Tariff Act, 1975', or any other law for the time being in force, on goods imported into, or exported from, India.

The body of the Customs Law comprises of -

(1) The Customs Act, 1962	This is a consolidating enactment providing levy of import and export duties of customs on goods imported into or exported from India through sea, air or land. It provides for the provisions of levy and collection of duty, importation or exportation, transit and transhipment, prohibition on importation or exportation of goods, warehousing, duty drawback, appeals, settlement commission, advance rulings, offences and penalties etc.
(2) The Customs Tariff Act, 1975	The Act contains various types of custom duties to be levied on the importation and exportation of the articles. It contains two Schedules - Schedule I known as, 'Import Tariff and Schedule II known as, 'Export Tariff.' 'Import Tariff consists of 98 Chapters grouped under 21 Sections. This Schedule refers to goods liable to import duty of customs. 'Export Tariff refers to goods liable to export duty of customs.
(3) Rules	Section 156 of the Customs Act, 1962 empowers the Central Government to make rules consistent with this Act. Such rules may provide for matters relating to the manner of determining the price of imported goods, duty drawback, baggage, detention and confiscation of goods etc.
(4) Regulations	Section 157 of the customs Act, 1962 empowers the Central Board of Excise and Customs to make regulations consistent with the Act and the rules, generally to carry out the purposes of the Act. For example, Import Manifest Vessels Regulation, Boat Note Regulations, Export Manifest Vessel Regulations have been framed in this regard.
(5) Notification under Customs Act	Notification, as per Article 13(3)(a) of the Constitution of India, means 'a written or printed matter that give notice'. Central Government has been empowered to issue notifications under various sections of the Customs act, 1962.

i. There are many common provisions in Central Excise and Customs Law.

ii. In case of imports, taxable event occurs when goods mix with landmass of India - *Kiran Spinning Mills* v. *CC* 1999(113) ELT 753 = AIR 2000 SC 3448 = 2000 AIR SCW 2090 (SC 3 member bench).

iii. In case of warehoused goods, the goods continue to be in customs bond. Hence, ' import' takes place only when goods are cleared from the warehouse - confirmed in *UOI* v. *Apar P Ltd.* 1999 AIR SCW 2676 = 112 ELT3 = 1999(6) SCC 118 = AIR 1999 SC 2515 (SC 3 member bench).-followed in *Kiran Spinning Mills* v. *CC* 1999(113) ELT 753 = AIR 2000 SC 3448 = 2000 AIR SCW 2090 (SC 3 member bench).

iv. In case of exports, taxable event occurs when goods cross territorial waters of India –*UOI* v. *Rajindra Dyeing and Printing Mills* 2005 (180) ELT 433 (SC)

v. Territorial waters of India extend upto 12 nautical miles inside sea from baseline on coast of India and include any bay, gulf, harbour, creek or tidal river.

   (1 nautical mile = 1.1515 miles = 1.853 Kms).

   Sovereignty of India extends to the territorial waters and to the seabed and subsoil underlying and the air space over the waters.

vi. Indian Customs waters extend upto 12 nautical miles beyond territorial waters. Powers of customs officers extend upto 12 nautical miles beyond territorial waters.

vii. '*Exclusive economic zone*' extends to 200 nautical miles from the base-line.

4.1.2 Common Aspects of Customs and Central Excise

i. There are many common links between Customs and Central Excise.

ii. Both are Central Acts and derive power of levy from list I - Union List - of the Seventh Schedule to Constitution.

iii. Both are under administrative control of one Board (Central Board of Excise and Customs) under Ministry of Finance.

iv. Organizational hierarchy is same from top upto Assistant Commissioner level. Transfers from customs to excise and *vice versa* are not uncommon.

v. Principal Chief Commissioner or Chief Commissioner in charge of each Zone is same for excise and customs at many places.

vi. In the interior areas, Excise officers also work as customs officers.

vii. Classification Tariffs of both acts are based on HSN and principles of classification are identical.

viii. Principles of deciding 'Assessable Value' have some similarities i.e. both are principally based on 'transaction value'. Concept of 'Related Person' appears in Customs as well as Excise valuation.

ix. Provisions of refund, including principle of 'Unjust Enrichment' are similar. Provisions for interest for delayed payment are also identical.

x. Provisions of raising demand for short levy, non-levy or erroneous refund are similar. Provisions in respect of recovery, mandatory penalties etc. are also similar.

xi. Provisions for granting exemptions from duty - partial or full, conditional or unconditional are identical.

xii. Powers of search, confiscations etc. are quite similar in many respects. In fact, some of provisions of Customs Act have been made applicable to Central Excise with suitable modifications.

xiii. Provisions in respect of Settlement Commission and Authority for Advance Ruling are identical.

xiv. Appeal provisions are identical.

xv. Appellate Tribunal (CESTAT) is same. Hence, procedures of appeal to Tribunal are identical.

4.1.3 Definitions Under Customs Act, 1962

1) **Adjudicating Authority [Section 2(1)]:** Adjudicating authority means any authority competent to pass any order or decision under this Act, but does not include:
   - The Central Board of Excise and Customs (CBE&C),
   - Commissioner of Customs (Appeals) or
   - Customs, Excise and Service Tax Appellate Tribunal (CESTAT)

2) **Assessment [Section 2(2)]:** Assessment means process of determining the tax liability in accordance with the provisions of the Act, which includes provisional assessment, self assessment, reassessment and any assessment in which the duty assessed is nil.

3) **Appellate Tribunal [Section 2(1B)]:** Appellate Tribunal means the Customs, Excise and Service Tax Appellate Tribunal constitute under section 129.

4) **Baggage [Section 2(3)]:** Baggage includes unaccompanied baggage but does not include motor vehicles.

5) **Bill of Entry [Section 2(4)]:** Bill of Entry means a bill of entry referred to in section 46. Bill of entry is the basic document for assessment of custom duty. The importer has to present bill of entry for clearance of imported goods.

6) **Board [Section 2(6)]:** Board means the Central Board of Excise and Customs constituted under the Central Board of Revenue Act, 1963.

7) **Bill of Export [Section 2(5)]:** The exporter of any goods shall make entry thereof by presenting to the proper officer in the case of goods to be exported by land, a bill of export in the prescribed form.

8) **Customs Airport [Section 2(10)]:** Customs airport means,-
   - Any airport appointed under section 7(a) to be a customs airport, and
   - Includes a place appointed u/s 7(aa) to be an air freight station.

9) **Conveyance [Section 2(9)]:** 'Conveyance includes a Vessel, an Aircraft and a Vehicle'. The specific terms are vessel (by sea), aircraft (by air) and vehicle (by land).

10) **Coastal Goods [Section 2(7)]:** The term coastal goods means goods, other than imported goods, transported in a vessel from one port in India to another.

    Under section 7(1)(d) of the Customs Act, 1962, the Central Board of Excise and Customs (CBE&C), may by notification in the Official Gazette, appoint the ports which alone shall be coastal ports for the carrying on of trade in coastal goods or any class of such goods with all or any specified ports in India.

11) **Customs Area [Section 2(11)]:** Customs area means the area of a customs station and includes any area in which imported goods or exported goods are ordinarily kept before clearance by Customs Authorities.

12) **Customs Port [Section 2(12)]:** Customs port means any port appointed under section 7(a) of the Customs Act, to be a customs port and includes a place appointed under section 7(aa) of the Customs Act, to be an inland container depot (ICD).

13) **Customs Station [Section 2(13)]:** Customs station means any customs port, customs airport or land customs station.

    As per Section 8 of the Customs Act, 1962, the Principal Commissioner or Commissioner of Customs may (i) approve proper places in any customs port or customs airport or coastal port for the unloading of goods or for any class of goods; (ii) specify the limits of any customs area.

    As per Section 141 of the Customs Act, 1962, all conveyances and goods in customs area are subject to control of officers of customs for enforcing the provisions of the Customs Act, 1962. The receipt/storage/delivery/dispatch/any other handling of goods (import/export) in the Customs area shall be in the prescribed manner and the responsibility thereon lies on the persons engaged in such activities (i.e. Custodian of the said goods).

14) **Customs Act,** 1962 and Customs Tariff Act, 1975 have been extended to whole of Exclusive Economic Zone (EEZ) and Continental Shelf of India for the purpose of (i) processing for extraction or production of mineral oils and (ii) Supply of any goods in connection with processing for extraction or production of mineral oils.

    Say for example, Goods imported by the assessee for consumption on oil rigs which are situated in Continental Shelf/Exclusive Economic Zones of India, are deemed to be a part of Indian Territory. Therefore, the supply of imported spares or goods or equipments to the rigs by a ship will attract import duty *[Aban Lloyd Chilies Offshore Ltd.* v *UOI* (2008) 227 ELT24 (SC)].

15) **Dutiable Goods [Section 2(14)]:** The term is defined to mean any goods which are chargeable to duty and on which duty has not been paid. It means to say that the name of the product or goods should find a mention in the Customs Tariff Act.

16) **Domestic Tariff Area** means the whole of India (including the territorial waters and continental shelf) but does not include the areas of the Special Economic Zones (Section 2(i) of Special Economic Zones Act, 2005), 100% Export Oriented Units (EOUs)/Electronic Hardware Technology Park (EHTP)/ Software Technology Park (STP)/ Bio Technology Park (BTP).

17) **Exclusive Economic Zone:** Exclusive Economic Zone extends to 200 nautical miles from the base line. In this zone, the coastal State has exclusive rights to exploit it for economic purpose like constructing artificial islands for oil exploration, power generation and so on.

(Note: one nautical mile = 1.1515 miles or 1.853kms.)

18) **Examination [Section 2(17)]:** "Examination" in relation to any goods, includes measurement and weighment thereof.

19) **Exporter [Section 2(20)]:** Exporter in relation to any goods at any time between their entry for export and the time when they are exported, includes any owner or any person holding himself out to be the exporter.

20) **Entry As per section 2(16)]:** Entry in relation to goods means an entry made in bill of entry, shipping bill or bill of export and includes in the case of goods imported or to be exported by post, the entry referred to in section 82 or the entry made under the regulations made under section 84 of the Customs Act.

21) **Export [Section 2(18)]:** The term export means taking out of India to a place outside India.

22) **Exported Goods [Section 2(19)]:** The term exported goods means any goods, which are to be taken out of India to a place outside India.

Example: The vessel sunk within territorial waters of India and therefore there is no export. Accordingly, no duty drawback shall be available in this case. *[Union of India v Rajindra Dyeing & Printing Mills Ltd. 2005 (180) ELT 433 (SC)]*. The territorial waters extend to 12 nautical miles into the sea from the base line.

23) **Fund [Section 2(21A)]:** Fund means the Consumer Welfare Fund established under section 12C of the Central Excise Act, 1944.

24) **Foreign going Vessel or Aircraft [Section 2(21)]:** The foreign going vessel or aircraft means any vessel or aircraft for the time being in the carriage of goods or passengers between any port or airport in India and any port or airport outside India, whether touching any intermediate port or airport in India or not. The following are also included in the definition:

- A foreign naval vessel doing naval exercises in Indian waters
- A vessel engaged in fishing or any other operation (like oil drilling by domestic vessel or foreign vessel) outside territorial waters
- A vessel going to a place outside India for any purpose whatsoever.

Example 1: A ONGC vessel and a vessel owned by A Ltd. of USA are drilling oil beyond 12 nautical miles in the sea. Hence, both the vessels are called as foreign going vessels.

25) **Goods [Section 2(22)]:** The term goods includes–

(a) Vessels, aircrafts and vehicles

(b) stores

(c) baggage

(d) currency and negotiable instruments and

(e) any other kind of movable property.

26) **High Seas:** An area beyond 200 nautical miles from the base line is called High Seas. All countries have equal rights in this area.

27) **Import [Section 2(23)]:** The term import means bringing into India from a place outside India.

28) **Imported Goods [Section 2(25)]:** The term imported goods means any goods brought into India from a place outside India but does not include goods which have been cleared for home consumption.

29) **Importer [Section 2(26)]:** The term importer means in relation to any goods at any time between their importation and the time when they are cleared for home consumption, includes any owner or any person holding himself out to be the importer.

30) **India (i.e. Territorial Waters) [Section 2(27)]:** The term India is an inclusive definition and includes not only the land mass of India but also Territorial Waters of India. The territorial waters extend to 12 nautical miles into the sea from the base line. Therefore, a vessel not intended to deliver goods should not enter these waters.

31) **Indian Customs Waters [Section 2(28)]:** The term Indian Customs Waters means the waters extending into the sea up to the limit of contiguous zone of India under section 5 of the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zone Act, 1976 and includes any bay, gulf, harbour, creek or tidal river.

    Continental Shelf means the area of relatively shallow seabed between the shore of a continent and deeper ocean

    Indian Customs Waters extend up to 24 nautical miles from the base line. Thereby, Indian Customs Waters cover both the Indian Territorial Waters and Contiguous Zone as well. Indian Territorial Waters extend up to 12 nautical miles from the base line whereas Contiguous Zone extended to a further 12 nautical miles from the outer limit of territorial waters.

    Example 2: The proper officer of customs has reason to believe that any vessel in Indian Customs waters is being used in the smuggling of any goods, he may at any time stop any such vessel and examine and search any goods in the vessel (Section 106(1)(b) of the Customs Act, 1962).

32) **Import Report [Section 2(24)]:** The person-in-charge of a vehicle carrying imported goods or any other person as may be notified by the Central Government shall, in the case of a vehicle, deliver to the proper officer an import report within twelve hours after its arrival in the customs station, in the prescribed form.

33) **Import General Manifest (IGM) [Section 2(24)]:** IGM is a document to be filed in prescribed form with the customs by the carriers of the goods i.e. the steamer Agent or airlines in terms of Sec 30 of Customs Act, 1962. This document indicates the details of all the goods to be transshipped, private property of the crew and arms and ammunitions, gold and silver should also be cleared separately irrespective of whether for landing, for transshipment or for being carried as same bottom cargo. The IGM has to be filed within 24 hours after arrival of the ship/ aircraft. However, in the case of vessel (ship) the manifest maybe delivered even before the arrival of the vessel. This is known as 'prior entry import general manifest'. This system enables the importer to file Bills of Entry and get them assessed and pay duty so that the goods can be taken delivery soon after the unloading.

    Section 30 in being provide for electronic filing of import manifest and also provide that the commission of customs may, in cases where it is not feasible to deliver the import manifest by presenting electronically, all the same to be delivered in any other manner.

34) **Market Price [Section 2(30)]:** Market price in relation to any goods means the wholesale price of the goods in the ordinary course of trade in India.

35) **Person-in-Charge [Section 2(31)]:** means

1)	Vessel	Master
2)	Aircraft	Commander or Pilot in Charge
3)	Train	Conductor or Guard
4)	Vehicle	Driver
5)	Other Conveyance	Person in Charge

36) **Prohibited goods [Section 2(33)]:** Means any goods the import or export of which is subject to any prohibition under this Act or any other law for the time being in force but does not include any such

goods in respect of which the conditions subject to which the goods are permitted to be imported or exported have been complied with.

Say for example, Pornographic and obscene materials, Maps and literature where Indian external boundaries have been shown incorrectly, Narcotic Drugs and Psychotropic Substances, Counterfeit goods and goods violating any of the legally enforceable intellectual property right, Chemicals mentioned in Schedule 1 to the Chemical Weapons Convention of U.N. 1993, Wild life products, Specified Live birds and animals, Wild animals, their parts and products, Exotic birds except a few specified ones, Beef, tallow, fat/oil of animal origin, Specified Sea-shells, Human skeleton.

37) **Shipping Bill [Section 2(39)]:** Shipping bills means a shipping bill referred to in section 50. Shipping bill is the basic document for assessment of export duty. The exporter has to present shipping bill for clearance of export goods through vessel or aircraft.

38) **Smuggling [Section 2(39)]:** "Smuggling", in relation to any goods, means any act or omission which will render such goods liable to confiscation under section 111 (improper importation) or section 113 (improper exportation).

39) **Stores [Section 2(38)]:** Stores means goods for use in a vessel or aircraft and includes fuel and spare parts and other articles of equipment, whether or not for immediate fitting.

40) **Tariff value [Section 2(40)]:** Tariff value in relation to any goods, means the tariff value fixed in respect thereof under section 14(2) of the Act. The CBEC has the power to fix tariff values for any class of imported goods or exported goods. Fixing the tariff value for any class of imported goods or exported goods means the duty shall be chargeable with reference to such tariff value. (For example, please refer the duty based on the % of tariff value under Central Excise).

41) **Value [Section 2(41)]:** "Value" in relation to any goods, means the value thereof determined in accordance with the provisions of Section 14(1)(2) of the Act.

42) **Vehicle [Section 2(42)]:** Vehicle means conveyance of any kind used on land and includes a railway vehicle.

43) **Warehoused [Section 2(43)]:** "Warehouse" means a public warehouse appointed under section 57 or a private warehouse licensed under section 58.

44) **Warehouse Goods [Section 2(44)]:** "Warehouse Goods" means goods deposited in a warehouse.

45) **Warehouse Station [Section 2(45)]:** "Warehouse Station" means a place declared as a warehousing station under section 9.

Significance of Indian Customs Water under Custom Act, 1962

The significance of Indian Customs Waters is as under-

(i) Any person who has landed from/ about to board/ is on board any vessel within Indian Customs water and who has secreted about his person, any goods liable to confiscation or any documents relating thereto may be searched [Section 100];

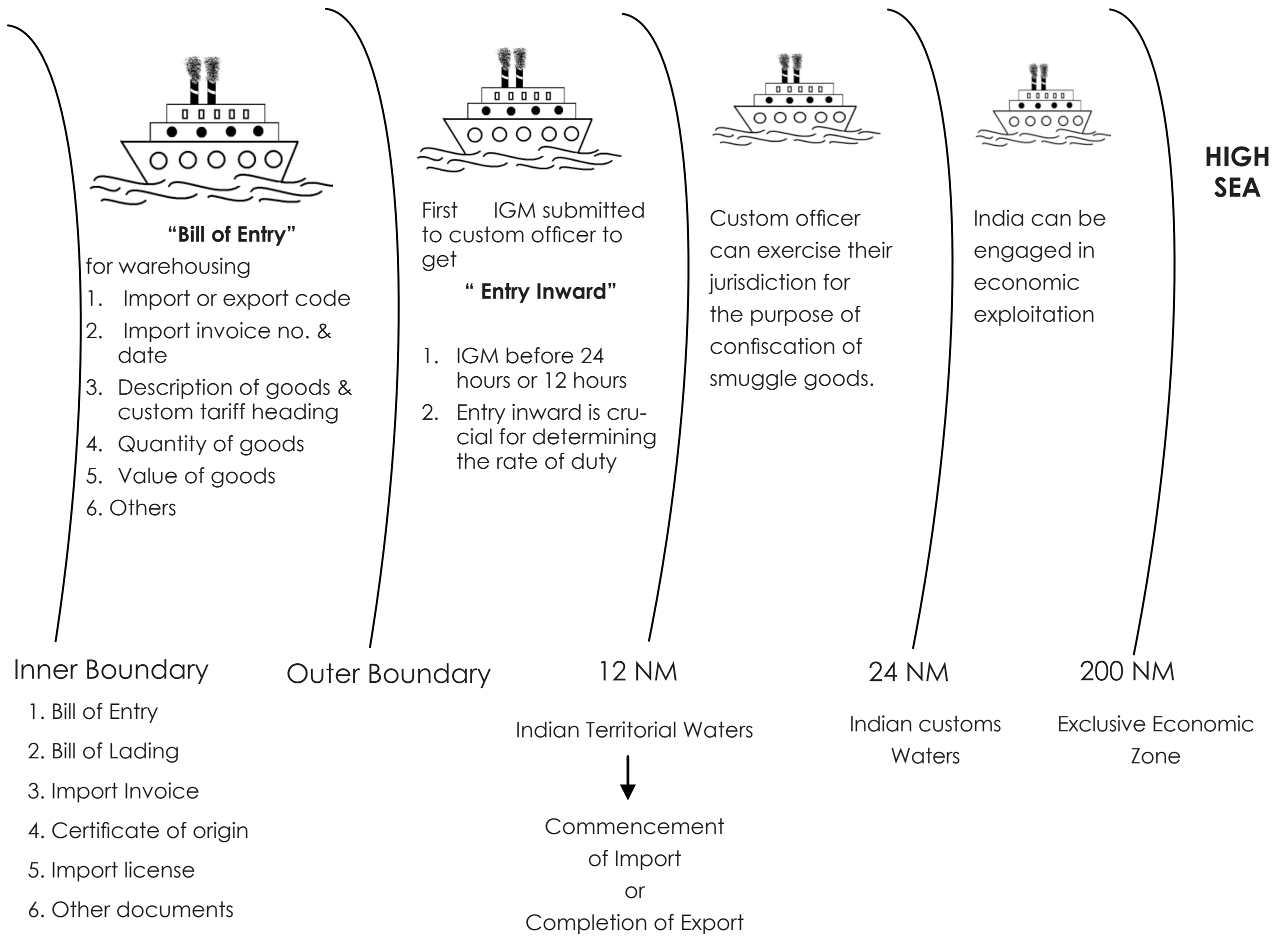
(ii) Any person within Indian Customs waters, who has committed an offence punishable under section 132 or 133 or 135 or 135A or 136, may be arrested [Section 104];

(iii) Any vessel within Indian custom water, which has been, is being, or is about to be, used in the smuggling of any goods or in carriage of any smuggling goods, may be stopped [Section 106];

(iv) Any goods which are brought within the Indian customs waters for the purpose of being imported from a place outside India, contrary to any prohibition imposed by or under this Act or any other law for the time being in force, shall be liable to confiscation [Section 111(d)]; and

(v) Any vessel which is or has been within Indian customs waters is constructed, adapted, altered or fitted in any manner for concealing for concealing goods shall be liable to confiscation [Section 115(1)(a)].

The primary concept has been explained in the following diagram



4.1.4 Circumstances of Levy

Section 12: Imported or Exported goods into or out of India is the taxable event for payment of the duty of customs. Lot of problems was faced in determining the point at which the importation or exportation takes place. The root cause of the problem was the definition of India.

The Supreme Court of India has given the landmark judgments in cases of *Union of India* v *Apar Industries Ltd* (1999) and further in the case of *Garden Silk Mills Ltd* v *Union of India* (1999). The import of goods will commence when they cross the territorial waters but continues and is completed when they become part of the mass of goods within the country, and the taxable event being reached at the time when goods reach the Customs barriers and Bill of Entry for home consumption is filed.

(A) Taxable event for Imported Goods

In the case of Kiran Spinning Mills (1999) the Hon'ble Supreme Court of India held that import is completed only when goods cross the customs barrier. The taxable event is the day of crossing of customs barrier and not on the date when goods landed in India or had entered territorial waters of India. Crossing customs barrier:

when goods are imported into India even after the goods are unloaded from the ship, and even after the goods are assessed to duty subsequent to the filing of a bill of entry, the goods cannot be regarded as having crossed the customs barrier until the duty is paid and the goods are brought out of the limits of the customs station.

Hence, taxable event in case of imported goods can be summed up in the following lines:

The taxable event occur in the course of imports under the customs law with reference to the principles laid down by the Supreme Court in the cases of *Garden Silk Mills Ltd.* **v** *Union of India;* and *Kiran Spinning Mills* v *CC:*

i. Unloading of imported goods at the Customs Port– is not a taxable event
ii. Date of entry into Indian Territorial Waters–is not a taxable event
iii. Date on which the goods cross the customs barrier - is a taxable event
iv. Date of presentation of bill of entry–is not a taxable event

No time limit for submission of bill of entry after the delivery of Import General Manifest (IGM):

As per Section 46(3) of the Customs Act, 1962 a bill of entry may be presented at any time after the delivery of import manifest or import report. Therefore, no time limit has been fixed for submission of bill of entry. Hence, no penalty can be imposed if there is delay in submission of Bill of Entry. However, cargo should be cleared from the wharf within 30 days of unloading.

Note: Bill of Entry can also be filed up to 30 days before the arrival of the goods in India. The classification, valuation and duty can be checked and verified beforehand so that when the consignment arrives it can be cleared immediately.

Provided that a bill of entry may be presented even before the delivery of such manifest or report, if the vessel or the aircraft or vehicle by which the goods have been shipped for importation into India is expected to arrive within thirty days from the date of such presentation. In case the vessel or aircraft or vehicle do not arrive within 30 days of presentation of the bill of entry, the bill of entry so presented shall stand cancelled.

(B) Taxable event for Warehoused Goods

The taxable event in case of warehoused goods is when goods are cleared from customs bonded warehouse, by submitting EX-bond bill of entry. As per Section 1 5(1)(b) of the Customs Act, 1962, when goods have been deposited into a warehouse, and they are removed there from for home consumption, the relevant date for determination of rate of duty is the date of presentation of ex-bond bill of entry (i.e. Sub-bill of Entry) for home consumption.

(C) Taxable event for Exported Goods

As per section 16(1) of the Customs Act, 1962, taxable event arises only when proper officer makes an order permitting clearance (i.e. entry outwards) granted —*Esajee Tayabally Kapasi* (1995)(SC) and loading of the goods for exportation took place under Section 51 of the Customs Act, 1962. In the case of any other goods, on the date of payment of duty.

Therefore, export duty rate prevailing as on the date of entry outwards granted to the vessel by the Customs Officer is relevant.

Example 3: An assessee submitted the shipping bill on 1st January 2016. At that time the export duty was nil (i.e. duty free). Let export order (i.e. entry outwards) was granted on 5th January 2016. However, due to some problems goods could not be loaded into ship. On 25th March 2016, the shipping bills were voluntarily resubmitted by the assessee with the request to permit the shipment by a different vessel. Subsequently, on 27th March 2016, let export order was granted. However, in the mean time the duty at the rate of 10% ad valorem was levied with effect from 1st March 2016. Examine, whether exporter is liable to pay duty?

Answer:

In the given case actual export took place only after revised shipping bill was submitted on 25th March 2016, for which entry outwards granted on 27th March, 2016. Hence, the rate prevalent as on the date of entry outwards granted to the vessel is relevant for determination of rate of duty. Therefore, assessee is liable to pay exportduty @10%.

Note: Export duties do not carry any cess.

(D) Entry inwards to the vessel

The Master of the vessel is not to permit the unloading of any imported goods until an order has been given by the proper officer granting Entry Inwards of such vessel. Normally, Entry Inwards is granted only after the import manifest has been delivered. This entry inward date is crucial for determining the rate of duty, as provided in section 15 of the Customs Act, 1962. Unloading of certain items like accompanied baggage, mail bags, animals, perishables and hazardous goods are exempted from this stipulation.

(E) Entry outwards to the vessel

The vessel should be granted 'Entry Outward' . Loading can start only after entry outward is granted under section 39 of Customs Act, 1962. Steamer Agents can file 'application for entry outwards' 14 days in advance so that intending exporters can start submitting 'Shipping Bills'. This ensures that formalities are completed as quickly as possible and loading in ship starts quickly.

If the shipping bill has been presented before the date of entry outwards of the vessel by which the goods are to be exported, the shipping bill shall be deemed to have been presented on the date of such entry outwards. The provisions of this section shall not apply to baggage and goods exported by post.

(F) Date of determination of Rate of duty and tariff valuation for Imported Goods

Date for determining the rate of duty and tariff valuation of imported goods will depend upon the imported goods entered for home consumption and cleared from warehouse. The determination of appropriate rate of duty and tariff valuation can be explained with the help of the following example:

Imported goods

Clearance for home consumption

Bill of entry is Presented Before the entry Inwards of the vessel Or arrival of aircraft or vehicle

The rate of duty and tariff valuation prevailing on the date of the entry Inwards of the vessel Or the date of arrival of aircraft or vehicle

Bill of entry is presented after the entry inwards of the vessel or aircraft

The rate of duty and tariff valuation prevailing on the date on which the bill of entry in respect such clearance is presented will be applicable.

Clearance from warehousing

The rate of duty and tariff valuation prevailing on the date on which a bill of entry for home consumption is presented will be applicable

Note: The applicable exchange rate is the rate declared by the CBEC on the date of submission of Bill of Entry. If more than one exchange of CEBC is available then consider the exchange rate which was prevailed as on the date of submission of Bill of Entry.

(G) Date of determination of rate of duty and tariff valuation of export goods [Section 16]: According to section 16 of the Customs Act, 1962, the provision relating to date for determination of rate of duty and tariff valuation of export goods are as under –

(a) in the case of goods entered for export under section 50, the date on which the proper officer makes an order permitting clearance and loading of the goods for exportation under section 51.

(b) in the case of any other goods, the date of payment of duty.

The provision of section 16 shall not apply to baggage and goods exported by post.

(H) Clearance of goods from DTA to SEZ

In the case of **Advait steel Rolling Mills Pvt. Ltd. vs. UOI [2012] 286 ELT 535(Mad)**, it is held that the clearance of goods from DTA to Special Economic Zone are not chargeable to export duty either under the SEZ Act, 2005 or under the Customs Act, 1962 on the basis of the following observations –

- The charging section needs to be construed strictly. If a person is not expressly brought within the scope of the charging section, he cannot be taxed at all.
- SEZ Act does not contain any provision for levy and collection of export duty on goods supplied by a DTA unit to a unit in a Special Economic Zone for its authorized operations. Since there is no charging provision in the SEZ Act providing for the levy of customs duty on such goods, export duty cannot be levied on the DTA supplier.
- Reading section 12(1) of the Customs Act, 1962 makes it apparent that Customs duty can be levied only on goods imported into or exported beyond the territorial water of India.

Since both the SEZ unit and the DTA unit are located within the territorial waters of India, supplies from DTA to SEZ would not attract Section 12(1).

(I) Determination of duty where goods consist of articles liable to different rates of duty [Section 19]: Except as otherwise provided in any law for the time being in force, where goods consist of a set of articles, duty shall be calculated as follows,-

(a) articles liable to duty with reference to quantity shall be chargeable as per quantity.

(b) articles liable to duty with reference to value shall be chargeable to duty as under,-

- if such articles are liable with the same rate of duty then duty shall be levied at that rate;
- if the articles in the set are liable to duty at different rates then duty shall be calculated at the highest of those rates.

(c) articles not liable to duty, then they shall also be chargeable to duty at the highest of the rates specified in (b) above.

Duty where evidence of separate value of articles is available : If the importer produces evidence to the satisfaction of the proper officer or the evidence is available regarding the value of any of the articles liable to different rates of duty, such article shall be chargeable to duty separately at the rate applicable to it.

(J) Rate of Duty applicable to accessories, etc. supplied with imported article [Accessories (Condition) Rules, 1963] : Certain accessories are sometimes compulsorily supplied with the main equipment. It may be difficult to value such accessories and to assess them separately or to charge duty on them when no additional consideration is involved in normal course. In such case, if any accessories of, spare parts and maintenance implements for, any article are imported along with that article, then such accessories/spare parts and maintenance implements shall be chargeable at the same rate of duty as that article, if the proper officer is satisfied that in the ordinary course of trade,-

(a) such accessories, parts and implements are compulsorily supplied with that article; and

(b) no separate charge is made for such supply, their price being included in the price of that article.

(K) Circumstance under which no duty will be levied

(i) No duty will be levied on pilfered goods under section 13 of the Customs Act. If any imported goods are pilfered after the unloading thereof and before the proper officer has made an order for clearance for home consumption or deposit in a ware house, then the importer shall not be liable to pay the duty leviable on such goods.

(ii) No duty will be levied when the goods are damaged or deteriorated before or during the course of their unloading, where it is shown to the satisfaction of the Assistant or Deputy Commissioner of Customs (Section 22).

(iii) No duty will be levied in case of warehoused goods, when the goods are damaged before their actual clearance from such warehouse, where it is shown to the satisfaction of the Assistant or Deputy Commissioner of Customs (Section 22).

(iv) No duty will be levied in case of goods lost or destroyed due to natural causes like fire, flood, etc. such loss may take place at any time before the clearance of goods for home consumption. The loss may be at the warehouse (Section 22).

(v) No duty will be levied in case of goods abandoned by importers. Sometimes it may so happen that importer is unwilling or unable to take delivery of the imported goods due to the following reasons:

- the said goods may not be according to the specification,
- the goods may have been damaged during voyage,
- there might have been breach of contract.

In all the above cases the importer has to relinquish his title to the goods unconditionally and abandon them. The relinquishment is done by endorsing the document of title to the goods in favour of the Principal Commissioner or Commissioner of Customs along with invoice.

(vi) No duty will be levied, if the Central Government is satisfied that it is necessary in the public interest not to levy import duty by issuing the notification in the Official Gazette.

(L) Self-assessment of Customs Duty (Section 17 of the Customs Act, 1962, w.e.f. 8-4-2011)

The importer or exporter shall self-assess the duty leviable on imported or exported goods respectively (except where goods are to be cleared as 'stores' for supply to vessels or aircrafts without payment of duty and without assessment under section 85 of Customs Act, 1962) as per section 17(1) of the Customs Act, 1962. The procedure of self assessment is same for imports and exports. Importer importing goods is required to submit Bill of Entry under section 46 of Customs Act, 1962. Exporter is required to submit shipping bill at the time of export under section 50 of Customs Act, 1962. Bill of Entry and Shipping Bill must be submitted electronically, unless manual submission is specifically permitted by Principal Commissioner or Commissioner of Customs.

Verification by proper officer

The self assessment may be verified by 'proper officer' by examining or testing the goods [section 17(2) of Customs Act 1962, w.e.f. 8-4-2011]. For verification of self assessment, 'Proper Officer' may ask importer, exporter or any other person (i.e. Customs House Agent or person who has purchased goods on high seas sale basis) to produce any contract, broker's note, insurance policy, catalogue or other documents whereby duty payable can be ascertained and to furnish further information for ascertainment.

Re-assessment

The proper officer can ask for only those documents which are within the powers of importer or exporter or other person to furnish [section 17(3) of Customs Act 1962, w.e.f. 8-4-2011]. On Such verification, 'proper officer' may re-assess the Bill of entry. Such re-assessment would be without prejudice to any other action which may be taken under Customs Act [section 17(4) of Customs Act, 1962, w.e.f. 8-4-

2011]. If the importer or exporter accepts in writing the reassessment made by proper officer about classification or valuation or exemption or concession, then no question of issuing any formal order arises.

Speaking order

Where the importer or exporter does not accept the re-assessment in writing, the proper officer shall pass a speaking order within 15 days from the date of re-assessment of 'Bill of Entry' [section 17(5) of Customs Act, 1962 w.e.f. 8-4-2011].

Audit by proper officer at his office or premises of importer or exporter

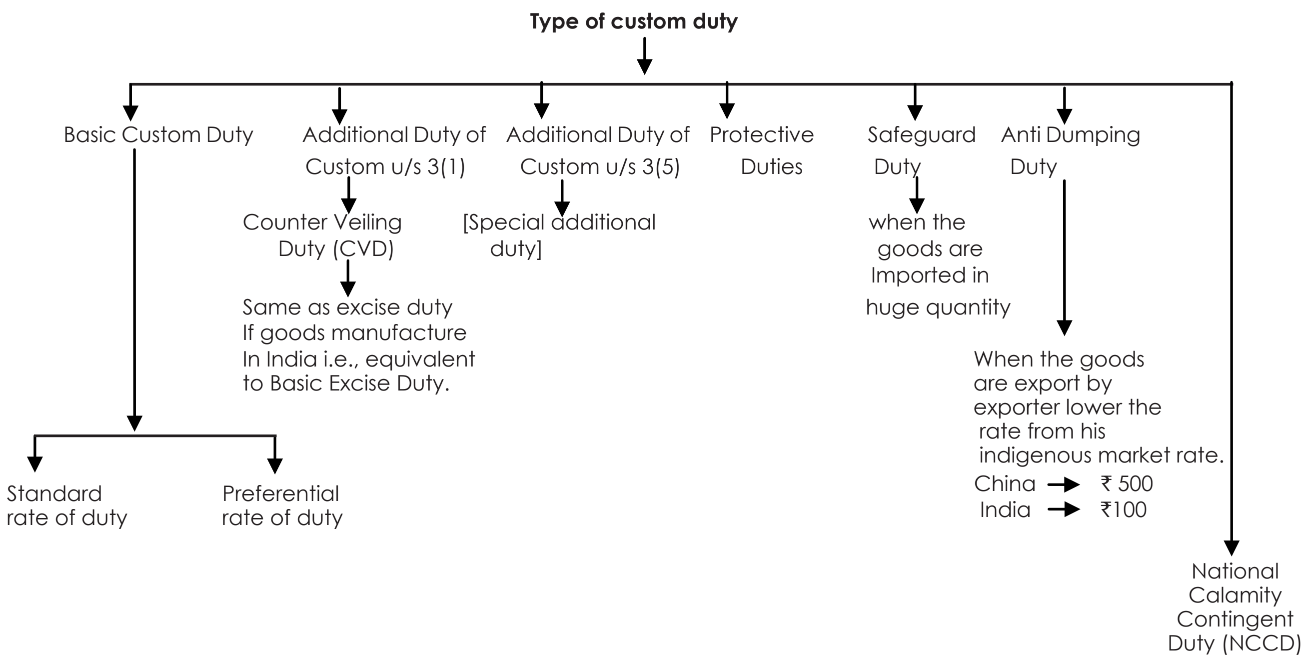
If the goods are not taken for verification of self assessment, the goods will be allowed to be cleared from customs. However, later, proper officer may audit the assessment of duty. Such audit can be done either in the office of proper officer or at the premises of importer, as may be expedient [section 17(6) of Customs Act, 1962 w.e.f. 8-4-2011]. Subsequent to such audit, demand for differential duty and interest can be made under section 28 of Custom Act 1962. This section also makes provisions in respect of penalty for such short payment.

General provisions

Assessment includes provisional assessment, self-assessment, re-assessment and any assessment in which the duty assessed is Nil [section 2(2) of Customs Act, 1962 as substituted w.e.f. 8-4-2011].

As per section 2(34) of Customs Act, 'proper officer' in relation to any function under Customs Act, the officer of customs who is assigned those functions by Board (CBE & C) or Principal Commissioner or Commissioner of Customs.

4.2 TYPES OF CUSTOM DUTY



4.2.1 Basic customs duty is levied under section 12 of Customs Act. Normally, it is levied as a percentage of value as determined under section 14(1). The basic customs duty are 5%, 7.5%, and 10%. Highest rate of basic customs duty is 10% for non-agricultural items, with some exceptions.

Assessable Value = CIF value of imported goods converted into Rupees at exchange rate specified in notification issued by CBE&C plus landing charges 1% (plus some additions often arbitrarily and whimsically made by customs).

Section 2 of the Customs Tariff Act, 1975 provides the rate of duty to be applied on the value of goods. Basically section 2 of the Customs Tariff Act, 1975 provides following:-

- First Schedule - Goods liable for import duty
- Second Schedule - Goods liable for export duty

Basic Customs Duty levied u/s 12 of Customs Act.

(i) The rate of basic customs duty is specified in Customs Tariff Act, read with relevant exemption notification. Generally, Basic Customs Duty is 10% of Non-Agricultural Goods.

(ii) CVD equal to excise duty is payable on imported goods u/s 3(1) of Customs Tariff Act. General excise duty rate is 12.5%. Consider only basic excise duty as CVD. It means CVD is equal to Basic Excise Duty(w.e.f 01-03-2015).

(iii) Special CVD (SAD) is payable @4% on imported goods u/s 3(5) of Customs Tariff Act. This is in lieu of Vat/Sales tax to provide level playing field to Indian goods.

(iv) Education Cess of customs @ 2% and SAH Education Cess of 1% is payable.

(v) NCCD has been imposed on a few articles. In addition, on certain goods, Anti-Dumping Duty, Safeguard Duty, Potective Duty etc. can be imposed.

Calculated of customs duty payable is as follows, w.e.f. 01.03.2015

Seq.	Duty Description	Duty %	Amount	Total Duty
(A)	Assessment Value ₹		20,000.00	
(B)	Basic Customs Duty	10	2,000.00	2,000.00
(C)	Sub-Total for calculating CVD '(A+B)'		22,000.00	
(D)	CVD 'C' x excise duty rate	12.5	2,750.00	2,750.00
(E)	Sub-total for edu cess on customs 'B+D'		4,750.00	
(F)	Edu Cess of Customs – 2% of 'E'	2	95.00	95.00
(G)	SAH Education Cess of Customs – 1% of 'E'	1	47.50	47.50
(H)	Sub-total for Spl CVD 'C+D+F+G'		24,892.50	
(I)	Special CVD u/s 3(5) – 4% of 'H'	4	995.70	995.70
(J)	**Total Duty**			**5,888.20**
(K)	Total duty rounded to	₹		5,888.00

Notes- Buyer, who is manufacturer, is eligible to avail Cenvat Credit of D and I above. A buyer, who is service provider, is eligible to avail Cenvat Credit of D above. A trader who sells imported goods in India after charging Vat/sales tax can get refund of Special CVD of 4% i.e. 'I' above.

4.2.2 Additional Customs Duty U/S 3(1) (CVD)

i. CVD (Countervailing Duty) is payable on imported goods u/s 3(1) of Customs Tariff Act to counter balance impact of excise duty on indigenous manufactures, to ensure level paying field.

ii. CVD is payable equal to Excise Duty payable on like articles if produced in India. It is payable at effective rate of Excise Duty, which is generally 12.5%. It means CVD is equal to Basic Excise Duty (w.e.f 01-03-2015).

iii. CVD is payable on assessable value plus basic customs duty. In case of products covered under MRP provisions, CV duty is payable on MRP basis as per section 4A of Central Excise.

iv. CVD can be levied only if there is 'manufacture'.

v. CVD is neither Excise Duty nor Basic Customs Duty levied under Customs Act. However, all provisions of Customs Act apply to CVD. Calculation of duty payable is as follows -

Example 4: An importer imported some goods for subsequent sale in India at $12,000 on CIF basis. Relevant exchange rate as notified by the Central Government and RBI was ₹ 45 and ₹ 45.50 respectively. The item imported attracts basic duty at 10%. If similar goods were manufactured in India, Excise Duty payable as per Tariff is 14%. Arrive at the Assessable value and the total duty payable thereon.

Answer:

Assessable Value	= ₹ 5,45,400
Add: Basic Customs Duty 10% x 5,45,400	= ₹ 54,540
Balance	= ₹ 5,99,940
Add: CVD 14% on ₹ 5,99,940	= ₹ 83,992
Add: Education Cess 2% on 54,540 + 83,992	= ₹ 2,771
Add: SAH 1% on 54,540 + 83,992	= ₹ 1,385
Total value of imported goods	= ₹ 6,88,088

Working Note:

CIF Value	= 12,000 US$
Total CIF in₹ @ 45.00 per US $	= ₹ 5,40,000
Add: Landing Charges @1% of CIF	= ₹ 5,400
Assessable value	= ₹ 5,45,400

4.2.3 Additional Duty Under Section 3(5) (Special CVD - SAD)

Section 3(5) of Customs Tariff Act empowers Central Government to impose additional duty. This is in addition to Additional Duty leviable u/s 3(1). Provision for this duty has been made w.e.f. 1-3-2005. Purpose of the Additional Duty is to counter balance Sales Tax, VAT, Local Tax or Other charges leviable on articles on its sale, purchase or transaction in India.

The obvious intention is to provide level playing field to manufacturers in India who are manufacturing similar goods. Hence, it is termed as 'Special CVD "or 'SAD'(Special Additional Duty).

Exemption from SAD - Some categories of imports have been exempted from this special CVD (SAD), vide customs notification No. 20/2006-Custom dated 1-3-2006. The main among these are: Articles of jewellery attracts a lower rate of special CVD at 1%.

Departmental clarifications - Department has clarified as follows, vide MF (DR) circular No. 1 8/2006-Cus dated 5-6-2006 –

i. Special CVD of 4% is not leviable in case of imports under advance authorisation, EOU, EPCZ and SEZ schemes

ii. In case of Export Promotion Schemes like DEPB, target plus, service from India, DFCE and Vishesh Krishi and Gram Udyog Yojana, 4% Special CVD is required to be debited to the duty scrip/entitlement certificate.

iii. In case of DFRC scheme, 4% special CVD is payable.

iv. Duty debited through DEPB, DFCE, target plus scheme etc. will be eligible for Cenvat Credit or duty drawback.

4.2.4 Safeguard Duty under the Custom Tariff Act, 1975

In order to ensure that goods imported in increased quantity do not cause or threaten to cause serious injury to domestic industry, there are provisions for levy of safeguard duty on import of such articles into India. It can provide adequate protection to the indigenous industry against competition from the world players. The safeguard duty on imported goods is leviable under Section 8B of the Customs Tariff Act, 1975 read with the Customs Tariff (Identification and Assessment of Safeguard Duty) Rules, 1997.

(i) Imposition: Safeguard Duty can be imposed if the Central Government on enquiry finds that the imports in increased quantity - (a) have caused serious injury to Domestic Industry or, (b) is threatening to cause serious injury to Domestic industry. It can be imposed irrespective of origin of imported goods.

Serious injury means an injury causing significant overall impairment in the position of a domestic industry.

Threat of serious injury means a clear and imminent danger of serious injury.

(ii) No Safeguard Duty on Articles Originating from Developing Countries: In case of articles originating from a Developing Country (i.e. a country notified by the Government of India for purpose of levy of such duty), this duty cannot be imposed under following circumstances -

(a) If the imports of such article from that developing country does not exceed three percent of the total imports of that article into India.

(b) Where the article is originating from more than one developing countries (each with less than three percent import share), then the aggregate of imports from all such countries taken together does not exceed nine percent of the total imports of that article into India.

(iii) Provisional Safeguard Duty Pending Enquiry: Section 8B(2) enables the Central Government to impose a provisional Safeguard Duty in appropriate cases, pending the determination of the issues as to whether the import of the concerned article to India would cause or threaten to cause serious injury to the domestic industry. The duty so collected, shall be refunded if, on a final determination, the Central Government is of the opinion that neither any injury has been caused to the Domestic Industry, nor there is any such threat to cause serious injury.

The Provisional safeguard Duty cannot remain in force for more than *200* days from the date when it was first imposed.

(iv) Duration: The Safeguard Duty shall, unless it is revoked earlier, be in force till the expiry of 4 years from the date of its imposition. However, the Central Government reserves the right for its extension but total period of imposition cannot be beyond 10 years from the date of its imposition.

(v) No Safeguard Duty in certain cases: Unless specifically provided, the safeguard duty shall not be imposed on goods imported by a 100% EOU or unit located in Free Trade Zone/ Special Economic Zone.

(vi) Provision of custom Act, 1962 to apply: The provision of custom Act, 1962 and the rules and regulations made there under, including those relating to the date for determination of rate of duty, assessment, non-levy, short levy, refunds, interest, appeals, offences and penalties shall, as far as may be, apply to the duty chargeable under this section as they apply in relation to duty leviable under that act.

4.2.5 Refund of Special CVD of Customs to Traders

Traders selling imported goods in India after charging sales tax/Vat can claim refund of special CVD of 4% from Customs Department – Notification No. 102/2007-Cus dated 14-9-2007. The dealer (trader) (if he is registered with Central Excise and is issuing Cenvatable Invoice) selling such imported goods must mention in his invoice that the buyer will not be able to avail Cenvat credit of such duty. This is required if he is claiming refund of the special CVD. If he is not claiming refund, obviously, such remark is not required. A manufacturer using these goods in his manufacture can avail Cenvat credit of this duty. Thus, he gets credit through central excise route.

Example 5: An importer imported some goods for subsequent sale in India at $ 20,000 on CIF basis. Relevant exchange rate as notified by the Central Government ₹ 45. The item imported attracts basic duty at 10% and education Cess as applicable. If similar goods were manufactured in India, Excise Duty payable as per Tariff is 12.5%. Special Additional Customs Duty is 4%. Find the total duty payable.

Answer:

		(₹)
CIF value USD 20,000 X 45	=	9,00,000
Add: Loading and unloading @1%	=	9,000
Assessable Value	=	9,09,000
Add: Basic Customs Duty @10% on ₹9,09,000	=	90,900
	=	9,99,900
Add: Additional Customs Duty [@12.5% x ₹9,99,900]	=	1,24,988
		11,24,888
Add: Education Cess 2% on (₹90,900 + ₹1,24,988)	=	4,318
Add: SAH @1% on (₹90,900 + ₹1,24,988)	=	2,159
	=	11,31,365
Add: Special Additional Customs Duty [@4% × ₹11,31,365]	=	45,255
Total value of imported goods	=	11,76,620

Therefore total duty payable is ₹ 2,67,620.

Valid points:

(i) While calculating CVD we should not take into account NCCD of excise.

(ii) CVD can also be imposed even if there is exemption from Basic Customs Duty.

(iii) Imported goods contain more than one classification and the importer is unable to give the breakup of each item with value then the highest rate of duty among them will be considered.

(iv) CVD can be levied only when the importer imported manufactured goods. It means CVD can be levied only if goods are obtained by a process of manufacture *Hyderabad Industries Ltd* v *Union of India* (1995) (SC).

Example 6: Mr. X imported the coal from USA. Exporter in USA exported the coal after washing coal to reduce its ash content. Hence, no CVD on coal, because the imported product was not manufactured and the same imported into India.

(v) If the importer is the manufacturer, he can claim the CENVAT credit of CVD.

(vi) No CVD on Anti Dumping Duty, Safeguard Duty, Protective Duty or Countervailing Duty on Subsidized articles.

If the importer is the manufacturer availing the benefit of SSI Exemption benefit under Notification No.8/2003 under Central Excise. Thereby he is not paying excise duty on his final product manufactured by him in India. Such a manufacturer is not liable to pay CVD (equivalent of Excise Duty) on his imports, even if he is not liable to pay any duty under Central Excise Act, 1944.

4.2.6 Anti-Dumping Duty

i. Anti dumping duty is leviable u/s 9A of Customs Tariff Act when foreign exporter exports his goods at low prices compared to prices normally prevalent in the exporting country.

ii. Dumping is unfair trade practice and the anti-dumping duty is levied to protect Indian manufacturers from unfair competition.

iii. Margin of dumping is the difference between normal value (i.e. his sale price in his country) and export price (price at which he is exporting the goods).

iv. Price of similar products in India is not relevant to determine 'margin of dumping'.

v. 'Injury Margin' means difference between fair selling price of domestic industry and landed cost of imported products. Dumping duty will be lower of dumping margin or injury margin.

vi. Benefits accruing to local industry due to availability of cheap foreign inputs are not considered. This is a drawback.

vii. CVD is not payable on anti-dumping duty. Education Cess and SAH education Cess is not payable on anti-dumping duty · In case of imports from WTO countries, anti-dumping duty can be imposed only if it causes material injury to domestic industry in India.

viii. Dumping duty is decided by Designated Authority after enquiry and imposed by Central Government by notification. Provisional antidumping duty can be imposed.

ix. Appeal against antidumping duty can be made to CESTAT.

Example 7: Mr. X an importer imported certain goods CIF value was US $20,000 and quantity 1,000 Kgs. Exchange rate was 1 US $ = ₹ 50 on date of presentation of Bill of Entry. Customs Duty rates are— (i) Basic Customs Duty 10%, (ii) Education Cess 2%, (iii) SAH Education Cess – 1%. There is no excise duty payable on these goods if manufactured in India. As per Notification issued by the Government of India, anti-dumping duty has been imposed on these goods. The anti-dumping duty will be equal to difference between amount calculated @ US $30 per kg and 'landed value' of goods. Compute Customs Duty liability and anti-dumping liability.

Answer:

Part I	**Amount in ₹**
Total CIF Price US $ 20,000 x ₹ 50	10,00,000
Add: Landing charges @ 1% x ₹10,00,000	10,000
Assessable Value	10,10,000
Basic duty @ 10%	1,01,000
Sub total	11,11,000
Add: Education cess 2% on ₹ 1, 01,000	2,020
Add: Secondary and Higher Education Cess [@1% on ₹ 1,01,000]	1,010

Value of imported goods	11,14,030
Total Customs Duty payable is ₹ 1,04,030.	
Part II	
Rate as per Anti Dumping Notification is ₹ 15,00,000 [US $ 30 per kg x 1,000 Kgs x ₹ 50]	
Part III	
Computation of anti-dumping duty	
Rate as per Anti Dumping Notification	15,00,000
Less: Value of imported goods as computed above	(11,14,030)
Anti Dumping Duty payable	3,85,970

(i) Anti Dumping Duty on Dumped Articles

Often, large manufacturer from abroad may export goods at very low prices compared to prices normally prevalent in export market. Such dumping may be with intention to cripple domestic industry *or* to dispose of their excess stock. This is called 'Dumping' and is an unfair trade practice. In order to avoid such dumping and to protect domestic industry, Central Government can impose, under section 9A of Customs Tariff Act, anti-dumping duty, if the goods are being sold at less than its normal value. Levy of such anti-dumping duty is permissible as per WTO agreement. Anti dumping action can be taken only when there is an Indian industry producing 'like articles'. In *Shenyang Mastusushita* v. *Exide Batteries* 2005 (181) ELT 320 (SC 3 member bench), it was observed, ' Principle behind anti-dumping laws is to protect the domestic industry from being adversely affected by import of goods at export prices which are below the normal value of the goods in the domestic market of the exporter. The duty is calculated on the margin of dumping which is the difference between the export price and the normal value'.

In *SS Enterprise* v. *Designated Authority* AIR 2005 SC 1527 = 181 ELT 375 (SC 3 member bench), it was held that purpose being imposition of anti-dumping duty is to curb unfair trade practices resorted to by exporters of a particular country of flooding the domestic markets at rates which are lower than the rate at which the exporters normally sell the same or like goods in their own countries, so as to cause or be likely to cause injury to the domestic market. The levy of dumping duty is a method recognized by GATT *(should be WTO)* which seeks to remedy the injury and at the same time balances the rights of exporters from other countries to sell their products within the country with the interest of domestic markets. Thus the factors to constitute ' dumping' is (i) an import at prices which are lower than the normal value of goods in exporting country, (ii) the exports must be sufficient to cause injury to domestic industry.

However, negligible quantity of imports would not be sufficient to cause such injury.

Presently, countries like China, Taiwan are said to be involved in dumping. Even Indian steel exporters are facing charges of dumping goods in USA.

(ii) Provisional Anti-Dumping Duty

Pending determination of margin of dumping, duty can be imposed on provisional basis. After dumping duty is finally determined, Central Government can reduce such duty and refund duty extra collected than that finally calculated. Such duty can be imposed upto 90 days prior to date of notification, if there is history of dumping which importer was aware or where serious injury is caused due to dumping.

(iii) No CVD on Anti-Dumping Duty

Anti Dumping Duty and Safeguard Duty is not required to be considered while calculating CVD – view confirmed in *Tonira Pharma* v. *CCE* (2007) 208 ELT 38(CESTAT 2 v. 1 order).

(iv) No Education Cess and SAHE Cess on Anti-Dumping Duty – Education Cess and SAH Education Cess is not payable on anti-dumping duty.

(v) No Anti-Dumping Duty in Case of Imports by EOU and SEZ – Anti-dumping duty is not applicable for imports by EOU or SEZ units, unless it is specifically made applicable in the notification imposing anti-dumping duty. [section 9A(2A) of Customs Tariff Act]

(vi) Margin of Dumping

'Margin of dumping' means the difference between normal value and export price (i.e. the price at which these goods are exported). [Section 9A(1)(a)].

'Normal Value' means comparable price in ordinary course in trade, for like article, when destined for consumption in the exporting country or territory. If such price is not available or not comparable (a) comparable representative price of like article exported from exporting country or territory to appropriate third country or (b) cost of production plus reasonable profit, can be considered [section 9A(1)(c) of Customs Tariff Act]. The 'normal value' is to be determined as per rules.

In *Reliance Industries Ltd. v. Designated Authority* 2006 (202) ELT 23 (SC), it was held that 'normal value' a are not exporter specific but exporting country specific. Once dumping of specific goods from country is established, dumping duty can be imposed on all exports of those goods from that country in India, irrespective of the exporter. Rate of duty may vary from exporter to exporter depending upon the export price.

'Export Price' means the price at which goods are exported. If the export price is unreliable due to association or compensatory arrangement between exporter and importer or a third party, export price can be constructed (revised) on the basis of price at which the imported articles are first sold to independent buyer or according to rules made for determining margin of dumping. [Section 9A(1)(b)].

Margin of dumping is determined on basis of weighted average of 'normal value' and the 'export price' of product under consideration.

(vii) Quantum of Dumping Duty

The anti-dumping duty will be dumping margin or injury margin, *whichever is lower.* 'Injury margin' means difference between fair selling price of domestic industry and landed cost of imported product. The landed cost will include landing charges of 1% and basic customs duty. Thus, only anti-dumping duty enough to remove injury to domestic industry can be levied.

For example, if normal value in exporting country is ₹ 11 and export price is ₹ 8, dumping margin is ₹ 3. If landed cost is ₹ 9 and fair selling price of domestic industry is ₹ 10, then injury margin is ₹ 1. Hence, anti-dumping duty of only Re 1 can be imposed.

In *Reliance Industries Ltd. v. Designated Authority* 2006 (202) ELT 23 (SC), it was held that non-injurious price (NIP) has to be calculated for domestic industry as a whole and not in respect of any particular company or enterprise. [Hence, even if product is captively consumed by Indian manufacturer, transfer price (market value) of inputs is to be considered and not actual cost of captive consumption]. It was observed that there has to be a single NIP for a product and not several NIP for the same product. NIP is not exporter specific.

In Alkali Manufacturers Association of India v. Designated Authority 2006 (194) ELT 161 (CESTAT). Designated Authority had calculated domestic price on basis of profit of 22% of investment. It was held that this is reasonable.

(viii) Dumping Duty for WTO Countries

Section 9B of Customs Tariff Act provides restrictions on imposing dumping duties in case of imports from WTO countries or countries given 'Most Favored Nation' by an agreement. Dumping duty can be levied on import from such countries, only if Central Government declares that import of such articles in India causes material injury to industry established in India or materially retards establishment of industry in India.

[WTO agreement permits levy of anti-dumping duty when it causes injury to domestic industry as a result of specific unfair trade practice by foreign producer, by selling below normal value].

'Injury to domestic industry' will be considered on basis of volume effect and price effect on Indian industry. There must be a 'casual link' between material injury being suffered by dumped articles and the dumped imports.

(ix) Rules for Deciding Subsidy or Dumping Margin

Central Government has been empowered to make rules for determining *(a)* subsidy or bounty in case of bounty fed goods *(b)* the normal value and export price to determine margin of dumping in case of dumping. Accordingly, Customs Tariff (Identification, Assessment and Collection of Anti-dumping duty

on Dumped Articles and for determination of Injury) Rules, 1995 *[Customs Notification No. 2/95 (N.T.) dated 1-1-95]* provide detailed procedure for determining the injury in case of dumped articles.

(x) Procedure for Fixing Anti Dumping Duty

After the 'designated authority' is satisfied about *prima facie* case, he will give notice to Governments of exporting countries. Opportunity to inspection of documents and making representations will be given to interested parties who are likely to be affected. Designated Authority will first give preliminary finding and then final finding within one year. Provisional duty can be imposed on basis of preliminary finding which can continue upto 6 months, extendable to 9 months. Additional duty may be imposed on basis of the final finding.

As per rule 18 of Anti-Dumping Duty Rules, Central Government has to issue a notification fixing anti-dumping duty within three months from date of notification issued by designated authority.

(xi) Appeal Against Order Determining Dumping Duty

Appeal against the order determining the duty can be made to CESTAT. The appeal will be heard by at least three members bench consisting of President, one judicial member and one technical member [section 9C of Customs Tariff Act].

(xii) No Appeal against Order of Tribunal

Section 9C does not provide for statutory appeal against order of Tribunal. Hence, only remedy is either writ in High Court or SLP in Supreme Court.

(xiii) High Court should not Exercise Writ Jurisdiction

In view of appeal provisions, High Court should not entertain writ petitions and grant interim relief. Otherwise, the provisions of appeal would be rendered otiose –*Association of Synthetic Fibre Industry* v. *J K Industries 2006* (199) ELT 196 (SC) * Nitco Tiles v. Gujarat Ceramic Floor Tiles Mfg Association 2006 (199) ELT 198 (SC).

(xiv) Mid-Term Review

Mid-term review of Anti-Dumping Duty is permissible under rule 23 of Anti-Dumping Duty Rules. In *Rishiroop Polymers* v. *Designated Authority 2006* (196) ELT 385 (SC), it was held that scope of review enquiry by Designated Authority is limited to the satisfaction as to whether there is justification for continuing imposition of Anti-Dumping Duty. The inquiry is limited to change in various parameters like normal value, export value, dumping margin, fixation of non-injury price and injury to domestic industry. Only changed parameters should be considered.

(xv) New Shipper Review

After imposing of Anti-Dumping Duty, a new exporter may want to export same goods to India. As per rule 22, if he had not exported earlier, he can ask for review of Anti-Dumping Duty. During the period of review, Government may resort to provisional assessment and may allow imports on submission of guarantee, pending review. If anti-dumping duty is determined, it will be payable retrospectively from date of initiation of review. Such review is termed as 'new Shipper Review'.

(xvi) Discontinuation of Anti-Dumping Duty i.e. Sunset Review

Anti dumping duty ceases on the expiry of five years from date of imposition. However, Central Government can extend the anti-dumping duty, if it is of the opinion that cessation is likely to lead to continuation or recurrence of dumping and injury.

Example 8: An importer imported some goods. Description of goods: Mulberry Raw Silk (not thrown) (HS Code 5002 00) from People's Republic of China. CIF value was US $ 20,000 and quantity 1,000 Kgs. Exchange rate was US $ =₹ 44 on date of presentation of Bill of Entry. Customs Duty rates are – (i) Basic Customs Duty 10%, (ii) Education Cess 2%, (iii) SAH Education Cess - 1%. There is no excise duty payable on these goods if manufactured in India. As per Notification No. 106/2003-Cus dated 10-7-2003, anti-dumping duty has been imposed on these goods imported from China, manufactured by any producer in People' s Republic of China. The anti-dumping duty will be equal to difference between amount calculated @ US $31.69 per Kg and 'Landed value' of goods. Compute Customs Duty liability & anti-dumping liability.

Answer:

(a)	Computation of Customs Duty :	
	Total CIF Price	US $ 20,000
	CIF @ ₹ 44 per 1 US $	₹ 8,80,000.00
	Add – Landing charges @ 1%	₹ 8,800.00
	Assessable Value	₹ 8,88,800.00
	Basic duty @ 10%	₹ 88,880.00
	Education Cess @ 2% on 88,880.00	₹ 1,777.60
	SAH education Cess 1%	₹ 888.80
	Total Customs Duty payable (Basic + Education Cess)	₹ 91,546.40
	Rounded off	₹ 91,546.00
(b)	Computation of landed value	
	Assessable Value Under Customs Act	₹ 8,88,800.00
	Add: All Duties of Customs	₹ 91,546.40
	Landed Value as per Anti-Dumping Notification	₹ 9,80,346.40
(c)	Computation of anti-dumping duty	
	Rate of Silk Yarn as per Anti-Dumping Notification	
	(US $ 31.69 per kg) × 1000 kgs =	US $ 31,690
	Value @ ₹ 44 per US $ = (31,690$ x ₹ 44)	₹ 13,94,360
	Less : Landed value as per Anti-Dumping =	₹ 9,80,346
	Anti-Dumping Duty Payable	₹ 4,14,014

4.3 VALUATION IN CUSTOMS

4.3.1 Customs duty is payable as a percentage of 'Value' often called '*Assessable Value*' or '*Customs Value*'. The Value may be either *(a)* 'Value' as defined in section 14(1) of Customs Act or *(b)* Tariff value prescribed under section 14(2) of Customs Act. The provisions relating to customs valuation have been completely revamped by introducing new section 14 w.e.f. 10-10-2007.

4.3.2 Tariff Value -

i. Tariff Value can be fixed by CBE&C (Board) for any class of imported goods or export goods. CBE&C should consider trend of value of such or like goods while fixing tariff value. Once so fixed, duty is payable as percentage of this value. (The percentage applicable is as prescribed in Customs Tariff Act). Fixing tariff value is not permitted under GATT convention. However, the provision of fixing tariff values has been retained.
ii. Tariff value for crude palm oil, RBD Palmolein, palm oil, crude soya-bean oil and brass scrap has been fixed by notification No. 36/200 1 -Cus (NT) dated 3-8-2001.
iii. Transaction value at the time and place of importation or exportation, when price is sole consideration and buyer and sellers are unrelated is the basic criteria for 'value' u/s 14(1) of Customs Act. Thus, CIF value in case of imports and FOB value in case of exports is relevant.
iv. In case of high sea sale, price charged by importer to assessee would form the assessable value and not the invoice issued to the importer by foreign supplier. –*National Wire* v. *CC* 2000(122) ELT 810 (CEGAT) * *Godavari Fertilizers* v. *CC* (1996) 81 ELT 535 (CEGAT).
v. Rate of exchange will be as determined by CBE&C or ascertained in manner determined by CBE&C.
vi. Valuation for customs is required to be done as per provisions of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007
vii. CIF value of goods plus 1% landing charges is the basis for deciding 'Assessable Value'.
viii. Commission to local agents, packing cost, value of goods and tooling supplied by buyer, royalty relating to imported goods are addible.
ix. Interest on deferred payment, demurrage and value of computer software loaded is not to be added.
x. Old machinery and old cars are often valued on basis of depreciated value, though such method has no sanction of law.

4.3.3 Additions To 'Customs Value'

Rule 10 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 [Rule 9 upto 10-10-2007] provide that following cost and services are to be added, *if these are not already included in the invoice price. –*

i. Commission and brokerage, except buying Commission, if not already included in the invoice price [rule 10(1)(a)(i)].
ii. Cost of container which are treated as being one with the goods for customs purposes, if not already included in the invoice price [rule 10(1)(a)(ii)]. Cost of packing whether labour or materials, if not already included in the invoice price [rule 10(1)(a)(iii)].
iii. Materials, components, tools, dies, moulds, and consumables used in production of imported goods, supplied by buyer directly or indirectly, free of charge or at reduced cost, to the extent not already included in price [rule 10(1)(b)(i), (ii) and (iii)]
iv. Engineering, development, art work, design work, plans and sketches undertaken elsewhere than in India and necessary for production of imported goods, to the extent not already included in price [rule 10(1)(b)(iv)].
v. Royalties and license fees relating to imported goods that buyer is required to pay, directly or indirectly, as a condition of sale of goods being valued [rule 10(1)(c)]
vi. Value of proceeds of subsequent resale, disposal or use of goods that accrues directly or indirectly to seller (i.e. to foreign exporter) [rule 10(1)(d)]
vii. All other payments made as condition of sale of goods being valued made directly or to third party to satisfy obligation of seller, to the extent not included in the price [rule 10(1)(e)]
viii. Cost of transport upto place of importation [rule 10(2)(a)]

ix. Loading, unloading and handling charges associated with delivery of imported goods at place of importation [These are termed as landing charges and are to be taken as 1%] [ru le 10(2)(b)]

x. Cost of insurance [rule 10(2) (c)]

The additions should be on the basis of objective and quantifiable data [rule 10(3) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 (earlier rule 9(3)].

4.3.4 Services / Documents / Technical Know-How Supplied by Buyer

Cost of engineering, development, art work, design work and plans and sketches undertaken by buyer which is necessary for production of imported goods is includible, only if such work is undertaken *outside India.* [Rule 10(1)(b)(iv) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 (earlier rule 9)] The addition should be done on objective and quantifiable data. Data available with importer should be used as far as possible. If the services are purchased or leased by importer, such purchase/lease cost should be added. If the importer has himself done the work abroad, its cost should be added on basis of structure and management practices of importer and his accounting methods (in other words, if development work, plans, sketches etc. is done by importer himself *outside India,* its cost should be calculated based on normal accounting practices - like apportionment of overheads, apportionment over various jobs if the same development work, design work etc. is used for more than one jobs etc.) [Interpretative Note to rule 10(1)(b)(iv) of Customs Valuation Rules].

4.3.5 Technical Know How Related to Imported Machinery

In *CC* v. *Essar Gujarat Ltd.* (1997) 9 SCC 738 = 88 ELT 609 = 17 RLT 588 (SC 3 member bench), it was held that payment of license fee and transfer of technology, without which the imported plant could not function, will have to be added to the value of imported plant. However, training charges cannot be included. —wrongly followed in *CC* v. *Himson Textile Engg. Ltd.* 1997(93) ELT 301 (CEGAT).

4.3.6 Royalties and License Fee

Royalties and license fees related to imported goods that the buyer is required to pay, directly or indirectly, as a condition of sale of the goods being valued, to the extent that such royalties and fees are not included in the price actually paid or payable, are required to be added in assessable value. [Rule 10(1)(c) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 (earlier rule 9)].

4.3.7 Royalty Payment Un-connected with Imported Goods not to be Added

Often, a lump-sum payment of royalty is made to foreign collaborators for technical know-how. In addition, components / parts/ CKD packs are procured from foreign collaborators. Customs department normally holds that the price of parts/CKD packs should be loaded, on assumption that the part of price of component parts/CKD packs has been paid as 'royalty payment'.

4.3.8 Charges for Reproduction of Goods in India not to be Added

Interpretative Note to rule 10(1)(c) of Customs Valuation Rules makes it clear that charges for right to reproduce the imported goods in India shall not be added.

4.3.9 Barge/ Lighterage Charges includible

In some cases, the ship is not brought upto jetty. Goods are discharged at outer anchorage. This may be for various reasons, e.g. (a) deep draught at port, (b) Ports are busy, (c) Odd dimensional or heavy lifts or hazardous cargo discharged at anchorage. Charges for brining the goods from outer anchorage are known as 'barging/ lighterage charges'.

As per *explanation* to rule 10(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 [inserted w.e.f. 10-10-2007], ship demurrage charges on chartered vessels, lighterage or barge charges are includible. Mode of computation of freight of time chartered/daughter vessel has been specified in MF(DR) circular No. 4/2006-Cus dated 12-1-2006.

4.3.10 Landing Charges to be added

Cost of unloading and handling associated with delivery of imported goods in port(*called landing charges)* shall be added. These will be calculated @ 1% of CIF value, i.e. FOB price plus freight plus insurance. [Rule 10(2)(b) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 –earlier rule 9].

4.3.11 Cost of Transport upto Port should be added

Cost of transport from exporting country to India is to be added in 'Assessable Value'. [Rule 10(2)(a) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 (earlier rule 9).] In other words, CIF value is the basis for valuation. If the goods are imported by air, the air freight will be very high. Hence, in case air freight is higher than 20% of FOB price of goods, only 20% of FOB price will be added for Customs Valuation purposes.

If cost of transport is not ascertainable, it will be taken as 20% of FOB value of goods. However, cost of transport within India is not to be considered.

Freight

Air

Freight can't exceed 20% of FOB value

[if actual is less than 20% of FOB value,

then take actual freight]

Other than air

Actual freight

If actual freight is unknown

∴ Freight=20% of FOB value.

4.3.12 Insurance Cost should be added

Insurance charges on goods are to be added. [Rule 10(2)(c) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007]. If these are not ascertainable, these will be calculated @ 1.125% of FOB Value of goods.

Insurance

Actual Amount

If actual is unknown

Insurance → 1.125% of FOB value.

4.3.13 Exclusions from Assessable Value

Interpretative Note to rule 3 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007provide that following charges shall be excluded:

(a) Charges for construction, erection, assembly, maintenance or technical assistance undertaken *after* importation of plant, machinery or equipment

(b) Cost of transport *after* importation

(c) Duties and taxes in India

Other payments from buyer to seller *that do not relate* to imported goods are not part of the customs value. Demurrage charges payable to port trust authorities for delay in clearing goods are not to be added. - *Dee pak Fertilisers* v. *CC* 1989(41) ELT 550 (CEGAT) * *Hindustan Lever* v. *UOI* 2002(142) ELT 33 (Cal HC). [However, ship demurrage is includible w.e.f. 10-10-2007].

Ship demurrage includible w.e.f. 10-10-2007 - explanation to rule 10(2)

4.3.14 Essential Ingredients of Valuation (section 14)

The essential ingredients of section 14 may be analyzed as under:

a) Section 14 would be applicable only when customs duty is chargeable on goods based on their value either under the Customs Tariff Act, 1975 or under any other law for the time being in force.

b) The value of goods under section 14(1) is deemed value.

c) The assessable value will be price at which like goods are ordinarily sold.

d) Where there is no sale price, the value shall be the price at which such or like goods are ordinarily offered for sale.

e) The terms of the price should be for delivery at the time and place of importation or exportation, as the case may be.

f) The sale or offer for sale should be in the course of international trade.

g) There should be no mutuality of interest between the seller and the buyer.

h) Price should be the sole consideration for sale or offer for sale.

Analysis in the Light of Judicial Decisions

The above ingredients may be further explained with the help of judicial rulings as under:

(a) Assessable Value is Deemed Value

Section 14(1)(a) brings about the concept of deemed value, which is a fictional value that relates to the concept of intrinsic value of goods, which it may fetch in the international market.

In the case of *Union of India v Glaxo Laboratories Ltd.,* the Court observed that the assessable value as per section 14(1), need not as a matter of fact, be the invoice price or the price that is agreed between the parties. It may be deemed value.

(b) Price

In N *Gulabair D Parekh v Union of India,* it was observed that the invoice price based on the prevailing price list, should be accepted in terms of section 14(1) (a) of the Customs Act.

A declared price list can be used for the purpose or arriving at the value but there is no hard and fast rule and the invoice may supersede the price list as held by the Supreme Courtin *Mirah Exprots Pvt. Ltd. v CC.*

In *Rajkumar Knitting Mills P Ltd. v CC,* a three member bench of Supreme Court held that for valuation purposes, ' ordinary' price at the time of importation is relevant and *not* the price prevalent on the date of contract.

(c) At which such or like goods Are Ordinarily Sold

In *Chander Prakash & Co v Collector of Customs,* it was held that when the invoice price was very low and when the prices of comparable goods were available, it would not be appropriate to adopt the invoice price.

(d) Where there is no sale price, the 'Offer for Sale' price will be applicable

In case a sale price is not available, the offer for sale price may be construed as the basis determining the assessable value. For example, in case a price list is available, such price list is the quotation as well.

(e) Ordinarily Sold

In *Collector of Customs, Bombay v Maruti Udyog Limited* (1987), Maruti Udyog Limited, which had collaboration with Suzuke Motor Co. Limited, was the only buyer of Suzuki SKD/CKD packs and complete vehicles. A controversy arose so to whether the price charges by Suzuki could be considered as one at which goods were ordinarily sold or offered for sale. In this case, the court held that the price charged by the Suzuki was a commercial price. Also, it was held that there was nothing to prove that the transaction between the two companies were not at arm's length.

(f) In the course of International Trade

In *Satellite Engineering Limited v Union of India* (1983), the assessee, who was manufacturers of fluorescent starter switches imported lead glass tubing at rate of 0.15 pounds per kg. However, the customs department which was of the opinion that the value was low obtained two more quotations which were 0.430 pounds per kg. And 0.429 pounds per kg. respectively. It was held that the prices indicated in the two quotations were in the course of international trade and hence that rate will form the basis for determining the assessable value.

(g) Price being the Sole Consideration

In *Sanjay Chandiram v Collector of Customs,* the court held that as there is no proof of comparable goods being imported at a higher rate and as it cannot be shown that the importer had paid to the supplier, an amount more than that required to be paid, there is no ground for rejection of the transaction value.

4.3.15 Relevant Date for Rate and Valuation of Import Duty

Section 15 of Customs Act prescribes that rate of duty and tariff valuation applicable to imported goods shall be the rate and valuation in force at one of the following dates *(a)* if the goods are entered for home consumption, the date on which bill of entry is presented *(b)* in case of warehoused goods, when Bill of Entry for home consumption is presented u/s 68 for clearance from warehouse and *(c)* in other cases, date of payment of duty.

4.4 METHODS OF VALUATION

The Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, based on WTO Valuation Agreement (earlier GATT Valuation Code), consist of rules providing six methods of valuation.

i. The methods of valuation for customs methods are as follows —

ii. Transaction Value of Imported goods [Section 14(1) and Rule 3(1)]

iii. Transaction Value of Identical Goods [Rule 4]

iv. Transaction Value of Similar Goods [Rule 5]

v. Deductive Value which is based on identical or similar imported goods sold in India [Rule 7]

vi. Computed value which is based on cost of manufacture of goods plus profits [Rule 8]

vii. Residual method based on reasonable means and data available [Rule 9]

4.4.1 Methods to be applied Sequentially

These methods are to be applied in sequential order, i.e. if method one cannot be applied, then method two comes into force and when method two also cannot be applied, method three should be used and so on. The only exception is that the 'Computed value' method may be used before 'deductive value 'method, if the importer requests and Assessing Officer permits.

4.4.2 Rejection of 'Value'

Importer has to declare 'value' of goods. If the assessing officer has reason to doubt about truth or accuracy of the value declared by the importer, he can ask the importer to submit further information and evidence. If the customs officer still has *reasonable doubt,* he can reject the 'value' as declared by the importer. [Rule 12(1) w.e.f. 10-10-2007 – earlier rule 10A(1) of Customs Valuation Rules added w.e.f. 19-2-1 998]. If the importer requests, the assessing officer has to give reasons for doubting the truth or accuracy of value declared by importer [Rule 12(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 –earlier rule 10A(2) of Customs Valuation Rules upto 10-10-2007].

4.4.3 Rule 12 is only Mechanism to Reject the Declared Value

As per *explanation (1)(i)* to Rule 12, the Rule 12 does not provide any method for determination of value. It only provides mechanism to reject declared value, where there is reasonable doubt. If transaction value is rejected, valuation has to be done as per Rule 4 to 9 *[Explanation* (1)(i) to Rule 12 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007].

4.4.4 Transaction Value of Imported Goods [Section 14(1) and Rule 3(1)]

As per rule 3(1), value of imported goods shall be transaction value adjusted in accordance with provisions of rule 10 [Rules effective from 10.10.2007].

As per rule 10 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, various additions like sales commission, cost of containers, cost of packing; cost of materials, components etc. or services supplied by buyer; royalties payable, transport charges, insurance etc. are includible, *if these do not already form part of transaction value (as mentioned above).*

Rule 3(1) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 is subject to rule 12, which means that provisions of rule 12 overrides provisions of rule 3. As per rule 12 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, the value as declared by importer can be rejected by Assessing Officer, if he has doubts about truth or accuracy of the value as declared. However, the Assessing Officer has to give reasons for his doubts in writing and provide opportunity of personal hearing. Thus, it is not obligatory on customs officer to accept the transaction value if he has reasons to doubt the truth or accuracy of the same.

Transaction value can be rejected either for special circumstances as per section 14(1) or conditions as specified in rule 3(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007.

(A) Special circumstances as per Section 14(1) - *The 'special circumstances' in section 14(1) are (a) Buyer and seller should not be related and (b) Price should be the sole consideration for the sale. If these 'special circumstances' are not satisfied, transaction value can be rejected. Any other 'special circumstances' cannot be considered.*

(B) Conditions as per Rule 3(2) - *As per rule 3(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 [Earlier rule 4(2) of Customs Valuation Rules], transaction value can be accepted only if following requirements are satisfied –*

(C) No restriction on Buyer for Disposal of Goods - There are no restriction on buyer on disposition or use of goods *except* the following: *(a)* restrictions prescribed by public authorities in India *(b)* restriction on geographical area within which goods may be resold e.g. goods should not be sold outside particular State or outside India *or (c)* restriction that does not materially affect value of goods - e.g. exporter puts a condition to importer of automobile that car should not be exhibited before a particular date – illustration given in Interpretative Note to rule 3(2) (a) (iii). [rule 3(2) (a)].

(D) Sale not subject to conditions of which value cannot be determined - *The sale or price should not* be subject to a condition or consideration for which value cannot be determined. Examples given in interpretative note to rule 3(2) (b) are – (a) Price is subject to condition that buyer buys some other goods in specified quantities from seller (b) price is dependent on price at which buyer of imported goods sells other goods to seller (c) Price is based on form of payment extraneous the imported goods. However, (i) buyer furnishing engineering and plans undertaken in India to seller (ii) Buyer undertaking activities of marketing of imported goods in India will not form part of value of imported goods [rule 3(2) (b)].

(E) No further consideration to Seller of which adjustment cannot be made - *Seller should not be entitled* to further consideration like part of subsequent resale, disposal or use of goods by the buyer will accrue directly or indirectly to seller, unless proper adjustment in value terms can be made as per rule 10 e.g. if the importer is a trader and the condition is that after he sells the goods in India, the foreign exporter will get a fixed amount after the sale, that extra amount can be added for Customs Valuation [rule 3(2) (c)].

(F) Unrelated Buyer and Seller, Except when price acceptable under Rule 3(3) - *Buyer and seller are not* be related, unless the transaction value is acceptable under rule 3(3) [rule 3(2)(d)] [earlier ru le 4(2)(h) upto 10-10-2007]. *If any of the aforesaid requirements is not satisfied, 'transaction value' cannot be accepted for valuation purposes.*

Related person under Customs Valuations Provisions

Rule 2(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 and Rule 2(2) of Customs Valuation (Determination of Value of Export Goods) Rules, 2007 define that persons shall be deemed to be 'related' only if one of the conditions is satisfied:

- they are officers or directors of one other's businesses [Rule 2(2)(i)]
- they are legally recognised partners in business [Rule 2(2)(ii)]
- they are employer and employee [Rule 2(2)(iii)]
- any person directly or indirectly owns, controls or holds 5% or more of shares of both of them [Rule 2(2)(iv)]
- one of them controls other directly or indirectly [Rule 2(2)(v)]
- both of them are controlled - directly or indirectly - by third person [Rule 2(2)(vi)]
- together they control a third person - directly or indirectly [Rule 2(2)(vii)]
- they are members of same family [Rule 2(2)(viii)]. (what is **"family"** is not defined).

Person includes legal person i.e. Company, partnership firm, trust etc. [Explanation I to Rule 2(2)].

If a person is sold agent or sole distributor or sole concessionaire of other, he will be deemed to be 'related', if he falls within the criteria of rule 2(2) [Explanation II to Rule 2(2)]. Thus, sole selling agent or sole distributor or sole concessionaire will be 'related person' only if he falls within the criteria as specified in rule 2(2). A sole selling agent or sole distributor or sole concessionaire is not automatically deemed as 'related person' in all the cases.

Interpretative Note to rule 2 clarify that for purpose of rule 2(2)(v), one person is deemed to control other if he is legally or operationally in a position to exercise restraint or direction over the other. Thus, control need not be only legal - even operational control is enough.

In CC v. East African Traders 2000(115) ELT 613 (SC), it was held that authorities can pierce the corporate veil to ascertain whether the buyer and seller are indeed related persons within the meaning of the rule. [Piercing corporate veil means looking behind the facade to see the persons who are in real control]. [The Tribunal had held that even if MD of supplier company is brother of importing firm, supplier and importer cannot be treated as related person. However, Supreme Court has said that they can be treated so by piercing the corporate veil].

However, merely because two parties are related to each other will not amount to under valuation per se. It will depend on facts and circumstances of each individual case - CC v. Variant (India) Ltd. (2007) 210 ELT 481 (SC).

In Siemens Ltd v. CC2000(126) ELT 1134 (CEGAT), it was held that even if buyer is a subsidiary company, invoice price should be accepted if the relationship has not affected the invoice price and price is same as the price sold to other independent buyers.

4.4.5 Transaction Value of Identical Goods

Rule 4(l) (a) of Customs Valuation (Determination of Value of Imported Goods) Rules 2007 of Customs Valuation Rules provide that if valuation on the basis of ' transaction value' is not possible, the 'Assessable value' will be decided on basis of transaction value of identical goods sold for export to India and imported at or about the same time.

Rule 4(1)(b) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 provides that transaction value of identical goods at the same commercial level and in substantially same quantity as the goods being valued shall be used to determine value of imported goods.

If transaction value at different commercial level or in different quantities *or both* is available, suitable adjustments can be made to take into account the difference.

Identical goods' are defined under Rule 2(1)(d) of Custom Valuation (Determination of value of Imported Goods) Rules, 2007 as those goods which fulfill all following conditions i.e. *(i)* the goods should be same in all respects, including physical characteristics, quality and reputation; except for minor differences in appearance that do not affect value of goods, *(ii)* the goods should have been produced in the same country in which the goods being valued were produced, *(iii)* they should be produced by same manufacturer who has manufactured goods under valuation - if price of such goods are *not* available, price of goods produced by another manufacturer in the same country. However, if engineering, development work, art work, design work, plan or sketch undertaken in India were completed by the buyer on these imported goods free of charge or at reduced rate for use in connection with the production and sale for export of these imported goods, these will not be 'identical goods'.

Summary of valuation of 'Identical Goods'

i. Contemporaneous imported goods,

ii. Same in all respect,

iii. Minor difference in appearance like Nokia 6265 (steel gray) & Nokia 6265 (Black colour),

iv. Produced in same country at same commercial level, substantially same quantity – Lowest value to be taken,

v. 1st preference – same manufacturer,

vi. 2nd preference – only if same manufacturer not available them different manufacturer,

Adjustments to be made

Price of identical goods should be compared at same commercial level and in substantially same quantity of goods [rule 4(1)(b) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007] - noted in Elite Packaging Industries v. CC-1992 (60) ELT 311 (SC).

If transaction value at different commercial level or in different quantities or both is available, suitable adjustments can be made to take into account the difference. It should be on demonstrated evidence which clearly establishes reasonableness and accuracy of adjustments [rule 4(1)(c) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007].

As per interpretative note to rule 4 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, if price of identical goods at same commercial level and in substantially the same quantities as the goods being valued is not available, customs officer can use any of the following price of identical goods - (a) sale at same commercial level but in different quantities (b) sale at different commercial levels but in substantially the same quantities or (c) sale at different commercial level and in different quantities. Such price can be only 'transaction value' which has already been accepted under rule 3. After such sale is found, adjustment will be made for (a) quantity factor only (b) commercial level factors only or (c) both commercial level and quantity factors.

Such adjustment can be only on basis of demonstrative evidence e.g. valid price lists containing prices referring to different levels or different quantities. For example, assume that import is for 10 units, while transaction value of identical goods is available for 500 units. If the seller is known to be giving quantity discounts and if seller's price list for 10 units and 500 units is available, adjustment can be made based on seller's price list. In such case, price of identical goods made in 10 units need not be available. Such adjustment can be only on objective measure on bona fide evidence and not arbitrary.

Adjustment for distances and transport costs - If valuation of identical goods was made after adding costs and services as per rule 10 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, differences arising due to differences in distances and means of transport should be considered, while arriving at 'Assessable Value' of goods under valuation. This will be required if value of identical goods manufactured by different manufacturer and/or at different place is being taken as basis for valuation [Rule 4(2).

4.4.6 Transaction Value of Similar Goods

If first method of transaction value of the goods or second method of transaction value of identical goods cannot be used, rule 5 (earlier rule 6) provide for valuation on basis of 'Transaction value of similar goods imported at or about the same time'.

What are Similar goods - Rule 2(1)(f) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 [earlier rule 2(1)(e) upto 10-10-2007] define 'similar goods' as *(a)* alike in all respects, have like characteristics and like components and perform same functions. These should be commercially inter-changeable with goods being valued as regards quality, reputation and trade mark. *(b)* the goods should have been produced in the same country in which the goods being valued were produced. *(c)* they should be produced by same manufacturer who has manufactured goods undervaluation - if price of such goods are not available, price of goods produced by another manufacturer in the same country can be considered. . However, if engineering, development work, art work, design work, plan or sketch undertaken in India were completed by the buyer on these imported goods free of charge or at reduced rate for use in connection with the production and sale for export of these imported goods, these will not be 'similar goods'.

As per rule 5(2) and interpretative note to rule 5 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007, the adjustments that can be made are same as can be done in respect of identical goods under rule 4 i.e. (a) Adjustments for commercial level and/or quantity can be made (b) if valuation of similar goods is made after adding costs and services as per rule 10, differences arising due to differences in distances and means of transport should be considered, (c) if more than one value is available, lowest of such values should be taken.

Distinction between identical goods and similar goods

The major distinction between 'identical goods' and 'similar goods' is that the 'identical goods' should be same in all respects, except for minor differences in appearance, while in case of 'similar goods', it is enough if they have like characteristics and like components and perform same functions. In both the cases, (a) quality and reputation (including trade mark reputation) should be same (b) Goods should be from same country, (c) Goods produced by another manufacturer can be considered if price of goods produced by same manufacturer are not available. However, brand reputation and quality of other manufacturer should be comparable (d) If engineering, development work, art work, design work, plan or sketch undertaken in India were completed by the buyer on these imported goods free of charge or at reduced rate for use in connection with the production and sale for export of these imported goods, the price cannot be considered.

'Similar' does not mean identical but means corresponding to or resembling to in many respects. - Vishrut Industries v. CCE 2001(130) ELT 225 (CEGAT).

Goods produced in Japan and goods produced in France cannot be termed as 'similar goods' for purpose of these rules - Nitisodya Diamond Tools v. CC - 1994 (74) ELT 49 (CEGAT)

Summary of valuation of 'Similar Goods'

i. Contemporaneous imported goods,
ii. Not like in all respect,
iii. Like characteristics and component materials,
iv. Perform same functions,
v. Commercially inter changeable w.r.t. quality, reputation & trademark,
vi. Produced in same country,
vii. 1st preference – same manufacturer,
viii. 2nd preference – only if same manufacturer not available then different manufacturer.

4.4.7 Deductive Value Method

Rule 7 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 provide for the next i.e. fourth alternative method, which is called 'deductive method'.

If the importer requests and the Customs Officer approves, 'computed value' method as given in rule 8 can be used before the method of 'deductive value' [proviso to Rule 6 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007].

This method should be applied if transaction value of identical goods or similar goods is not available; but these products are sold in India. The assumption made in this method is that identical or similar imported goods are sold in India and its selling price in India is available. The sale should be in the same condition as they are imported. Assessable Value is calculated by reducing post-importation costs and expenses from this selling price. This is called 'deductive value' because assessable value has to be arrived at by method of deduction (deduction means arrive at by inference i.e. by making suitable additions/subtractions from a known price to arrive at required 'Customs Value').

Price at or about the time of valuation - Price at or about the time at which goods in question are being valued should be considered. However, rule 7(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 provide that if such price is not available, price at the date after importation but within 90 days can be considered. Thus, if price prevalent prior to date of import of goods under-valuation is not available, even price subsequent to import of the goods can be considered under this rule.

Such sale should be in sufficient quantity to establish unit price.

Price after processing - If price of identical or similar goods in India is not available, but price in India is available after the imported goods are processed, such price can be considered after deducting processing cost. Such deduction should be on objective and quantifiable data. This method is not normally applicable if the imported goods lose identity after processing, unless value of imported component can be determined accurately without difficulty even after such conversion. This method also should not be applied if after processing, imported goods form a minor part of the processed goods. In such cases, reducing costs of other materials and processing costs from selling price of processed goods may not give reliable results [rule 7(3) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007].

The method may be used when goods are extracted on High Seas (e.g. minerals, crude oil etc.) and brought into India for sale. It will be 'import' and dutiable. In other cases, chances of using this method of valuation are indeed very rare.

Subtractions from selling price in India - Following subtractions should be made from selling price of imported goods in India, (a) Selling commission, general (selling) expenses and selling profits made in connection with sale of imported goods in India. General expenses includes direct and indirect cost of marketing the goods in question in India, (b) transport, insurance and associated costs within India (c) customs duties, sales tax and other taxes levied in India.

Seller in India of imported goods will incur all these expenses and hence, if is clear that 'CIF Value' can be arrived at i.e. 'deduced only after all these expenses are reduced from selling price of identical or similar goods sold in India. In other words, all (estimated) expenses incurred after importation of goods should be subtracted from selling price in India to arrive at 'CIF Price' of goods.

Unit price sold in greatest numbers - Rule 7 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 specify that while considering selling price of imported goods in India, unit price at which greatest aggregate quantity of identical or similar goods are sold to unrelated persons in India should be the basis. Interpretative Note to rule 7 of Customs Valuation Rules gives some illustrations - e.g. if 65 units are sold @ ₹100, 55 units are sold @ ₹95 and 80 units are sold @ ₹90; then greatest aggregate quantity is 80 which is sold @ ₹90 per unit, which will be the basis for valuation. Another example given in the Interpretative Note is that if 500 units are sold at price of ₹95 and 400 units are sold at ₹90, then greatest quantity is 500 and hence price of ₹95 should be considered.

Summary of valuation of 'Deductive value method'

i. Transaction value of imported goods or identical or similar goods is not ascertainable,

ii. Goods one sold in India after importation,

iii. Sale in India in same condition,

iv. Goods sold after further processing shall be considered,

v. Sale to unrelated person,

vi. Sales are made at or about the time (within a maximum 90 days after import),

vii. Unit price at which greatest number of unit it sold at the first commercial level after importation,

4.4.8 Computed Value Method

If valuation is not possible by deductive method, the same can be done by computing the value under rule 8 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 [earlier rule 7A upto 10-10-2007], which is the fifth method. If the importer requests and the Customs Officer approves, this 'computed value' method can be used before the method of 'deductive value' [proviso to Rule 6 of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007].

In this method, value is the sum of (a) Cost of value of materials and fabrication or other processing employed in producing the imported goods (b) an amount for profit and general expenses equal to that usually reflected in sale of goods of the same class or kind, which are made in the country of exportation for export to India, (c) The cost or value of all other expenses under rule 10(2) i.e. transport, insurance, loading, unloading and handling charges.

Method suitable when producer prepared to give costing - Generally, valuation should be done on basis of information available in India. Thus, this method is normally possible when the importer in India and foreign exporter are closely associated and the foreign exporter is willing to give necessary costing and to provide for subsequent verification, which may be necessary.

In Rabindra Chandra Paul v. CC(2007) 209 ELT 326 (SC), it was observed that this rule may be involved in agro processing, processing of seeds, refined oil from crude oil etc, where raw material has a crucial role to play in the method of costing.

How to calculate cost and profit - Interpretative Note to rule 8 [earlier rule 7A upto 10-10-2007] of Customs Valuation Rules explains how cost or value and profit should be calculated.

The Cost and Value should be on the basis of information supplied by or on behalf of the producer. The information should be on basis of commercial accounts based on generally accepted accounting practices. Cost of commission and brokerage and packing cost has to be added. Similarly, cost of material supplied free, tooling cost, development and engineering charges, design work cost etc. have also to be added. No cost should be counted twice.

How to calculate profit - The amount of profit and general expenses should be taken as a whole. A low profit and higher general expenses may occur in cases where for valid commercial reasons, the prices have been kept low e.g. (a) producers have to sale at lower profit due to unforeseen drop in demand (b) Goods are sold to complement a range of goods produced in India and low price is accepted to maintain competitiveness. However, if the data of producer is not consistent with those generally reflected in sale of goods of same class sold in India, amount of profit and general expenses may be based on other relevant information.

What are General Expenses - General Expenses means direct and indirect cost of producing and selling goods for export, other than those already covered above. [In costing terminology, these are termed as 'overheads'.]

Same class or kind of goods - If data of profit and general expenses of another producer is considered, the goods should be of same class or kind. This should be within very narrow range of group of goods. It must be from same country and not from another country.

Summary of valuation of 'Computed Value Method'

i. When the producer is willing to give necessary costing data and subsequent clarification,

ii. Sum total of the production / processing cost of imported goods and,

iii. Add the usual profit and general expenses and,

iv. Add costs and charges as per Rule 10(2).

4.4.9 Residual Method

The sixth and the last method is called "residual method". It is also often termed as 'fallback method'. This is similar to 'best judgment method' of the Central Excise, Income Tax and Sales Tax. This method is used in cases where 'Assessable Value' cannot be determined by any of the preceding methods. While deciding Assessable Value under this method, reasonable means consistent with general provisions of these rules should be the basis and valuation should be on basis of data available in India. [Rule 9(1) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007].

The value cannot exceed normal price - The value so determined cannot be more than the 'normal price' i.e. price at which such or like goods are ordinarily sold or offered for sale for delivery at the time and place of importation in course of International Trade, when seller and buyer have no interest in the business of each other or one of them has no interest in the other and price should be sole consideration for sale or offer for sale [proviso to rule 9(1). There was no parallel proviso in earlier rule 8(1)].

Summary of valuation of 'Residual Value Method'

i. Value to be determined,

ii. Using reasonable means and section 14 & data available,

iii. Value so determined shall not exceeds the price at which such or like goods are ordinary sold at the time and place of importation in the course of international trade,

iv. Buyer or seller are not interest in business of other,

v. Selling price in India of goods produced in India can't take.

4.4.10 Inclusions/Exclusions in Customs Value

i. Valuation for customs is required to be done as per provisions of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007.

ii. CIF value of goods plus 1% landing charges is the basis for deciding 'Assessable Value'.

iii. Commission to local agents, packing cost, value of goods and tooling supplied by user, royalty relating to imported goods are to be added.

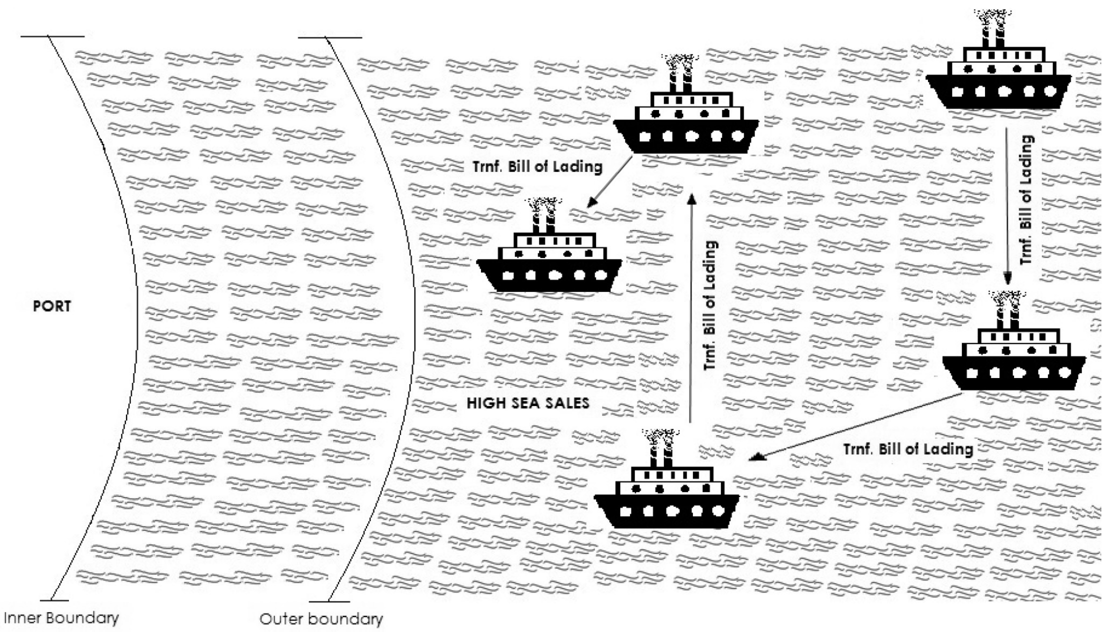
iv. Interest on deferred payment, demurrage at port is not required to be added.

v. Value of computer software loaded on machine is to be added to value of machinery.

vi. Old machinery and old cars are valued on basis of depreciated value, though such method has no sanction of law.

No other additions - No other addition shall be made to price paid or payable, except as provided for in rule 10 [rule 10(4) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007 (earlier rule 9(4)]. Interpretative Note to rule 3 (earlier rule 4) also clarifies that activities undertaken by buyer other than those for which adjustments are provided in rule 10 are not to be added, even though it may be regarded as benefit to the seller.

4.4.11 High Sea Sales



It is the responsibility of the importer to prove that the high seas sales transactions constituted transfer of goods. He has to establish a link between the first International transfer of goods to the last transaction.

Custom Valuation Rules, 1988, determination of assessable value for goods sold on high seas- In case the actual high sea sale contract price is more than ''the CIF value plus 2%'', then the ''actual contract price'' paid by the last buyer is being taken as the value for the purpose of assessment. In some of the custom Houses, however, audit has raised objection stating that if, in a particular transaction, there were about three/ four high-sea-sales, then high-sea-sales service charges @ 2% has to be added to the CIF value, for each such transaction.

4.4.12 "Green Channel Procedure" for Clearance of Imported Goods

Green Channel procedure has been introduced in major Custom Houses on experimental basis to expedite clearance of imported goods. This procedure is applied only in respect of certain specified imports.

Some of such imports identified are:-

a) Goods imported by Government departments and public sector undertakings, which do not require physical identification for the purpose of either ITC classification/ restrictions or Customs classification.

b) Imports under project Import Regulations.

c) Bulk imports sourced directly from reputed suppliers.

d) Consignments, which consist of single product of a well- known brand or specification, tested earlier and, covered by valid test report of an earlier import.

e) Imports by importers with proven identity and unblemished record of past conduct.

The Bills of Entry under this procedure are processed and assessed to duty under the second appraisement system i.e., assessment and duty collection is done first and then consignment examined. In such cases the Assessing Officer indicates on the reverse of the duplicate Bill of Entry to the Appraiser in charge of examination to 'Inspect the lot and check marks and numbers on the packages'. After inspection of the lot and marks and numbers of the packages with reference to the declaration in the Bill of Entry and other connection documents, the Docks Appraiser gives 'passed Out of Customs' order. The Docks Appraiser, in the presence of Assistant Commissioner may examine the goods in exceptional cases.

4.4.13 Practical Problems of Computing Customs Value

BCD, CVD & Spl. CVD

Example 9: D Ltd., an actual user imports certain goods from USA, at Chennai port, at cost of $1,00,000 FOB. The other details are as follows:

(i) Packing charges: $22,000.

(ii) Sea freight to Indian port: $28,000.

(iii) Transit insurance: $10,000.

(iv) Design and development charges paid to a consultant in USA by importer: $9,000.

(v) Selling commission to be paid by the Indian importer:₹ 5,000.

(vi) Rate of exchange announced by RBI:₹ 40.60/$.

(vii) Rate of exchange notified by the Central Board of Excise and Customs:₹ 40.70/$.

Rate of basic custom duty: 15%.

Compute the assessable value of the imported goods and the basic customs duty payable.

Answer :

Statement showing Assessable value of the imported goods and customs duty payable

Particulars	Value (in US$)	Remarks	Workings
FOB	1,00,000		
Add: Packing charges	22,000	Included into the Assessable value	
Add: sea freight	28,000	-Do-	No restriction on sea freight.
Add: insurance	10,000	-do-	
Add: Design and development charges	9,000	-do-	
Add: Selling Commission	122.8501	-do-	₹ 5,000/₹ 40.70
CIF value	1,69,122.8501		
Add: 1% loading and unloading on CIF	1,691 .2285		$ 1,69,122.8501 x 1%
Assessable Value	1,70,814.0786		

Particulars	Value in ₹	Remarks	Workings
Assessable Value	69,52,133		USD 1,70,814.0786 x ₹ 40.70
Add: Basic Customs Duty	10,42,820		₹ 69,52,133 x 15%
Add: 2% Education cess	20,856		₹ 10,42,820 x 2%
Add: 1% SAH Education cess	10,428		₹10,42,820 x 1%
Landed value	80,26,237		

Example 10: The following information is furnished by Mr. K on 8th June 2015, in respect of articles of jewellery imported from USA in the month of April 2015.

FOB value	$20,000
Exchange rate	$1 =₹ 44
Air freight	$4,500
Insurance charges	Not known
Landing charges	₹ 1,000
Basic customs duty	10%
Excise duty chargeable on similar goods in India as per tariff rate	12.5%
Additional duty of customs u/s 3(5) of the Customs Tariff Act, 1975	As applicable.

Calculate the total customs duty payable by Mr. K.

Answer :

Statement showing customs duties payable by Mr. K.

Particulars	USD ($)	Remarks	Workings
FOB	20,000		
Add: Air freight	4,000	Air freight should not exceed 20% on FOB	20,000$ x 20%= 4,000
Add: Insurance	225		1.125% on FOB
CIF value	24,225		
Add: 1% loading and unloading	242.25		24,225 x 1%
Assessable value	24,467.25		
	Value in ₹		
Assessable value	10,76,559		USD24,467.25 x ₹ 44
Add: Basic Customs Duty	1,07,656		₹ 10,76,559 x 10%
Sub-total	11,84,215		
Add: CVD 12.5%	1,48,027		₹ 11,84,215 x 12.5%
Sub-total	13,32,242		
Add: 2% education cess	5,114	2% calculated on BCD plus CVD	₹ 2,55,683 x 2%
Add:1% SAH education cess	2,557	1% calculated on. BCD plus CVD	₹ 2,97,130 x 1%
Sub-total	13,39,913		
Add: Spl . CVD u/s 3(5) of the Customs Tariff Act, 1975	53,597	Spl. CVD is equal to 4%	₹ 13,39,913 x 4%
Value of imported goods	13,93,510		
Total Customs Duty	₹ **3,16,951**		

Example 11: A consignment is imported by air. CIF price is 2,000 Euro. Air freight is 550 Euro and insurance cost is Euro 50. Exchange rate announced by CBE&C as per customs notification is 1 Euro = ₹ 54.15. Basic customs duty payable is 10%. Excise duty on similar goods produced in India is 12.5%. Find value for customs purpose and total customs duty payable. How much Cenvat can be availed by importer, if he is manufacturer?

Answer :

Particulars	**Value in EURO (€)**	**Remarks**	**Workings**
CIF price	2,000		
Less: Air freight	550		
Less: Insurance	50		
FOB price	1,400		
Add: Air freight	280	Restricted to 20% on FOB	EURO 1,400 × 20%
Add: Insurance	50		
CIF (corrected value)	1,730		
Add: 1% unloading on CIF value	17.30		EURO 1,730 × 1%
Assessable Value	1747.30		
	Value in ₹		
Assessable value	94,616	Relevant exchange rate is ₹ 54.15 per EURO	EURO 1,747.30 × 54.15
Add; Basic Customs Duty	9,462	Relevant rate 10%	₹ 94,616 × 10%
Sub-total	1,04,078		
Add: CVD	13,010	Relevant rate 12.5%	₹ 1,04,078 x 12.5%
Sub-total	1,17,088		
Add: 2% Education Cess	449		₹ 22,472 × 2%
Add: 1%SAH education cess	225		₹ 22,472 × 1%
Sub-total	1,17,762		
Add: Spl . CVD	4,710		₹ 1,17,762 × 4%
Total value of imported goods	1,22,472		
Total Customs Duty	**27,856**		

Importer, if he is manufacturer can avail the following duties as Cenvat credit under Cenvat Credit Rules, 2004 is as follows:

CVD = ₹ 13,010 & Spl. CVD = ₹ 4,710

Example 12: M/s. Premium Industries Ltd., has imported a machine from Japan at an F.O.B. cost of 1,00,000 yen (Japanese). The other expenses incurred were as follows: (i) Freight from Japan to Indian port 10,000 yen; (ii) insurance paid to insurer in India ₹ 5,000; (iii) Designing charges paid to consultancy ifrm in Japan 15,000 yen; (iv) M/s Premium Industries Ltd. spent ₹ 50,000 in India for development work connected with the machine; (v) Transportation cost from Indian port to factory ₹ 15,000; (vi) Central Government has announced exchange rate prevailing in the market was 1 yen = ₹ 0.40 by notification under section 14(3). However the exchange rate prevailing in the market was 1 yen = ₹ 0.4052 (vii) M/s Premium Industries Ltd. made payment to the bank based on exchange rate of 1 yen = ₹ 0.4150, (viii) The commission payable to the agent in India was @5% of F.O.B. price in Indian rupees. The rate is BCD @10%. Similar goods are subject to 12.5% excise in India. Education cess and special CVD is as applicable. Find the customs duty and other duties payable. How much CENVAT can be availed by importer, if he is manufacturer?

Answer :

Particulars	Japanese Yen
FOB	1,00,000
Add: Freight	10,000
Add: Designing charges	15,000
Sub-total	1,25,000

	Value in ₹
Sub- total (1,25,000 YEN x ₹0.40)	50,000
Add: Insurance	5,000
Add: Commission (1,00,000 YEN x 5% x ₹0.40)	2,000
CIF Value	57,000
Add: 1% unloading on CIF	570
Assessable Value	**57,570**

Calculate of Custom Duty payable:

@10%BCD is ₹ 5,757, CVD @12.5% is ₹ 7,916, Education Cess is ₹ 273, SAH Education Cess is ₹137 and Special CVD @4% is ₹ 2,866. Total Customs Duty payable is ₹ 16,949.

Cenvat credit of ₹ 7,916 (CVD) can be availed up to 50% in the first year and balance in the subsequent years. However, with regard to Special CVD is ₹ 2,866 can be availed fully in the first year itself.

Example 13: Compute the Customs duty from the following data— (i) Machinery imported from USA by Air (FOB) 8,000 US $, (ii) Accessories were compulsorily supplied with Machine (Electric Motor & others) (FOB) 2,000 US $, (iii) Air freight 3,000 US$ (iv) Insurance 100 US $, (v) Local agents commission to be paid in Indian Rupees is ₹ 4,500 (say equivalent to US $ Dollars 100), (vi) The exchange rate is 1 US Dollars = Indian Rupees is ₹ 45, (vii) Customs duty on Machinery –10% ad valorem, (viii) Customs Duty on Accessory –normal rate 20% *ad valorem,* (ix) CVD – 24% (Effective Rate is 16% by a notification), (x) Education Cess and special CVD is as applicable. How much Cenvat can be availed by importer, if he is manufacturer?

Answer :

	US $
FOB value of Machinery	8,000
FOB value of Accessories compulsorily supplied with machine	2,000
Total FOB value	10,000
Add: Air freight 20% on FOB is US$ 2,000 or US $ 3,000	2,000
(WHICHEVER IS LOWER) Add: Insurance	100
Add: Commission	100
CIF Value	12,200
Add: 1% unloading charges on CIF value	122
Assessable Value	12,322
	=======
Assessable value (i.e. US $ 12,322 x₹ 45)	Value in ₹ 5,54,490

Calculation Custom duties: BCD ₹ 55,449, CVD ₹ 97,590, EC ₹ 3,061, SHEC ₹ 1,530 and SPL. CVD ₹ 28,485

CENVAT credit available to the importer being a manufacturer is ₹ 97,590 (CVD) and Special CVD is ₹ 28,485.

Cenvat Credit	Amount in ₹
CVD (₹ 97,590 × 50%)	48,795
SPL. CVD (100% allowed as Cenvat Credit)	28,485
TOTAL	77,280

Note: CENVAT credit on CVD can be availed up to 50% in the 1st year and balance in the subsequent years.

Example 14: 'A' import by air from USA a gear cutting machine complete with accessories and spares. Its HS classification is 8461 40 10 and value US $ F.O.B. 20,000 other relevant date/ information: (1) At the request of the importer, US $ 1,000 have been incurred for improving the design, etc. of machine, but is not reflected in the invoice, but will be paid by the party, (2) Freight – US $ 6,000, (3) Goods are insured but premium is not shown/ available in invoice, (4) Commission to be paid to local agent in India ₹ 4,500, (5) Freight and insurance from airport to factory is ₹ 4,500, (6) Exchange rate is US $ 1 = ₹ 45, (7) Duties of customs: basic – 10%, CVD – 12.5% Education Cess on duty as applicable. Compute (i) Assessable value (ii) customs duty. How much CENVAT can be availed by importer, if he is manufacturer?

Answer:

Assessable Value ₹ 11,51,021, BCD is ₹ 1,15,102, CVD @12.5% is ₹ 1,58,265, Education Cess is ₹ 5,467 and S&H Education Cess is ₹ 2,734. Total Customs duty is ₹ 2,81,568.

Note: CENVAT credit is ₹ 1,51,935 (CVD). Up to 50% of CVD can be avail in the 1st year and the balance in the subsequent years. It is assumed that Spl. CVD is exempted.

Example 15: Compute the duty payable under the Customs Act, 1962 for an imported equipment based on the following information:

Assessable value of the imported equipment US $10,100.

Date of Bill of Entry 25.4.2015 basic customs duty on this date 20% and exchange rate notiifed by the Central Board of Excise and Customs US $ 1 = ₹ 65.

Date of Entry inwards 21.4.2015 Basic customs duty on this date 12% and exchange rate notiifed by the Central Board of Excise and Customs US $ 1 =₹ 50.

Additional duty payable under section 3(1) and (2) of the Customs Tariff Act, 1975: 12.5%.

Additional duty under section 3(5) of the Customs Tariff Act, 1975: 4%.

Educational cess @2% in terms of the Finance Act (No. 2), 2004 and secondary and higher educational Cess @ 1% in terms of the Finance Act, 2007.

Make suitable assumptions where required and show the relevant workings and round off your answer to the nearest Rupee.

Answer :

	Value in ₹
A.V	6,56,500 (10,100 x 65)
ADD: BCD 20% on ₹6,56,500	1,31,300
Balance	7,87,800
ADD: CVD 12.5% on ₹7,87,800	98,475
Balance	8,86,275
ADD: 2% EDU. CESS	4,596 (2,29,775 x 2%)
ADD: 1% SAH EDU. CESS	2,298 (2,29,775 x 1%)

Balance	8,93,169
ADD: SPL. CVD (4% ON ₹ 8,93,169)	35,727
Value of Imported Goods	9,28,896
Customs Duty	2,72,396

BCD, CVD & Spl. CVD and CENVAT CREDIT:

Example 16: CIF value of imported goods is ₹ 10,00,000. Basic Customs duty payable is 10%. If the goods were produced in India, excise duty payable would have been 12.5%. Education Cess is 2% and SAH Education Cess is 1 %. Special CVD is payable at appropriate rates. Find the Customs duty payable. What are the duty refunds /benefits available if the importer is (a) manufacturer or, (b) service provider or, (c) trader?

Answer :

Statement showing assessable value and customs duties

Particulars	**Value in ₹**	**Workings**
CIF value	10,00,000	
Add: 1% unloading charges	10,000	₹ 10,00,000 x 1%
Assessable value	10,10,000	
Add: Basic Customs Duty	1,01,000	₹ 10,10,000 x 10%
Sub-total	11,11,000	
Add: CVD @ 12.5%	1,38,875	₹ 11,11,000 x 12.5%
Sub-total	12,49,875	
Add: 2% Education cess	4,798	₹ 2,39,875 x 2%
Add: 1% SAH Education cess	2,399	₹ 2,39,875 x 1%
Sub-total	12,57,072	
Add: Spl. CVD	50,283	₹ 12,57,072 x 4%
Value of imported goods	13,07,355	

The following import duties are allowed as CENVAT credit:

If the importer	**BCD**	**CVD ₹**	**SPL.CVD ₹**	**Edu. CESS**
Manufacturer	CENVAT credit not allowed	1,38,875	50,283	CENVAT credit not allowed
Service provider	CENVAT credit not allowed	1,38,875	CENVAT credit not allowed	CENVAT credit not allowed
Dealer	CENVAT credit not allowed	CENVAT credit not allowed	CENVAT credit not allowed. However refund is allowed if VAT paid. (₹ 50,283)	CENVAT credit not allowed

Revised CIF Value:

Example 17: Robotics Private Limited imported some goods by air from ABC Inc. of US. Compute the value of the goods for the purpose of levying the duty:-

Particulars	**Dollars($)**
CIF value	5,000
Freight paid	1,500
Insurance cost	500

The banker realized the payment from importer at the exchange rate of ₹ 45 per US $.

Central Board of Excise and Customs notified the exchange rate as ₹ 44.50 per US $.

Basic Customs Duty @10% advalorem. There is no CVD and Special CVD. Find the total import duty.

Answer:

Particulars	**US $**
CIF value	5,000
Less: Air Freight	1,500
Less: Insurance	500
FOB value	3,000
Add: Insurance	500
Add: Air Freight 20% on FOB	600
CIF value	4,100
Add: 1% unloading charges on CIF value	41
Assessable value	4,141
Assessable value in ₹ 1,84,275 (i.e.₹ 44.50 x US $ 4,141) Total customs duty =₹ 18,980 (i.e.₹ 1,84,275 x 10.30%)	

Import of MRP Products and Cenvat Credit

Example 18. Assessable value of certain goods imported from USA in ₹ 10,00,000. The packet contains 10,000 pieces with maximum retail price ₹ 200 each. The goods are assessable under Section 4A of the Central Excise Act, 1944, after allowing an abatement of 40%. The excise duty rate is 8% advalorem. Calculate the amount of Additional duty of Customs under Section 3(1) of the Customs Tariff Act, 1975; assuming basic customs duty@10% advalorem.

Answer :

MRP of imported goods	= ₹ 20,00,000	(i.e. ₹ 200 x 10,000 pieces)
Less: abatement @ 40%	= ₹ 8,00,000	(i.e. ₹ 20 lakhs x 40%)
Assessable for CVD purpose	= ₹ 12,00,000	

Additional Duty of Customs under Section 3(1) of the Customs Tariff Act, 1975 is ₹ 96,000. (i.e. ₹ 12 lakhs x 8%)

Valuation of Imported Goods (Rule 4)

Example 19: A consignment of 8,000 units of product X was imported from USA by a charitable organization in India for free distribution to below poverty line citizens in a backward area. This being a special transaction, a nominal price of US$ 50 per product was charged for the consignment to cover the freight and insurance charges. The Customs House found out that at or about the time of import of this gift consignment, there were following imports of product X from USA:

S. No.	**Quantity imported in metric tonnes**	**Unit price in US $ (CIF)**
1.	200	260
2.	1,000	220
3.	5,000	200
4.	9,000	175
5.	4,000	180
6.	7,800	160

The rate of exchange on the relevant date was 1 US $ = ₹ 50.00 and the rate of basic customs duty was 10% ad valorem. There is no countervailing duty or special additional duty. Calculate the amount of duty leviable on the consignment under the Customs Act, 1962 with appropriate assumptions and explanations where required.

Answer :

		US$
CIF value	=	160.00
Add: 1% unloading charges on CIF value	=	1.60
Assessable value per unit	=	161.60
		Value in ₹
Assessable value for total import	=	6,46,40,000 (i.e. 161.60 x 8,000 units x ₹50)
Add: Customs Duty	=	66,57,920 (i.e. 6,46,40,000 x 10.30%)
Total value of imports	=	7,12,97,920

Anti-Dumping Duty

Example 20: A commodity is imported into India from a country covered by a notification issued by the Central Government under section 9A of the Customs Tariff Act, 1975. Following particulars are made available:

CIF value of the consignment: US$25,000

Quantity imported: 500 kgs.

Exchange rate applicable:₹ 50= US$1

Basic customs duty: 20%

Education and secondary and higher Education Cess as applicable as per the Finance Act, 2008.

As per the notification, the anti-dumping duty will be equal to the difference between the costs of commodity calculated @US$70 per kg. and the landed value of the commodity as imported.

Appraise the liability on account of normal duties, Cess and the anti-dumping duty.

Assume that only 'Basic Customs Duty' (BCD) and Education and Secondary and Higher Education Cess are payable.

Answer : Statement showing land value of imported goods and anti-dumping duty:

Particulars	**US $**
CIF value	25,000
Add: 1% unloading charges on CIF	250
Assessable value	25,250
	Value in ₹
Assessable value (i.e. 25,250 x ₹ 50)	12,62,500
Add: Customs duty 20.60% on Assessable value	2,60,075
Landed value (or value of imported goods)	15,22,575
Market value of imported goods (500 kgs x ₹ 50 x US$70)	17,50,000
Anti-dumping duty (₹ 17,50,000 – ₹ 15,22,575)	2,27,425
Total customs duty payable	₹ **4,87,500**

4.5 EXPORT GOODS - VALUATION FOR ASSESSMENT

Customs value of export goods is to be determined under section 14 of Customs Act, read with Customs Valuation (Determination of Value of Export Goods), Rules, 2007. Transaction value at the time and place of exportation, when price is sole consideration and buyer and sellers are unrelated is the basic criteria If there is no sale or buyer or seller are related or price is not the sole consideration, value of the goods will be determined as per Valuation Rules [Clause (ii) of second proviso to section 14(1)].

4.5.1 Valuation when buyer and seller are related

Definition of related person as per rule 2(2) of Customs Valuation (Determination of Value of Export

Goods) Rules, 2007 is same as per definition of rule 2(2) of Customs Valuation (Determination of Value of Imported Goods) Rules, 2007.

As per rule 3(2) of Customs Valuation (Determination of Value of Export Goods) Rules, 2007, the transaction value, the transaction value will be accepted as 'value' even if buyer and seller are 'related', if the relationship has not influenced price.

4.5.2 Valuation if value cannot be determined on basis of transaction value

If valuation is not possible on basis of transaction value, valuation will be done by proceeding sequentially through rules 4 to 6 [Rule 3(3) of Customs Valuation (Determination of Value of Export Goods) Rules, 2007].

The methods are - Export value by comparison on the basis of transaction value of 'goods of like kind and quality' exported at or about the same time to other buyers in same destination country [Rule 4}, Computed value on basis of cost of production plus profit [Rule 5] and Residual method using reasonable means consistent with principles and general provisions of rules [Rule 6].

4.5.3 Rejection of Value as Declared by Exporter

As per rule 7 of Customs Valuation (Determination of Value of Export Goods) Rules, 2007, the exporter has to file declaration about full 'value' of goods. If the assessing officer has doubts about the truth and accuracy of 'value' as declared, he can ask exporter to submit further information, details and documents. If the doubt persists, the assessing officer can reject the value declared by importer. [rule 8(1) of Customs Valuation (Determination of Value of Export Goods) Rules, 2007]. If the exporter requests, the assessing officer has to give reasons for doubting the value declared by exporter [rule 8(2)].

4.5.4 Rule 8 is only Mechanism to Reject the Declared Value

As per *explanation (1)(i)* to rule 8, the Rule 8 does not provide any method for determination of value. It only provides mechanism to reject declared value, where there is reasonable doubt.

Declared value shall be accepted if assessing officer is satisfied about truth and accuracy of the declared value [Explanation (1)(ii) to rule 8 of Customs Valuation (Determination of Value of Export Goods) Rules, 2007].

4.6 SELF ASSESSMENT ON BASIS OF 'RISK MANAGEMENT SYSTEM'(RMS)

One major step is being taken to move in the direction of implementing international best practices in customs clearance. A 'Risk Management System' for customs clearance of import and export cargo has been introduced. The details of scheme are contained in MF (DR) circular No. 43/2005-Cus dated 24-11-2005– see also CC, Bangalore-I PN 88/2006 dated 31-7-2006 (201 ELT T5). Initially, the scheme will be introduced in Air Cargo Complex, Sahar Mumbai and then it will be introduced in other customs houses in phases. Under Risk Management System (RMS), only high risk cargo is selected for examination. The system provides for special customs clearance for Accredited Clients having good track record and meet specified criteria.

The scheme proposes to do away with existing system of routine assessments and concurrent audit. Goods will be normally cleared on basis of self assessment of importer. Bill of Entry submitted electronically will be transmitted to RMS. The RMS will process the data and produce an electronic output. This output will determine whether the Bill of Entry will be taken up for appraisement/examination or be cleared after payment of duty without any assessment and examination. Any change is system will require prior approval of Principal Commissioner or Commissioner of Customs and after recording reasons. Focus will be on quality assessment, examination and post clearance audit of Bills of Entry selected by the Risk Concurrent audit will be replaced by Post Clearance Audit on Bill of Entry selected by the Risk Management System. Subsequently, demand can be raised even if goods have been cleared from customs.

4.6.1 No change in Custom Act and Rules

The scheme is being introduced without making any change in Customs Act or Rules, the basic procedures of sanctions and approvals remain unaltered and hence is not similar to scheme of self-assessment under Central Excise, where clearances are affected by assessee without supervision or presence of excise inspectors. Scope of the scheme is also very limited.

4.6.2 Scheme open only to 'Accredited Clients'

The scheme is limited to only 'Accredited Clients' as defined in MF (DR) circular No. 42/2005-Cus dated 24-11-2005. They should have imported goods valued at ₹ 10 crores in previous financial year or paid duty more than ₹ 1 crore. In case of importers who are central excise, they should have paid at least ₹ 1 crore of duty through PLA in previous financial year. They should have filed at least 25 Bills of Entry in the previous financial year.

4.7 PROCEDURES FOR IMPORT

Import Procedure has been explained as follows

Goods should arrive at customs port

↓

Person in charge of conveyance is required to submit import general Manifest/import report

↓

Goods can be unloaded only after grant of entry inward

↓

Importer has to submit Bill of Entry

↓

Goods are assessed to duty

↓

Goods can be cleared from port after payment of Duty/cleared for warehousing

↓

Out of customs charge order is issued by customs officer after payment of duty.

4.7.1 Goods should arrive at Customs Port/Airport only

i. Person in charge of conveyance is required to submit Import Manifest or Export-Manifest,

ii. Goods can be unloaded only after grant of 'Entry Inwards',

iii. Importer has to submit Bill of Entry giving details of goods being imported, along with required documents. Electronic submission of documents is to be done in many ports,

iv. Goods are assessed to duty, examined and customs duty is paid. Bond is executed if required,

v. Goods can be cleared from port after 'Out of Customs Charge' order is issued by customs officer,

vi. Self Assessment on basis of 'Risk Management System' (RMS) has been introduced in some ports in respect of specified goods and importers,

vii. Demurrage is payable if goods are not cleared within three days from port. Goods can be disposed of if not cleared within 30 days.

4.7.2 Overview of Procedures for Import

The broad procedures to be followed for assessment and clearance of imported goods are as follows –

i. Importer to submit Bill of Entry giving details of goods to be cleared from customs,

ii. Bill of Entry can be for home consumption (i.e. clearance after payment of duty) (white colour) or for warehousing (keeping in warehouse without payment of duty and later clearing on payment of duty when required) (yellow colour),

iii. Importer to submit other documents like Invoices, contracts, product literature, packing lists, import license etc. So that customs officer can assess the imported goods under clearance,

iv. Noting of Bill of Entry by customs officer,

v. Examination of goods and assessment by customs officer (if first appraisement system) or assessment of goods on basis of documents (if second appraisement system),

vi. Pre-audit by customs department,

vii. Customs Officer to approve assessment (valuation of goods) on the Bill of Entry and return to importer,

viii. Importer to execute bond if clearance at concessional rate of duty subject to some conditions or clearance is under provisional assessment,

ix. Importer to pay duty, if clearance is for home consumption or execute bond, if clearance is for warehousing,

x. Inspection of goods (if assessment was under second appraisement system),

xi. Out of customs charge order by customs officer,

xii. Pay dues of port trust, pay demurrage (if applicable), pay other dues,

xiii. Transport the goods from customs.

These procedures are for import by ship/air/road. There is separate procedure for goods imported as a baggage or by post.

4.7.3 Submission of Bill of Entry

Bill of Entry is a very vital and important document which every importer has to submit to customs officer in respect of imported goods other than goods intended for transit or transhipment. Bill of Entry should be in prescribed form. It can be either for home consumption or for warehousing [section 46(1)]. It should include all goods mentioned in Bill of Lading or other receipt given by carrier to consignor [section 46(2)]. Importer has to declare that contents of Bill of Entry are true [section 46(4)]

i. Bill of Entry is for home consumption. Imported goods are cleared on payment of customs duty.

ii. Bill of Entry is for warehousing. It is also termed as 'into bond Bill of Entry' as bond is executed. Duty is not paid and imported goods are transferred to warehouse where these are stored.

iii. Bill of Entry is for clearance from warehouse on payment of customs duty. It is for ex-bond clearance.

4.7.4 When should the Bill of Entry be filed ?

Bill of entry can normally be filed to clear the goods after the Import General Manifest (IGM) is presented to the Custom officers by the steamer Agents/Airlines as the case may be. Provided that a bill of entry may be presented even before the delivery of such manifest or report, if the vessel or the aircraft or the vehicle by which the goods have been shipped an importation into India is expected to arrive within thirty days from the date of such presentation. In addition of the goods entered in the vessels manifest Bills of Entry are also required for the clearance of –

(a) Ship's stores if in considerable quantities.

(b) Ship's Ballast such as stone, sand, Shingla etc.

(c) Salvaged goods

(d) "Sweepings" of import cargo.

4.7.5 Any imported goods should be cleared within 30 days from the date of unloading of goods at a customs station failing which the goods maybe disposed of by way of auction.

4.7.6 Time limit to pay Duty once a Bill of Entry has been assessed:

Duty has to be paid within two days from the date on which the Bill of Entry is returned after assessment to the importer / Agent for payment of duty. If duty is not paid within the stipulated time, simple interest @ 15% p.a presently on amount of duty is payable (Section 47 of the Customs Act, 1962).

4.7.7 Documents to be submitted by Importer to Clear the Imported Goods for Home Consumption

Documents required by customs authorities are required to be submitted to enable them to *(a)* check the goods *(b)* decide value and classification of goods and *(c)* to ensure that the import is legally permitted. *The documents that are essentially required are :*

i. Copy of order/ contract.

ii. Supplier's invoice in four copies.

iii. Copy of the Letter of Credit.

iv. Import licence.

v. Bill of Lading (original and non-negotiable).

vi. Packing List (2 copies).

vii. Weight specification.

viii. Freight insurance memo.

ix. Manufacturer's test certificate.

x. Exchange slip for purpose of exchange rate.

xi. Certificate of origin.

xii. Delivery order issued by Shipping company, its agent or carriers.

xiii. If spare parts are being imported, invoice should indicate unit price and extended total of each item.

xiv. If invoice is for FOB, freight charges and insurance premium amount certificate should be attached.

xv. OGL declaration.

xvi. No commission letter to be given by importer i.e., Agent's commission, if any, has not been paid in India.

xvii. Customs declaration (4 copies)

xviii. Catalogue/write-up/ drawing for machinery items.

xix. Importer-Exporter Code Number.

xx. If second-hand machinery is being imported then Chartered Engineer's certificate is necessary as per the Import Export Policy.

xxi. If steel is being imported then analysis certificate from manufacturers.

xxii. In the case of chemicals and allied products like synthetic resin wax, literature showing chemical composition.

xxiii. Textile Principal Commissioner or commissioner's endorsement in respect of textile items.

4.7.8 Electronic Submission under EDI system

Customs work at many ports has been computerized. In that case, the Bill of Entry has to be filed electronically, i.e. through Customs EDI system through computerization of work. Procedure for the same has been prescribed vides Bill of Entry (Electronic Declaration) Regulations, 1995.

i. The broad procedures to be followed for exports are as follows –

ii. Submit Shipping Bill for export to customs authorities,

iii. Submit invoice, packing lists, contracts, export license (if applicable) and other related documents,

iv. Submit necessary declarations for export. Submit * GR/SDF/SOFTEX form as required under FEMA * Excise ARE-1form

v. Noting of Shipping Bill by customs officer

vi. Assessment i.e. valuation and classification of goods. Checking of Advance License, if applicable

vii. Custom check whether export is restricted/prohibited

viii. Examination of goods by customs officer

ix. Pay export duty, if applicable

x. Stuffing of container, if not already done

xi. 'Let export' Order by customs officer

xii. Obtain ARE-1 form duly signed by customs officer. Obtain Bill of Lading from shipping company. Submit proof of export to excise authorities.

Complete formalities relating to claim of duty drawback.

4.7.9 Prior Submission of Bill of Entry

After the goods are unloaded, these have to be cleared within stipulated time - usually three working days. If these are not so removed, demurrage is charged by port trust/airport authorities, which is very high. Hence, importer wants to complete as many formalities as possible before ship arrives. Proviso to section 46(3) of Customs Act allows importer to present bill of entry upto 30 days before expected date of arrival of vessel. In such case, duty will be payable at the rate applicable on the date on which ' Entry Inward' is granted to vessel and not the date of presentation of Bill of Entry, but rate of exchange will be as prevalent on date of submission of bill of entry. - confirmed in CC, New Delhi circular No 64/96 dated 10.12.1996 and CBE&C circular No. 22/97-Cus dated 4.7.1997.

Department has clarified that if vessel does not arrive within 30 days, filing of fresh bill of entry will be necessary and in such cases, date of filing fresh Bill of Entry will be considered for calculating rate of exchange.

4.7.10 Importer can Abandon the Imported Goods

He can abandon the imported goods at any time before the proper officer has given the order for clearance of the goods for home consumption or for warehousing. However if any offence has been committed in respect of the said goods, then the option to abandon the goods is not available.

4.7.11 Customs Recognized Brokers for the purposes of Customs Clearance who can be approved for clearance of Import

Every custom house has authorized Customs Brokers licensed by that particular custom house. Each Customs Brokers has a license / registration no. and identity cards which can be verified from the nearest Custom House / Custom Station.

An importer / exporter can file documents on his own account without the help of any Customs Brokers. But before this he must get an authority / permission from the proper officer for 'self – clearance'. It is not mandatory to take the help of the Customs Brokers in clearing consignment.

4.8 PROCEDURES FOR EXPORT

Export Procedure has been explained as follows

Submit shipping Bill for export to customs

↓

Submit invoice, packing lists, contracts etc.

↓

Submit Guarantee Receipt (GR), Statutory Declarations Form (SDF)

↓

Noting Shipping bill by customs office

↓

Valuation and classification of goods

↓

Customs check whether export is restricted or prohibited

↓

Examination of goods by customs officer

↓

Stuffing of container if not already done

↓

Let export order by customs officer

↓

Claim the duty drawback or export incentives.

The broad procedures to be followed for exports are as follows —

i. Submit Shipping Bill for export to customs authorities,

ii. Submit invoice, packing lists, contracts, exports authorization (if applicable) and other related documents,

iii. Submit necessary declarations for export. Submit* GG/SDF/SOFTEX form as required under FEMA* Excise ARE-1form,

iv. The 'Export Value Declaration' should be in form given in Annexure A to MF(DR) circular No. 37/2007-Cus dated 9-10-2007,

v. Noting of Shipping Bill by customs officer,

vi. Assessment i.e. valuation and classification of goods. Checking of Advance Authorization, if applicable,

vii. Custom check whether export is restricted/prohibited,

viii. Examination of goods by customs officer,

ix. Pay export duty, if applicable,

x. Stuffing of container, if not already done,

xi. 'Let export' Order by customs officer,

xii. Obtain ARE-1 form duly signed by customs officer. Obtain Bill of Landing from shipping company. Submit proof of export to excise authorities,

xiii. Complete formalities relating to claim of duty drawback.

4.8.1 Every Exporter should take following initial steps

Obtain BIN (Business Identification Number) from DGFT. It is a PAN based number

Open current account with designated bank for credit of duty drawback claims

Register licenses/advance license/DEPB etc. at the customs station, if exports are under Export Promotion Schemes.

4.8.2 RCMC Certificate from Export Promotion Council

Various Export Promotion Councils have been set up to promote and develop exports (e.g. Engineering Export Promotion Council, Apparel Export Promotion Council, etc.) Exporter has to become member of the concerned Export Promotion Council and obtain RCMC - Registration cum membership Certificate. Exporter should apply for registration with EPC that relates to his main line of business. However, exporter can take membership of any other EPC in addition –DGFT circular No. 2/2004-09 dated 6-10-2004.

4.8.3 Third Party Exports

Third party exports means exports made by an Exporter or Manufacturer on behalf of another exporter/s. The Shipping Bill shall indicate the names of both the exporter and/or manufacturer. The BRC, GR declaration, export order and the Invoice shall be in name of the third party exporter.

SEZ unit can export goods or software through a merchant exporter/status holder.

Merchant Exporter - Merchant Exporter means a person engaged in trading activity and exporting or intending to export goods.

4.9 TRANSIT AND TRANSHIPMENT OF GOODS

4.9.1 Transit of Goods (Section 53 of the Customs Act, 1962)

Any goods imported in any conveyance will be allowed to remain on the conveyance and to be transited without payment of duty, to any place out of India or any customs station.

Example 21: A vessel Bhishma, sailing from U.S.A. to Australia via India. Bhishma carries various types of goods namely ' A, B, C & D' . ' A & B' are destined to Mumbai Port and balance remains in the same vessel. Subsequently vessel chartered to Australia.

Find the imported goods and transit goods?

Answer:

Imported Goods are A & B

Transit goods are C & D

4.9.2 Transhipment of Goods (Section 54 of the Customs Act, 1962)

Transhipment means transfer from one conveyance to another with or without payment of duty. It means to say that goods originally imported from outside India into India, then transhipped to another vessel to a place within India or outside India.

4.9.3 Transhipment of goods without payment of duty under Section 54(3)

Transhipment of goods without payment of import duty is permissible only if the following conditions satisfy:

i. Transhipment of goods with foreign destination.

ii. The goods find place as Transhipment Goods in the Import of General Manifest (IGM) or Import Report in case of goods imported in a vehicle.

iii. Bill of Transhipment or Declaration of Transhipment filed.

iv. Goods must be transhipped to another vessel to place outside India.

Example 22: A vessel Bhishma, sailing from U.S.A to Australia via., India carries various types of products namely 'A, B, C & D'. 'A & B'are destined to Mumbai Port. On account of submission of **bill of transhipment** product 'A' transshipped to Chennai port as ultimate destination in India and product 'B' transhipped to Srilanka.

Find the imported goods, Transhipment goods and transit goods?

Answer :

Product 'A' is imported goods because its ultimate destination is in India.

Products ' A & B' are called as Transhipment goods, since these goods are transshipped to another vessel, Product ' A' transhipped to Chennai attracts import duty whereas product ' B' is destined to Srilanka without payment of duty.

Products C & D are transit goods since these goods remains in the same vessel Bhishma chartered to Australia.

4.10 EXEMPTIONS AND REMISSION

4.10.1 Basic conditions of Exemption and Remission

i. Exemption can be granted by Government by issuing a notification.

ii. Capital goods and spares can be imported under project imports at concessional rate of customs duty.

iii. Remission can be obtained on goods lost/pilfered in port.

iv. Title of imported goods can be relinquished and then no customs duty will be payable.

v. Goods exported can be re-imported. Concessional customs duty is payable in most of such re-imports.

4.10.2 Pilferage: Section 13 of the Customs Act, 1962

i. Pilferage means loss arising out of theft.

ii. No duty is payable at all under section 13, if the goods are pilfered.

iii. Importer does not have to prove pilferage, however, the pilferage is to find before the goods cleared from the customs.

iv. If the duty is paid before finding the pilferage, refund can be claimed if goods are found to be pilfered during examination but before order for clearance are made.

v. Section 13 does not apply for the warehoused goods.

4.10.3 Abatement of duty on damaged or deteriorated goods [Section 22]: Where it is shown to the satisfaction of the Assistant Commissioner of Customs or Deputy Commissioner of Customs,-

(a) that any imported goods had been damaged or had deteriorated at any time before or during the unloading of the goods in India; or

(b) that any imported goods, other than warehoused goods, had been damaged at any time after the unloading thereof in India but before their examination under section 17, on account of any accident not due to any wilful act, negligence or default of the importer, his employee or agent; or

(c) that any warehoused goods had been damaged at any time before clearance for home consumption on account of any accident not due to any wilful act, negligence or default of the owner, his employee or agent,

then, such goods shall be chargeable to duty determined in the following manner –

$$\boxed{\textbf{Duty leviable on such damaged or deteriorated goods}} = \frac{\text{Duty chargeable on the goods before the damage or deterioration}}{\text{Value of the goods before damage or deterioration}} \times \boxed{\text{Value of the damaged or deteriorated goods}}$$

$$\boxed{\text{Abatement of duty on damaged or deteriorated goods}} = \boxed{\text{Duty leviable on the goods before damage}} - \boxed{\text{Duty leviable on the goods after damage}}$$

Valuation of damaged/deteriorated goods: The value of damaged or deteriorated goods may be ascertained by either of the following methods (at the option of the owner),-

(1) The value of such goods may be ascertained by the proper officer; or

(2) Such goods may be sold by proper officer by public auction or by tender or with consent of owner in any other manner and the gross sale proceeds shall be deemed to be the value of such goods.

4.10.4 Loss or destruction of goods: Section 23 of the Customs Act, 1962

i. Loss or destruction (including leakage if any) must be due to fire natural calamity (like earthquake or bad weather).

ii. Section 23 applies only when there is no pilferage under section 13.

iii. Burden of proof is on importer to prove loss or destruction under section 23.

iv. Initially is duty levied under section 23 but the same is remitted by Assistant Commissioner of Customs. Once the duty is paid the same can be claimed for refund only if the remission is granted by Customs Department.

v. Loss or destruction should be found before clearance of goods from the customs.

vi. Section 23 is applicable even for the goods warehoused.

4.10.5 Pilfered goods u/s 13 vs. Lost or destroyed goods u/s 23

Pilfered goods u/s 13	Lost or destroyed goods u/s 23
Pilferage refers to that in small quantities	Lost or destroyed postulates loss or destroyed by whatever reason whether theft, fire, accident etc.
In this case, the importer is not liable to pay duty leviable on such goods.	The duty payable on lost goods is remitted by Assistant/Deputy Commissioner.
In this case, if the pilfered goods are retrieved duty becomes payable.	In this case, restoration is impossible if the goods one destroyed.
The pilferage must have occurred after the unloading of the goods but before the proper officer has made an order for clearance for home consumption under section 47 or deposit on a warehouse under section 60.	In this case, the goods must have been lost or destroyed at any time before their clearance for home consumption. Thus, it also covers the cases where the goods are lost after the duty has been paid and order for clearance has been given but before the goods are actually cleared.
These provisions do not apply to warehoused goods.	Section 23(i) is applicable to warehoused goods also.
The importer does not have to prove pilferage, as it is obvious at the time of examination by the proper officer.	In this case, the burden is cast on the importer to satisfy the Assistant/Deputy Commissioner that the imported goods have been lost or destroyed at any time before the physical clearance of the goods for home consumption.

4.10.6 Goods derelict, wreck, etc. [Section 21] :

All goods derelict, jetsam, flotsam and wreck brought or coining into India, shall be dealt with as if they were imported into India, unless it is shown to the satisfaction of the proper officer that they are entitled to be admitted duty-free under this Act.

4.10.7 Power to make rules for denaturing or mutilation of goods [Section 24] :

Section 24 of Customs Act 1962, provides that an importer can request Central Government to denature or mutilate the imported goods, which are ordinarily used for more than one purpose, so as to render them unfit for one or more of such purpose. If the goods are denatured or mutilated, they are assessed as if the goods were imported in denatured or mutilated form. The Central Government has framed Denaturing of Spirit Rules, 1972 in this regard.

4.10.8 Duty Liability in Certain Special Circumstances

Goods are imported into India after exportation there from.

Imported goods have been originally exported to the overseas supplier for repairs.

Exported goods may come back for repairs and re-export.

Re-importation of goods [Section 20] : In case if any goods have been imported into India after exportation therefrom, such goods shall be liable to duty and subject to such restrictions and conditions, if any, to which the goods of like kind and value are liable or subject on the importation thereof.

Re-imports are entitled for following concessions as have been notified by the Government:

Condition -1:

Goods exported under claim of drawback or under bond without payment of duty or under claim for rebate and re-imported within 3 years (or extended period, if any) without being re-manufactured/ re-processed.

Duty Liability: The amount of benefit availed on account of duty drawback and excise duty concessions/ rebate when the goods were exported. [Notification No. 94/96-Cus., dated 16-12-1996).

Condition -2:

Goods exported for repairs abroad and reimported by the same person within 3 years (or extended period, if any) without being re-manufactured/ re-processed, and also without change in ownership between export and re-import.

Duty leviable on a value = Fair cost of repairs carried out including cost of materials used in repairs (whether such costs are actually incurred or not) + Insurance and freight charges, both ways. [Notification No. 94/96-Cus., dated 16-12-1996).

Condition -3:

Goods manufactured in India and re-imported into India -

(a) for repairs or re-conditioning within 3 years from the date of exportation (in case of Nepal, such re-importation takes place within 10 years from date of exportation); or

(b) for reprocessing; or refining; or re-making; or other similar process within 1 year from the date of exportation.

Duty Liability: NIL, if -

(a) such goods are re-exported within 6 months from the date of their re-importation or such extended period not exceeding a further period of six months as the Principal Commissioner or Commissioner of Customs may allow; and

(b) the Assistant Commissioner of Customs is satisfied as regards identify of the goods; [Notification No. 158/95-Cus., dated 1411-1995].

4.11 REFUND OF CUSTOMS DUTY

Importer or Exporter actually paid the duty on import or export, which is not required to pay alone allowed as refund.

4.11.1 Refund of Export Duty

As per Section 26 of the Customs Act, 1962, duty paid on exported goods can be claim for refund in the case of combined reading of the following if:

i. The goods are returned to such person otherwise than by way of re-sale;

ii. The goods are re-imported within ***One year*** from the date of exportation and

iii. An application for refund of such duty is made before the expiry of ***six months*** from the date on which the Customs officer makes an order for importation.

Example 23: X Ltd. exported product ' P ' to Y Ltd of USA on 1.1.2016. The duty paid on export of product 'P' for ₹ 1,00,000. Y Ltd. returned product ' P ' to X Ltd., on 1.8.2016. The return is otherwise than by way of sale (i.e. it may be sale return or rejected goods, goods sent on consignment returned by the overseas agent or goods sent for exhibition coming back etc.). It means to say that Y Ltd. should not be sold ' P

' to X Ltd. Moreover, exported goods are returned within One year from the date of exportation. Hence, X Ltd. can claim for refund of ₹ 1,00,000 within Six months from Customs clearances order for imported goods (i.e. 1.8.2016).

4.11.2 Refund of Import Duty [Section 26A]

Duty paid on imported goods can be claim for refund on account of satisfying following conditions:

(a) Goods are found defective

The goods are found to be defective or otherwise not in conformity with the specifications agreed upon between the importer and the supplier of goods:

Provided that the goods have not been worked, repaired or used after importation except where such use was indispensable to discover the defects or non-conformity with the specifications;

(b) The goods have not been worked, repaired or used after importation except where such use was indispensable to discover the defects or non-conformity with the specifications;

(c) Goods are easily identifiable as imported goods

The goods are identified to the satisfaction of the Assistant Commissioner of Customs or Deputy Commissioner of Customs as the goods which were imported;

(d) No drawback claim is made

The importer does not claim drawback under any other provisions of this Act; and

(e) Activities carried out after importation

- The goods are exported; or
- The importer relinquishes his title to the goods and abandons them to customs; or
- Such goods are destroyed or rendered commercially valueless in the presence of the proper officer, in such manner as may be prescribed and within a period not exceeding 30 days from the date on which the proper officer makes an order for the clearance of imported goods for home consumption under section 47.

Note:

(i) However, the period of 30 days may, on sufficient cause being shown, be extended by the Principal Commissioner or Commissioner of Customs for a period not exceeding three months.

(ii) No refund under section 26 is allowed in respect of perishable goods and goods which have exceeded their shelf life.

Moreover, nothing contained in this section (Sec. 26A of the Customs Act, 1962) shall apply to the goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

(f) Manner and time-limit of claiming refund

An application for refund of duty shall be made before the expiry of 6 months from the relevant date in prescribed form and manner.

Relevant date:

Relevant date in case of filing refund claim may be any one of the following:

- Let export order issued or
- Date of abandonment or
- Date of destruction of goods

(g) Exceptions to this Section

(i) Offending goods: This section shall not apply to the goods regarding which an offence appears to have been committed under this Act or any other law for the time being in force.

(ii) Perishable goods or Expired goods : No refund shall be allowed in under this Section in respect of perishable goods and goods which have exceeded their shelf life or their recommended storage-before-use period.

4.11.3 Claim for Refund of Duty (Section 27 of the Customs Act, 1962)

Section 27 of the Customs Act, 1962 deals with refund of duty paid on imported or exported goods in excess of what was actually payable. Sometimes, such excess payment of duty may be due to shortage/ short landing, pilferage of goods or even incorrect assessment of duty by Customs. In such cases, any excess interest has been paid by the importer or exporter can also be claimed for refund.

Provided that if the amount of refund claimed is less than rupees hundered, the same shall not be refunded.

A refund claim can be made u/s 27 if the payment of higher duty and interest in ignorance of a notification which allowed payment of duty at a concessional rate even if there was no assessment order and the payment u/s 27(i) has not been made pursuant to an assessment order. Section 27(ii) covers those classes of cases where the duty is paid by a person without an order of assessment. It means a refund claim can be filed under section 27 of the Customs Act, 1962 even if the payment of duty has not been made pursuant to an assessment order *[Aman Medical Products Ltd.* v *CCus., Delhi* 2010 (250) ELT30 (Del.)].

Attested Xerox copy of the GAR-7 Challan sufficient for claiming refund.

Refund claim *CAN NOT BE DENIED* purely on a technical contention that the assessee had produced the attested copy of GAR -7 (earlier TR-6) challan and not the original of the GAR-7 challan. Also as per clarification issued vide F.No. 275/37/2K-CX. 8A dated 2-1-2002, a simple letter from the person who made the deposit, requesting for return of the amount, along with the appellate order and attested Xerox copy of the Challan in Form GAR-7 would suffice for processing the refund application. [Narayan Nambiar Meloths v CCus. 2010 (251) ELT57 (Ker)]

4.11.4 Time Limit for claiming refund:

Person claiming refund	Time limit for claiming refund	Remarks
Individual– imported goods for his personnel use, Government or Any educational institutions or Any research institutions or Charitable institutions or hospitals	Application for refund can be made before the expiry of ONE year from the date of payment of duty and interest	The application for refund in duplicate has to be filed before the Assistant Commissioner or Dy. Commissioner of Customs.
Individual – for business use Companies or Firm etc.	Application for refund can be made before the expiry of ONE year (w.e.f. 8-4-2011) from the dateof payment of duty and interest	The application for refund in duplicate has to file before the Assistant Commissioner or Dy. Commissioner of Customs.

4.11.5 Interest on delayed refunds

As per section 27A of the Customs Act, 1962, if the refund ordered is not paid within 3 months from the date of receipt of refund application by the Assistant Commissioner or Deputy Commissioner of Customs, then the department is liable to pay interest at the rate of 6% p.a. (i.e. interest is liable to be paid after expiry of three months from the date of receipt of the application for refund).

4.11.6 Few differences between section 26 and section 27 of the Customs Act, 1962

Section 26 deals with refund of export duty whereas Section 27 deals with refund of any export duty, import duty interest paid thereon.

Refund of duty under section 26 is allowed on account of satisfying certain conditions whereas refund under section 27 is allowed only when duty paid in excess of normal duty.

Refund is payable to the exporter who paid the duty under section 26 whereas refund is payable to the importer who paid the duty or to the buyer by whom the duty was borne.

Chartered Accountant Certificate not sufficient to claim refund under section 27.

As per section 27 of the Customs Act, 1962 the importer to produce such documents or other evidence, while seeking refund, to establish that the amount of duty in relation to which such refund is claimed, has not been passed on by him to any other person.

However, if importer had not produced any document other than the certificate issued by the Chartered Accountant to substantiate its refund claim.

In the given case Madras High Court held that, the certificate issued by the Chartered Accountant was merely a piece of evidence acknowledging certain facts. It would not automatically entitle a person to refund in the absence of any other evidence. Hence, the importer could not be granted refund merely on the basis of the said certificate *[CCus., Chennai v BPL Ltd. 2010 (259) ELT526 (Mad)]*.

The period of limitation of one year for the purpose of refund of duty under Sec. 27(1B) shall be computed in the following manner, namely:

(i) In the case of goods which are exempt from payment of duty by a special order issued under section 25(2) of the Custom Act, the limitation of one year shall be computed from the date of issue of such order;

(ii) Where the duty becomes refundable as a consequence of any judgment, the limitation of one year shall be computed from the date of such judgment.

(iii) Where any duty is paid provisionally under section 18, the limitation of one year shall be computed from the date of adjustment of duty after the final assessment thereof or incase of re-assessment, from the date of such re-assessment.

4.12 APPOINTMENT OF OFFICERS OF CUSTOMS

(1) Classes of officers of customs [Section 3]: The various classes of Officers of Customs, as given under section 3, are: -

(a) Principal Chief Commissioner or Chief Commissioners of Customs;

(b) Principal Commissioner or Commissioners of Customs;

(c) Commissioners of Customs (Appeals);

(d) Joint Commissioners of Customs;

(e) Deputy Commissioners of Customs;

(f) Assistant Commissioners of Customs;

(g) Such other class of officers of customs as may be appointed for the purposes of this Act.

Among the other classes of officers of customs, the following officers have been appointed:

(i) Appraisers of Customs, who do the assessment work of import and export goods, including classification, valuation and examination of the goods; and

(ii) Preventive Officers of Customs, who do the executive duties like,

 (a) Boarding and checking ships and aircrafts;

 (b) Clearing passengers and crew and their baggage;

 (c) Supervision and control over loading and unloading of cargo;

(d) Preventing smuggling by checking suspect;

(e) Interrogating suspects/witnesses and investigation.

(iii) Ministerial Officers, who maintain records, keep accounts, etc.

(iv) Chemical Examiner, who tests samples of imported or export cargo for determination of true character of the goods for proper classification and value, necessary for determination of customs duty.

(2) Appointment of officers of Customs [Section 4]: The Board may appoint such persons as it thinks fit to be officers of customs. The Board may authorise a Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner or joint or Assistant or Deputy Commissioner of Customs to appoint officers of customs below the rank of Assistant Commissioner of Customs.

(3) Powers of officers of customs [Section 5]:

(a) Subject to such conditions and limitations as the Board may impose, an officer of customs may exercise the powers and discharge the duties conferred or imposed on him under this Act.

(b) An officer of customs may exercise the powers and discharge the duties conferred or imposed under this Act on any other officer of customs who is subordinate to him.

Powers of Commissioner (Appeals): Commissioner (Appeals) shall not exercise the powers and discharge the duties conferred or imposed on an officer of customs other than those specified in Chapter XV and Section 108.

(4) Entrustment of functions of Board and customs officers on certain other officers [Section 6]: The Central Government may entrust either conditionally or unconditionally to any officer of Central or State Government or local authority any function of the Board or any officer of customs.

4.13 APPOINTMENT OF CUSTOMS STATION, WAREHOUSING STATIONS ETC.

(a) Power to approve landing places and specify limits of customs area [Section 8]: The Principal Commissioner or Commissioner of Customs has the power to -

(i) approve proper places in any customs port or customs airport or coastal port for the unloading and loading of goods or for any class of goods;

(ii) specify the limits of any customs area.

(B) Power to declare places to be warehousing stations [Section 9]: The CBEC has the power to declare places to be warehousing stations at which alone public warehouses may be appointed and private warehouses may be licensed.

(c) Appointment of boarding stations [Section 10]: The Principal Commissioner or Commissioner of Customs has power to appoint, in or near any customs port, a boarding station for the purpose of boarding of, or disembarkation from, vessels by officers of customs.

Appointment of customs ports, airports, etc. [Section 7]: The CBEC may, by notification in the Official Gazette, appoint the following,

(a) ports and airports, which alone shall be customs ports or customs airport for the unloading of imported goods and the loading of export goods or any class of such goods.

(b) places, which alone shall be inland container depots or air freight stations for the unloading of imported goods and the loading of export goods or any class of such goods. [Bold portion amended by Finance Act, 2012 w.ef. 28-05-2012]

(c) places, which alone shall be land customs station for the clearance of goods imported or to be exported by land or inland water or any class of such goods.

(d) routes by which alone goods or any class of goods specified in notification may pass by land or inland water into or out of India, or to or from any Land Customs Station, or from or to any land frontier.

(e) ports which alone shall be coastal ports for the carrying on of trade in coastal goods or any class of such goods with all or any specified ports in India.

4.14 CENTRAL GOVERNMENT POWER OF PROHIBITION, DETECTION OF ILLEGALLY IMPORTED AND EXPORT GOODS

Power to prohibit importation or exportation of goods [Section 11]: If the Central Government is satisfied that it is necessary so to do for any of the purposes as specified, it may, by notification in the Official Gazette, prohibit either absolutely or subject to such conditions (to be fulfilled before or after clearance) as may be specified in the notification, the import or export of goods of any specified description.

Purposes of prohibition: The importation or exportation of goods may be prohibited for following purposes,

(a) the maintenance of the security of India;

(b) the maintenance of public order and standards of decency or morality;

(c) the prevention of smuggling;

(d) the prevention of shortage of goods of any description;

(e) the conservation of foreign exchange and the safeguarding of balance of payments;

(f) the prevention of injury to the economy of the country by the uncontrolled import or export of gold or silver;

(g) the prevention of surplus of any agricultural product or the product of fisheries;

(h) the maintenance of standards for the classification, grading or marketing of goods in international trade;

(i) the establishment of any industry;

(j) the prevention of serious injury to domestic production of goods of any description;

(k) the protection of human, animal or plant life or health;

(l) the protection of national treasures of artistic, historic or archaeological value;

(m) the conservation of exhaustible natural resources;

(n) the protection of patents, trade marks and copyrights;

(o) the prevention of deceptive practices;

(p) the carrying on of foreign trade in any goods by the State, or by a Corporation owned or controlled by the State to the exclusion, complete or partial, of citizens of India;

(q) the fulfillment of obligations under the Charter of the United Nations for the maintenance of international peace and security;

(r) the implementation of any treaty, agreement or convention with any country;

(s) the compliance of imported goods with any laws which are applicable to similar goods produced or manufactured in India;

(t) the prevention of dissemination of documents containing any matter which is likely to prejudicially affect friendly relations with any Foreign State or is derogatory to national prestige;

(u) the prevention of the contravention of any law for the time being in force; and

(v) any other purpose conducive to the interests of the general public.

(i) Detection of illegally imported goods and prevention of their disposal [Section 11A to 11G]:

"Illegal import" means the import of any goods in contravention of the provisions of this Act or any other law for the time being in force.

- **Power of Central Government to notify goods:** Goods of any class or description may be notified by Central Government for the purpose of checking the illegal import of such goods or facilitating the detection of such goods.
- **Persons possessing notified goods to intimate the place of storage, etc.:** Every person who owns, possesses or controls, any notified goods, shall, within seven days from the notified date, deliver to the proper officer a statement in relation to the notified goods specifying the place where such goods are to be kept.
- **Persons possessing notified goods to maintain accounts:** Such person shall maintain true and complete account of such goods and also state the particulars of the person from whom such goods have been acquired or sold. Such accounts shall be kept at the place where such specified goods are kept.
- **Precautions to be taken by persons acquiring notified goods:** No person shall acquire any notified goods except by way of gift or succession, from any individual in India, unless such goods are accompanied by voucher or memorandum as specified in rules,

  The restrictions as specified above does not apply to any notified goods which are:

  (a) in personal use of the person by whom they are owned, possessed or controlled, or

  (b) kept in the residential premises of a person for his personal use.

(ii) Prevention or detection of illegal export of goods [Section 11H to 11M]:

"Illegal export" means the export of any goods in contravention of the provisions of this Act or any other law for the time being in force.

- **Power of Central Government to specify goods:** Goods of any class or description may be specified by the Central Government for the purpose of checking the illegal export of such goods or facilitating the detection of goods which are likely to be illegally exported.
- **Persons possessing specified goods to intimate the place of storage, etc.:** Every person who owns, possesses or controls, any specified goods, the market price of which exceeds? 15,000 shall, within seven days from the specified date, deliver to the proper officer an intimation containing the particulars of the place where such goods are kept within the specified area.
- **Persons possessing specified goods to maintain accounts:** Such person shall maintain true and complete account of such goods and also state the particulars of the person from whom such goods have been acquired or sold. Such accounts shall be kept at the place where such specified goods are kept.

  When the specified goods are lesser in quantity than the stock shown in accounts, then it shall be presumed, unless the contrary is proved, that shortfall has been illegally exported.
- **Transport of specified goods to be covered by vouchers:** No specified goods shall be transported from, into or within any specified area or loaded on any animal or conveyance in such area, unless they are accompanied by a transport voucher (in such form and containing such particulars as may be specified by rules made in this behalf) prepared by the person owning, possessing, controlling or selling such goods
- **Steps to be taken by persons selling or transferring any specified goods:** Every person who sells or otherwise transfers within any specified area, any specified goods (except where he receives payment by cheque drawn by the purchaser), shall obtain, on his copy of the sale or transfer voucher, the signature and full postal address of the person to whom such sale or transfer is made

and take such other reasonable steps as specified by rules. If on inquiry made by a proper officer, it is found that the purchaser or the transferee, as the case may be, is not traceable or is a fictitious person, it shall be presumed, unless the contrary is proved, that such goods have been illegally exported.

The restrictions as specified above shall not apply to petty sales of any specified goods if the aggregate market price obtained by such petty sales, made in the course of a day, does not exceed ₹ 2,500.

Explanation: "Petty sale" means a sale at a price which does not exceed one thousand rupees.

Power to exempt [Section 11N]: If the Central Government is satisfied that it is necessary in the public interest so to do, it may, by notification in the Official Gazette, exempt generally, either absolutely or subject to such conditions as may be specified in the notification, goods of any class or description from all or any of the provisions from Section 11A to 11.

4.15 WAREHOUSING IN CUSTOMS

(1) Need for warehousing

If the imported goods are not required immediately, importer may like to store the goods in a warehouse without payment of duty under a bond and then clear from warehouse when required on payment of duty. This will enable him to defer payment of customs duty till goods are actually required by him. In such case, importer can keep goods in warehouse without payment of customs duty. Goods are cleared from customs port under bond and kept in the warehouse. The importer can clear goods from customs warehouse on payment of duty when he requires the goods for use/consumption/sale.

This facility is available to traders as well as direct importers.

A trader can import goods and keep in warehouse. He can supply the goods to buyers from warehouse, after paying customs duty. Thus, small importers, duty free shops etc. can procure goods from bonded warehouse without actually importing the goods.

A manufacturer can import inputs without payment of customs duty for manufacture in bond. He will have to export final product which was manufactured using imported duty free material.

Even duty free clearances can be made from bonded warehouse, if buyer is otherwise eligible for obtaining goods duty free, as confirmed vide MF(DR) circular No. 79/2000- Cus dated 22-9-2000.

(a) Use of warehousing facility

The facility is useful to direct importers also, in following cases -

(a) Importer has to plan his purchases well in advance. He also has to maintain some stocks to ensure that there is no loss of production if a shipment of imported raw materials is delayed. Thus, when the goods arrive in the port, the importer may not immediately require the goods as he may be having stock.

(b) Importer would like to store the imported goods without payment of customs duty as far as possible and pay duty only when goods are required for his immediate use, so that his funds are not blocked.

(c) The importer may be intending to clear the goods without payment of duty under Advance Licence or DEPB scheme. However, the licence/DEPB may not be in hands when imported goods have arrived at the docks.

(d) The importer may not be having adequate ready funds to pay customs duty.

(e) Importer can avail facility of manufacture in bonded warehouse and then reexport the final products

Warehousing by traders - Foreign Trade Policy permits keeping imported goods in bonded warehouse without payment of duty. These can be cleared later on payment of duty. Even goods under negative list can be imported by traders and kept in warehouse. These can later be supplied on payment of duty against specific licence.

Sale/transfer of warehoused goods - Imported goods kept in warehouse can be transferred to another person as per section 50 of Customs Act. Sale of imported warehoused goods to Duty Exemption or duty concession licence holders is also allowed. In such case, transferee can clear the goods on payment of customs duty, if any, and fulfilling other licensing provisions - CBE&C Circular No. 473 /43/94-LCdated 22-9-1994. (The words 'if any', mean that if no duty is payable,

Warehousing pending registration of project under project import - In Bharat Earth Movers v. CC2006 (201) ELT 60 (CESTAT), goods were kept in warehouse as contract for project import was yet to be registered. Goods were cleared from warehouse after contract was registered.

Duty credit scrips can be used to clear goods from customs bonded warehouse -Duty Credit Scrips like SFIS, VKGUY, FMS, FS, SHIS schemes can be used to clear goods from Customs Bonded warehouse under same procedure as applicable for DEPB scrip, subject to conditions and limitations mentioned in FTP - MF(DR) circular No. 50/2011-Cus dated 9-11-2011.

Warehouse to store imported goods without payment of duty - Provision of warehousing has been made in Customs Act to enable importer to store goods in warehouse without payment of duty and clear goods from warehouse only when these are actually required by him. Importer only has to pay warehousing charges. Thus, he can delay payment of customs duty. Both public and private warehouses are available all over India where goods can be stored.

(b) Warehousing Bond

Since imported goods are kept in warehouse without payment of customs duty, importer has to execute a bond binding himself to (A) observe all provisions of Customs Act and rules/regulations in respect of the goods (B) pay on demand the (i) duties, interest (ii) warehousing rent and charges with interest (C) pay all penalties leviable for violations of provisions of Customs Act, rules and regulations. The bond amount is equal to twice the amount of duty assessed. Generally, part of bond amount is secured by way of a bank guarantee. Bond will continue to be valid even if goods are transferred to another person or removed to another warehouse **[section 59]**.

Bond is cancelled and returned only when duty and all other dues are paid on goods cleared and goods are duly accounted for **(section 73)**.

Bonded warehouse - Since goods are kept in warehouse under a 'bond', the warehouse is termed as 'bonded warehouse'. It does not necessarily mean that the warehouse is physically bonded. For example, in case of manufacture in warehouse, the manufacture is in 'bonded warehouse' but there is no physical supervision of customs officer. However, in case of goods stored in warehouse and cleared from warehouse on payment of duty, the warehouse is under physical control of customs officer and clearance can be only with his permission.

Warehousing of export goods

Goods removed for export can be kept in a warehouse pending export. These provisions are useful when exporter would like to store the goods and export them as soon as export order is received.

(2) Public/Private Bonded warehouses

As per section 2(43) of Customs Act, 'warehouse' means a public warehouse appointed u/s 57 or a private warehouse licensed under section 58 of Customs Act. As per section 2(44), 'warehoused goods' means goods deposited in a warehouse.

Sections 57 and 58 of Customs Act provide that 'warehouse' can be appointed or licensed only at a 'warehousing station'. As per section 2(45) of Customs Act, 'warehousing station' means a place declared as a warehousing station u/s 9 of Customs Act.

Warehouses can be public or private.

(a) Warehousing station - Section 9 of Customs Act authorises CBE&C (Board) to declare places as warehousing stations. Public and private warehouses can be situated only at such approved warehousing stations. Board has issued over 300 notifications prescribing various areas. Generally, cities and towns where imported goods are stored for use or where there is Industrial Estate where imported raw material is required are declared as 'Warehousing Stations'.

Power to declare a place as warehousing station under section 9 of Customs Act have been delegated to Principal Chief Commissioner or Chief Commissioner - Chapter 9 Para 32 of CBE&C's Customs Manual, 2011.

(b) Public or private Warehouses - Warehouses are of two types (A) Public warehouses appointed by Assistant Commissioner of Customs under section 57 of Customs Act. (B) Private warehouses licensed by Assistant/Deputy Commissioner of Customs. The licence can be cancelled by giving one month notice. Licence can be cancelled if licensee contravenes any provisions of Customs Act. In such cases, show cause notice has to be issued and pending enquiry, licence can be suspended.

As the name suggests, goods can be stored in Public Warehouse by any importer, while goods can be stored in private warehouse only by person who has been licensed.

Private warehouses are permitted quite liberally. Even private operators can be appointed as custodian for public warehouse. CBE&C has clarified that permission for public or private warehouse can be given by Principal Commissioner or Commissioner without making any reference to Board. Permission for storage of any category of goods can be given if the applicant is financially sound, has good credibility and has not been involved in customs or excise duty evasion in last five years. Premises of storage should be suitable and adequately secured. Services of Customs Officer should be provided on cost recovery basis, or on payment of supervision charges - CBE&C Circular No. 68/95 dated 5-6-1995.

For keeping sensitive goods in private as well as public bonded warehouse, bank guarantee equal to 25% of duty in respect of sensitive goods should be taken - MF(DR) circular No. 18/2007-Cus dated 24-4-2007.

PSUs shall be exempt from furnishing bank guarantee or other form of security for storing sensitive goods in the duty free shop operated by them. However, double duty bond is required to be executed - MF(DR) circular No. 26/2012-Cus dated 10-9-2012.

It is not necessary to obtain 'No objection certificate' from public warehouse before granting license to private bonded warehouse - CBE&C circular No. 1 /96-Cus dated 1-1-1996.

License to EOU by AC/DC - The license to EOU for warehouse (section 58) and permission to manufacture in warehouse under bond (section 65) will be granted by Assistant/Deputy Commissioner - MF(DR) Circular No. 9/2008-Cus dated 25-6-2008.

Warehousing charges even if goods detained by customs - Warehousing charges are payable in case of public warehouse, even if goods are detained by customs - Monika Indiav. UOI(2010) 260 ELT 177 (P&H HC DB).

(c) Procedure for warehousing imported goods

Imported goods are cleared from seaport/airport on submission of Bill of Entry for warehousing. This Bill of Entry is printed on yellow paper and often called 'Yellow Bill of Entry'. Bond is executed for transfer of goods from port to warehouse.

Space Availability Certificate - If the goods are to be despatched to public bonded warehouse, a 'Space Availability Certificate' is required, before movement of goods. However, in case of private warehouses, 100% EOU, STP, EHTP etc., such certificate is not necessary - CCCE Hyderabad PN 16/97 dated 12.2.1997.

Transit bond and insurance - The importer has to execute a bond for movement of goods from customs port to warehousing station. Bond should be with bank guarantee. He also has to take transit insurance to cover duty element while the goods are in transit. However, EOU, STP & EHTP units do not have to give bank guarantee. They have to give either bond or take transit insurance policy. - MF(DR) circular No. 41/97-Cus dated 19.9.1997, as amended vide circular No. 38/98-Cus dated 21.5.1998.

When the warehouse is within the City or within 50 Kms within the jurisdiction of Principal Commissioner or Commissioner of Customs, goods can be sent under escort. If the goods are outside city limits, transit bond in form of cash security or bank guarantee should be taken. This should be 50% of duty involved for sensitive goods and 25% for non-sensitive goods. -CBE&C circular No. 99/95-Cus dated 20-9-1995 amended vide CBE&C No. 47/99-Cus dated 27-7-1999.

The importer should submit re-warehousing certificate within 30 days from date of despatch of goods from seaport/airport. Otherwise, duty is payable.

Waiver of warehousing at port of import - If goods are to be taken to a port in interior town, goods should be warehoused at the port of importation and then removed to another warehouse under bond u/s 67. Since this will involve double handling of goods, Assistant Commissioner of Customs can grant waiver of physical warehousing at the port of importation.

(3) Warehousing period under customs

Section 61 of Customs Act prescribes warehousing period. If goods are not removed within the prescribed period, Customs Officer can sell the goods after notice to owner as much quantity as he deems fit.

(a) Normal warehousing for one year, extension can be granted - Section 61(l)(b) of Customs Act provides warehousing period as one year from the date of issue of order by Customs Officer permitting deposit of goods in a warehouse. The period of one year can be reduced by Principal Commissioner or Commissioner if goods are likely to deteriorate. This period can be increased by Principal Commissioner or Commissioner upto 6 months and by Principal Chief Commissioner or Chief Commissioner of Customs without any limit of period.

In case of EOU, the normal warehousing period is three years for inputs, spares and consumables and five years for capital goods, [section 61(1)]. This warehousing period can be extended by Principal Commissioner or Commissioner without any upper time limit.

(b) Policy for granting extension - While considering requests for extension of warehousing period, concerned authority should be satisfied about condition of goods and should ensure that the goods are not likely to deteriorate during the extended period of warehousing. Whenever necessary, goods should be tested for quality before granting extension of warehousing period. Interest accrued should be paid before granting extension. This interest caji be adjusted against final interest payable. A liberal approach may be adopted in following cases, if goods are in good condition - (i) Ship stores/aircraft spares (ii) Goods supplied to diplomats (iii) Goods warehoused and sold through duty free shops (iv) Goods imported by EOU (v) Goods used in units operating under manufacture-in-bond scheme (vi) Machinery, equipments and raw materials imported for building and fitment in ships. Trade should file application for extension 15 days prior to warehousing period. However, request for warehousing can be considered even after expiry of warehousing period, after taking into consideration exceptional circumstances of the case. Though powers for unlimited extension are with Principal Chief Commissioner or Chief Commissioner, the aforesaid guidelines should be kept in mind. - CBE&C circular No. 47/2002-Cus dated 29-7-2002. [Earlier CBE&C circular No. 12/98-Cus dated 5-3-1998 subsumed in this circular].

Principal Commissioner or Commissioner can grant extension upto 6 months, Beyond 6 months, Principal Chief Commissioner or Chief Commissioner can grant extension. Such extension by Principal Chief Commissioner or Chief Commissioner will normally be 3 months at a time. However, in respect of goods falling under categories (v) and (vi) of para 5 of Circular No. 47/2002-Cus dated 29-7-2002, extension can be granted for a period even greater than 3 months if goods are not likely to deteriorate and interest is paid. The extension is subject to overall limit of warehousing permitted under section 61 of Customs Act for relevant category of goods - MF(DR) Instruction No. 473/2/ 2011-LC dated 1-6-2011.

(c) Interest not payable at the time of granting extension - Interest is not payable at the time of granting extension. Interest is payable only when it is due and if not waived - MF(DR) Instruction F No. 473/02/2011-LC dated 29-2-2012.

(d) If warehousing period reduced by law - If warehousing period is reduced by amendment to law, the reduced period will not apply to goods warehoused prior to such amendment - Bangalore Wire Rod Mills v. UOI 1992(61) ELT 37 (Kar) - approved by SC - 83 ELT 251 (SC) - accepted by CBE&C vide MF(DR) circular No. 12/2007-Cus dated 9-2-2007.

(e) EOU should consume inputs etc. within the warehousing period - In case of EOU units, the whole factory is treated as a bonded warehouse. Hence, bonding period of three years means inputs, consumables and spares should be consumed for manufacture of export product within that warehousing period. If not, application for extension should be made. - - However, interest will be payable on the basis of duty payable at the time of clearance (and not duty assessed when goods were warehoused), [section 61(2)(i)].

(f) Five years warehousing for capital goods for EOU - The warehousing period can be upto five years in case of capital goods intended for use in EOU unit, as per section 61(1)(a) of Customs Act. This period can be reduced by Principal Commissioner or Commissioner if goods are likely to deteriorate. The period can be extended without any upper limit.

However, if goods are stored beyond a period of five years, interest is payable for storing goods beyond the period of five years in the warehouse. The interest is payable on the basis of duty payable at the time of clearance (and not duty assessed when goods were warehoused), [section 61(2)(i)].

Extension in respect of capital goods obtained by EOU units will be granted at the time of renewal of license of EOU, even if five years of those capital goods are not over -MF(DR) circular No. 7/2005-Cus dated 14-2-2005.

(g) Interest payable beyond prescribed period

In case of goods allowed to be warehoused, interest is payable at prescribed rate. In case of normal warehousing (other than EOU), interest is payable if goods are warehoused beyond 90 days, [section 61(2)(ii)].

Presently, the interest rate is 15% [Notification No. 18/2003-Customs (NT) dated 1-3-2003]. Earlier, the interest rate was 24%. In case of EOU, interest is payable if warehousing is beyond three years in case of inputs/ consumables/spares and five years in case of capital goods.

(h) Interest if goods cleared after warehousing period is over - Interest is payable even if goods are cleared after warehousing period is over, till date of clearance. Interest is payable even if notice demanding interest is not issued - Suresh Chand v. UOI (201 0)254 ELT (Bom HC DB).

(i) Interest for warehousing beyond 90 days - Even if goods are permitted to be stored for one year (plus extension if permitted), interest is payable for storing goods beyond a period of 90 days in the warehouse. The interest is payable on the basis of duty payable at the time of clearance (and not duty assessed when goods were warehoused) [section 61(2)(ii)].

(j) Interest if goods provisionally assessed were stored in warehouse - If goods provisionally assessed were stored in the warehouse, assessee cannot file Bill of Entry for ex-bond clearance. Hence, interest will be payable only after the provisional assessment is finalized by department. Importer cannot suffer for delay by department - Nirma Ltd. v. CC(2011) 263 ELT 261 (CESTAT)

(k) Policy for granting waiver of interest - In following cases, application for waiver of interest should be considered, as charging of interest would enhance costs unnecessarily - (i) Ship stores/aircraft spares (ii) Goods supplied to diplomats (iii) Goods warehoused and sold through duty free shops (iv) Goods imported by EOU (v) Goods used in units operating under manufacture-in-bond scheme (vi) Machinery, equipments and raw materials imported for building and fitment in ships (vii) Petroleum products (viii) Plant and machinery imported for projects (ix) Machinery, equipments and raw materials imported for manufacture and installation of power generation units (x) goods imported under OGL and warehoused for subsequent clearance under advance authorisation/ DEPB etc. (xi) Goods imported in bulk by canalising agencies (xii) Imports under EPCG scheme (xiii) Import of capital goods by PSU [MF(DR) circular No. 10/2006-Cus dated 14-2-2006]. It is also clarified that when no duty is payable, interest payment is not necessary.

Demand of interest should be raised when due, but it should not be enforced. On fulfilment of purpose of import, waiver of interest should be decided within 6 months - MF(DR) circular No. 10/2006-Cus dated 14-2-2006.

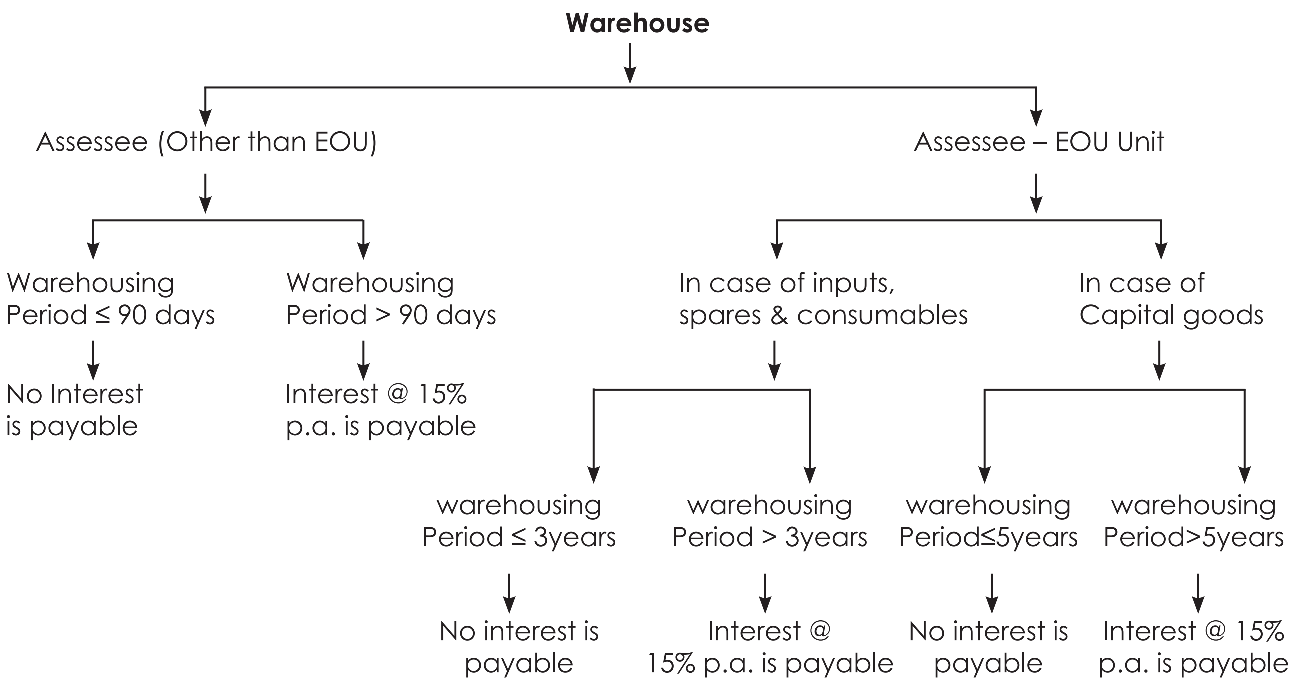
(l) Interest not payable when no customs duty payable - In some cases, no customs duty is payable on goods warehoused as they are exempt from duty on date of clearance. This may happen when goods are stored in warehouse as 'advance licence' is not available in hand. In such cases, goods are assessed at normal rates of customs duty and kept in warehouse. Subsequently, these are cleared after receipt of advance licence without payment of duty. In such cases, is interest payable beyond the period allowed for free warehousing? There were conflicting views. Finally, in Pratibha Processors v. UOI1996 AIR SCW 4299 = AIR 1997 SC 138 = 1996(11) SCC 101 = 88 ELT 12 (SC) it has been held that if no customs duty is payable at the time of clearance of goods from warehouse, no interest is payable. Interest is a mere 'accessory' to principal and if principal is not payable, interest is also not payable - view accepted by CBE&C vide circular No. 10/2006-Cus dated 14-2-2006 - reiterated in MF(DR) circular No. 26/2007-Cus dated 20-7-2007.

(m) Waiver of interest - Provision of interest @ 15% after just 90 days has made the provision of warehousing slightly unattractive. [Now, warehousing will be beneficial only when goods can be cleared later without payment of duty against advance license etc.]

Waiver of interest can be granted by Principal Chief Commissioner or Chief Commissioner upto ₹ two crores and by CBE&C above that.

(n) No interest if duty paid after warehousing period but before SCN? - In CC v. Stilbene Chemicals (2009) 236 ELT 78 (CESTAT), it was held that if duty is paid after warehousing period is over (but before issue of notice), interest is not payable - relying on Ghanshyam Das Suresh Chand v. UOI(2004) 165 ELT 514 (Del).

Summary of applicability of interest on warehouse goods



(4) Manufacture in customs bonded warehouse [Section 65]

Manufacturing or other operations can be carried out in the warehouse with sanction of Assistant Commissioner (section 65 of Customs Act). The facility is useful if final products are to be exported after manufacture (though final products can be cleared for home consumption too). After manufacture, the produced goods may either be exported without payment of customs duty or cleared for home consumption on payment of duty.

These provisions are applicable to EOU, STP, EHTP or BTP units who have to manufacture goods under customs bond. They have to obtain license from customs.

Facility for manufacture in warehouse under bond is also available for goods imported for repairs, re-conditioning, re-engineering etc. The goods can be imported without payment of customs duty and can be re-exported after repairs, reconditioning etc. Such re-export must be within three years from date of import. [Notification No. 134/94 - Cus dated 22-6-94]

Permission for in-bond manufacture facility can be given by Principal Commissioner or Commissioner. Permission can be given after scrutinising credibility and financial soundness of applicant - CBE&C circular No. 132/95-Cus dated 22-12-1995.

Permission by AC/DC in case of EOU - The license to EOU for warehouse (section 58) and permission for manufacture in warehouse under bond (section 65) will be granted by Assistant/Deputy Commissioner - MF(DR) Circular No. 9/2008-Cus dated 25-6-2008.

(a) Removal of waste or refuse arising during manufacture - If waste or refuse is generated during manufacturing operations, the provisions are as follows - (a) If the final product is exported, import duty on quantity of warehoused goods contained in such waste or refuse will be remitted if such waste or refuse is either destroyed, or duty is paid on such waste or refuse as if it had been imported into India in the form of waste or scrap (b) If final product is cleared for home consumption, import duty will be payable on quantity of warehoused goods contained in such waste or refuse [section 65(2) of Customs Act].

In view of section 65(2)(b) of Customs Act, import duty is payable on the quantity of the imported goods contained in the waste and not only on scrap value - Cochin Shipyards v. CC (2011) 267 ELT 387 (CESTAT).

(b) Conditions for manufacture in bonded warehouse

Board has framed 'Manufacture and Other Operations in Warehouse Regulations, 1966' prescribing procedures. Procedures for manufacture under bond have now been considerably simplified. Physical control and supervision of customs officer on the bonded warehouse has been done away with, since July 1998. - MF(DR) circular No. 88/ 98-Cusdated2-12-1998.

Owner has to make application giving full details regarding process to be carried out, imported and other goods used, plan and description of warehouse and volume of manufacture anticipated. On obtaining permission, necessary bond has to be executed undertaking to observe all regulations and maintaining accounts etc. Manufacture will not be under supervision of Customs Officers. However, customs officers can visit warehouse and control and supervise manufacturing process or imported and other goods. Detailed accounts are required to be maintained of raw materials, stock, WIP and production. Input-output norms should be fixed wherever considered necessary.

Manufacturer can suspend or discontinue manufacture with one month notice. Sanction for manufacture in warehouse can be withdrawn if conditions of Act or regulations are violated.

Procedures have been prescribed under Central Excise Law for bringing goods manufactured in India without payment of excise duty.

Special audit of accounts of the warehouse can be ordered by Principal Chief Commissioner or Chief Commissioner of Customs. He can appoint a cost accountant to conduct audit of accounts of warehouse, office, stores, godowns, factory, depot of the manufacturer. This provision has been made in July 1998, as physical control of customs officer has been removed.

(c) Goods manufactured in bonded warehouse are not made in India and are liable to customs duty? - In Mustan Teherbhai v. CC2003 (154) ELT 472 (CEGAT), it has been held that customs duty is payable on goods manufactured in customs bonded warehouse. Thus, goods manufactured in customs bonded warehouse are not 'made in India'. The reason given is that section 66 of Customs Act makes mention of 'rate of duty leviable on goods manufactured'. Such duty can only be customs duty.

(5) Clearance from bonded warehouse

Section 71 allows clearance for (a) home consumption, (b) re-exportation or (c) removal to another warehouse.

(a) Removal for home consumption

Under section 68, goods stored in warehouse can be removed on payment of duty. Procedure is summarised in Chapter 9 Para 19 of Customs Manual, 2011.

(b) Procedure for removal of goods - Importer has to submit bill of entry in prescribed form for removal of goods from warehouse for home consumption, this Bill of Entry is called 'Into Bond Bill of Entry' as bond is executed for transfer of goods in warehouse without payment of duty. The Bill of Entry is assessed by customs officer in charge of warehouse. Duty, penalties, rent and interest is payable as per rules. Goods are then allowed to be cleared by Customs Officer.

(c) No interest if duty not paid within 2 days on return of Bill of Entry - The provision for payment of duty within 2 working days after return of Bill of entry, as provided in section 47(2) of Customs Act applies to clearance from customs port and not to clearance from customs warehouse. Thus, no interest is payable so long as clearance is made within period allowable for interest free warehousing - CC v. Acalmar Oils (2009) 240 ELT 440 (CESTAT).

(d) Rate of duty as applicable on date of removal - As per section 15(l)(fc), rate of duty as prevalent on date of presentation of Bill of Entry for home consumption for clearance from warehouse is applicable and not rate prevalent when goods were removed from customs port.

(e) Rate of exchange in case of warehoused goods - Relevant exchange rate for valuation is as in force on date on which bill of entry is presented u/s 46. Bill of Entry is presented u/s 46 of Customs Act either for home consumption or for warehousing. Hence, in case of warehoused goods, exchange rate prevailing on the date on which Bill of Entry is presented u/s 46 and not when Bill of Entry is presented u/s 68 for clearance from customs warehouse.

(f) No Anti dumping duty on goods warehoused prior to levy of anti-dumping duty - Antidumping duty is leviable on date of importation. Hence, if goods are already warehoused prior to imposition of anti-dumping duty, anti-dumping duty will not be leviable on warehoused goods, even if cleared subsequent to imposition of anti-dumping duty. Section 15(1)(b) of Customs Act does not apply to anti-dumping duty u/s 9A of Customs Tariff Act. - CCv. Suja Rubber Industries 2002(142) ELT 586 (CEGAT).

Same principle will apply to protective duty and safeguard duty also.

(g) Duty payable only on quantity cleared from warehouse - In Mangalore Refinery v. CCE 2002(141) ELT 247 (CEGAT), it was held that taxable event is when goods are cleared from warehouse. Hence, customs duty is payable only on the quantity which is cleared from warehouse and not the quantity which had entered the territorial waters.

(h) Duty payable if warehousing period is not extended - Goods which are not removed within the permissible period, are deemed to be improperly removed on the day it should have been removed. Thus, duty applicable on such date (i.e. last date on which the goods should have been removed) is applicable, and not the date on which goods were actually removed.

Sometimes, goods are not cleared even after warehousing period is over and extension has not been obtained or granted. In such cases, the relevant date for determination of rate of duty is as follows - (a) If importer does not remove the goods even after expiry of warehousing period, customs officer can issue notice u/s 72 demanding duty. In such case, the last date on which goods should have been removed is 'deemed date of removal' and duty applicable on that date is payable, (b) If importer submits bill of entry and obtains clearance u/s 68, the relevant date is the date on which Bill of Entry for home consumption is submitted u/s 68 (That time it was date of payment of duty) - Raymond Synthetics Ltd. v. CC 2000(119) ELT 205 (CEGAT 5 member bench). - civil appeal admitted by SC on 3.9.2001 - (2001) 134 ELT A166.

(i) Title can be relinquished even after warehousing period is over - In RPG Cables v. CC (2007) 212 ELT 538 (CESTAT), it was held that importer can relinquish title even after warehousing period is over, since title can be relinquished anytime before clearance for home consumption - same view in Macmillan Indiav. CC(2008) 223 ELT 449 (CESTAT) - same view in JK Cement Works v. CCE (2008) 223 ELT 138 (Raj HC DB), where it was also held that even after relinquishment, rent, interest etc. is required to be paid. It was also held that acceptance of option of relinquishment is not subject to discretion of proper officer, but only for fulfilment of conditions prescribed in proviso to section 68 of Customs Act.

(j) Interest if goods cleared after warehousing period is over - Interest is payable even if goods are cleared after warehousing period is over, till date of clearance. Interest is payable even if notice demanding interest is not issued - Suresh Chand v. t/O/(2010) 254 ELT (Bom HC DB).

(k) Re-export can be permitted even after bonding period has expired - Importer may be allowed to re-export goods even after the period of warehousing has expired and demand notice is issued. Before granting the permission, warehousing period should be extended, so that importer can re-export the goods within such extended warehousing period.

(l) Interest not payable even if duty paid after five days from return of ex-bond bill of entry -As per section 47(2) of Customs Act, if duty is not paid within five working days from date of return of Bill of Entry to importer. This section is applicable for clearance from port and not for clearance from warehouse, for which separate provisions have been made under section 68 of Customs Act. This is self contained provision. Hence, in case of warehoused goods, interest is not payable even if duty is paid beyond period of five days from return of ex-bond bill of entry. However, interest as provided in section 61 (2) would be payable - MF(DR) Circular No. 15/2009-Cus dated 12-5-2009.

(m) Sales Tax and octroi/entry tax on warehoused goods - Sales tax is payable when goods are sold from bonded warehouse. State sales tax is also payable when goods are supplied to foreign going vessel. However, sales tax should not be payable in following - (A) Goods exported from bonded warehouse (B) Goods sold by transfer of documents when goods are within the bonded warehouse.

Octroi/Entry Tax can be levied on warehoused goods for which 'Value' can include customs duty payable on such goods, even if not paid at the time of warehousing. However, in case of EOU/SEZ, since they do not have to pay customs duty, the custom duty will not be includible in value for purpose of octroi payment.

(n) Sale of goods when goods are in bonded warehouse is 'sale in the course of import'

In Kiran Spinning Mills v. CC1999(U3)ELT753 =2000 AIRSCW2090 = AIR2000 SC 3448 (SC 3 member bench), it has been held that goods continue to be in customs barrier when they are in customs bonded warehouse. Import would be completed only when goods cross customs barrier and not when they land in India or enter territorial waters.

Thus, if documents are transferred when goods are in customs bonded warehouse, it will be treated as transfer of documents before goods cross customs barrier.

(o) Transfer to other bonded warehouse

Section 67 of Customs Act permit removal to other warehouse under bond. Transit bond for customs duty involved backed by bank guarantee/security should be furnished. In the case of EOU, bank guarantee for transfer of goods is not required -Chapter 9 Para 18 of CBE&C's Customs Manual, 2011.

In case of inter-city transfer of goods from one warehouse to another warehouse, bank guarantee is not required in case of Central and State Public Sector Undertakings (PSU). However, transit bond should be executed - MF(DR) circular No. 42/2007-Cus dated 30-11-2007.

(p) Clearance for export

Customs warehoused goods can be exported without payment of duty, vide section 69(1) of Customs Act. A shipping bill or bill of export or label or declaration (in case of export by post) has to be presented. Export duty, penalties, rent, interest etc. is payable as applicable and then goods are allowed to be exported.

If warehoused goods are re-exported without payment of duty, no interest is payable -MF(DR) circular No. 38/2005-Cus dated 28-9-2005.

(6) Other provisions of customs warehousing

Other provisions in respect of warehousing are as follows.

(a) Relinquishing of title after warehousing - The owner of warehoused goods can relinquish the title of goods any time before order for home clearance is made. He will be required to pay rent, interest, other charges and penalties that may be payable, but duty will not be payable [proviso to section 68 inserted w.e.f. 14-5-2003]. The word 'interest' is not clear and is likely to lead to litigation. It has been consistently held that when duty is not payable, question of payment of duty does not arise.

Relinquishment of title of goods will not be permissible if offence appears to have been committed in respect of such goods under Customs Act or any other law [second proviso to section 68 of Customs Act inserted w.e.f. 18-4-2006].

(b) Repurchase of goods after relinquishing - The goods relinquished are normally auctioned. In that case, the person who has relinquished the goods can repurchase the goods as the goods are no more 'imported goods' - Aabhas Spinners v. UOI(20\0) 260 ELT 554 **(P&H HC DB).**

(c) Remission of duty permissible - If goods are damaged in warehouse, the damage is covered u/s 23 and hence no duty is payable, since clearance from port to the warehouse is not 'clearance for home consumption'.

(d) Remission if Loss of inputs in stores or during process of EOU - If inputs are lost due to fire, after they are issued for production and are is in 'work in progress', no duty is payable on imported and indigenous inputs received duty free. Remission of duty is required to be granted - Sarni Labs v. CC(2007) 216 ELT 59 (CESTAT).

Remission can be obtained by EOU if goods deteriorated when in the factory (as it is a warehouse) - Sandoz P Ltd. v. CCE (2012) 278 ELT 259 (CESTAT) * CC v. Next Fashion Creators (2012) 280 ELT 374 (Karn HC DB).

(e) No remission after warehousing period is over - In CCE v. Decorative Laminates (2010) 257 ELT 61 (Kar HC DB), it was held that remission cannot be granted after expiry of warehousing period [reversing Decorative Laminates v. CC (2006) 195 ELT 175 (CESTAT), where it was held that application for remission can be made even after expiry of warehousing period but before clearance from warehouse for home consumption.

(f) Control over bonded warehouse - The warehouse is subject to control of Customs Officer, who has powers to enter warehouse and examine the goods.

(g) Transfer to another person - Goods in warehouse can be transferred to another person u/s 59(3). Sale of warehoused goods to holder of duty concession license is also permissible.

(h) Rent and warehouse charges - Rent and warehouse charges are payable by importer. If not paid, the warehouse keeper can sell the goods after giving notice to importer and with permission of Customs Officer (section 63).

(i) Owner's rights to deal in goods in warehouse - With the permission of Customs Officer and on payment of prescribed fees, owner can deal with warehoused goods as follows (A) inspect the goods (B) separate damaged or deteriorated goods (C) sort the goods or change containers for preservation, sale, export or disposal of goods (D) show the goods for sale (E) take samples of goods - the samples can be removed without payment of duty with permission of Customs Officer, but if these are not brought back, customs duty is payable (section 64).

(j) No remission if there is theft in warehouse - Remission cannot be granted if there was theft in warehouse - Maneesh Exports (EOU), In re (2011) 273 ELT 466 (GOI).

Goods not accounted for - If goods are removed in contravention of rules or if goods are not properly accounted for, full duty is payable on such goods together with penalty, interest, rent etc. If duty, penalty etc. is not paid, goods in warehouse can be sold by Customs Officer after giving notice to importer. Besides, bond or bank guarantee executed by importer can be encashed [section 72(1)(d)].

(k) Goods improperly removed from warehouse

As per section 72(1), following goods are 'goods improperly removed from warehouse, etc'

(a) Warehoused goods removed in contravention of provisions of section 71 are goods improperly removed [section 72(1)(a)]. [Section 71 allows clearance for home consumption on payment of duty, re-exportation or removal to another warehouse].

(b) Warehoused goods not removed at the expiration of warehousing period as specified in section 61 (unless extension is obtained)

(c) Taking samples from warehouse without payment of duty and not returning them

(d) Goods entered into warehousing under bond u/s 59 are not duly accounted for [section 72(1)(d)].

In such case, full duty, along with interest, penalty, rent and other charges can be demanded. If these are not paid, the warehoused goods can be sold by customs officer, besides other action that can be taken under customs law [section 72(2)].

(l) Reassessment cannot be made at warehouse

The department has clarified as follows - 'Insofar as value for assessment of duty is concerned, it is not required to be re-determined and it is the original value as determined at the time of filing of 'Into Bond Bill of Entry' and assessments before warehousing. - Chapter 9 Para 19.3 of CBE&C's Customs Manual, 2001.

(7) Storage in warehouse pending clearance

Normally, imported goods are kept in customs bonded warehouse after goods are assessed to duty. However, occasionally, it may happen that assessment of duty may take time for want of some clarification/reports etc. In such cases, goods lying in docks may incur heavy demurrage. There is a provision that Customs department can issue 'detention certificate' and on the basis of such certificate, port trust authorities may remit demurrage. However, chances of pilferage or loss are high if goods lie at docks.

Hence, if assessment is likely to be delayed, section 49 of Customs Act allows that goods can be stored in public warehouse for period upto 30 days. However, such goods are not to be treated as 'warehoused goods' for purposes of Customs Act as the goods are not assessed. Hence, it is called 'storage without warehousing' or 'warehousing without warehousing'. The goods are cleared from the warehouse after duty is assessed and paid [The limit of 30 days was put w.e.f. 10th May, 2013]

The storage period is 30 days. The period can be extended by Principal Commissioner or Commissioner of Customs by 30 days at a time - [proviso to section 49 of Customs Act, inserted w.e.f. 10th May, 2013].

PRACTICAL PROBLEMS

Example 24: An importer imported some goods in February, 2016 and the goods were cleared from Mumbai port for warehousing on 8th February, 2016 after assessment. Assessable value was ₹ 4,86,000 (US $ 10,000 at the rate of exchange ₹ 48.60 per US $). The rate of duty on that date was 20% (assume that no additional duty is payable). The goods were warehoused at Pune and were cleared from Pune warehouse on 4th March, 2016, when rate of duty was 15% and exchange rate was ₹ 48.75 = 1 US $. What is the duty payable while removing the goods from Pune on 4th March, 2016?

Answer: **Amount in ₹**

The rate of exchange will be ₹ 48.60 per USD Assessable value	4, 86,000
(i.e. US$ 10,000 at ₹ 48.60 per US$) Rate of duty	@15%.
Basic Customs Duty payable	72,900
Education Cess 2% on ₹ 72,900	1,458
SAH @1% on ₹ 72,900	729
Total Duty payable	75,087

Example 25: Certain goods were imported in February 2015. "Into bond" bill of entry was presented on 14th February, 2015 and goods were cleared from the port for warehousing. Assessable value was $5,00,000. Customs officer issued the order under section 60 permitting the deposit of the goods in warehouse on 21st February, 2015 for 3 months. Goods were not cleared even after warehousing period was over, *i.e.*, 21st May, 2015 and extension of time was also not obtained. Customs officer issued notice under section 72 demanding duty and other charges. Goods were cleared by importer on 28th June, 2015. What is the amount of duty payable while removing the goods? Compute on the basis of following information (assume that no additional duty or special additional duty payable).

	14.02.2015	21.05.2015	28.06.2015
Rate of Exchange per USD	₹ 48.30	₹ 48.40	₹ 48.50
Basic customs duty	35%	30%	25%

Answer:

Rate of duty applicable	@30%
Exchange rate	₹ 48.30
Assessable value	₹ 2,41,50,000
Customs Duty @30% x ₹ 2,41,50,000	₹ 72,45,000
Education cess 2% x ₹ 72, 45,000	₹ 1,44,900
SAH @ 1% x ₹ 72, 45,000	₹ 72,450
Total Customs duty payable	₹ 74,62,350

Note: Goods not removed from the warehouse within the permissible period, is considered as deemed to be removed *improperly* on the due date, even though, the goods actually removed at a later date. The rate of duty prevailing on the date on which the goods should have been removed is to be considered *i.e.* 30% (21-5-2015) *[Kesoram Rayon* v *Commissioner of Customs* (1996)]

Example 26: An importer imported some goods on 1st January, 2015 and the goods were cleared from Mumbai port for warehousing on 8th January, 2015 by submitting Bill of Entry, exchange rate was ₹ 50 per US $. FOB value US $ 10,000. The rate of duty on 8th January, 2015 was 20%. The goods were warehoused at Pune and were cleared from Pune warehouse on 31st May, 2015, when rate of basic customs duty was 15% and exchange rate was ₹ 48.75 per 1 US $. What is the duty payable while removing the goods from Pune on 31st May, 2015? CVD @10% and Special CVD 4% are applicable.

You are required to find:

(a) The total Customs duty payable?

(b) The interest if any payable?

Answer:

	(US $)
FOB	10,000
ADD: 20% Freight on FOB	2,000
ADD: 1.125% Insurance on FOB	112.50
CIF	12,112.50
ADD: 1% on CIF	121.13
ASSESSABLE VALUE	12,233.63

	(₹)	
ASSESSABLE VALUE	6,11,681.50	(i.e. 12,233.63 x ₹50)
Add: BCD 15%	91,752.23	(I.e. 6,11,681.50 x 15%)
Balance	7,03,433.73	
Add: CVD 10%	70,343.37	(i.e. 703,433.73 x 10%)
Balance	7,73,777.10	
Add: 2% Ed. Cess	3,241.91	(i.e. 1,62,095.60 x 2%)
Add: 1%SAH Ed. Cess	1,620.96	(i.e. 1,62,095.60 x 1%)
Balance	7,78,639.97	
Add: Spl. CVD 4%	31,145.60	(i.e. 7,78,639.97 x 4%)
Value of import	8,09,785.57	
Amount of Customs duties	1,98,104.07	or 1,98,104

Interest:

(i.e. ₹1,98,104 x 15% x 54/365) 4,396.28

Jan 24 days + Feb 28 days + Mar 31 + April 30 days + May 31 days = 144 days

144 days –90 days = 54 days.

4.16 PROVISIONAL ASSESSMENT OF DUTY (SECTION 18)

Provisional assessment [Section 18]: The provisional assessment can be directed by proper officer in the following circumstances,-

(a) where the importer or exporter is unable to make self-assessment under section 17(1) and makes a request in writing to the proper officer for assessment; or

(b) where the proper officer deems it necessary to subject any imported goods or export goods to any chemical or other test; or

(c) where the importer or exporter has produced all the necessary documents and furnished full information but the proper officer deems it necessary to make further enquiry; or

(d) where necessary documents have not been produced or information has not been furnished and the proper officer deems it necessary to make further enquiry.

- **Furnishing of security**: The proper officer may direct provisional assessment if the importer or the exporter, as the case may be, furnishes such security as the proper officer deems fit for the payment of the deficiency, if any, between the duty as may be finally assessed or re-assessed (as the case may be), and the duty provisionally assessed.

- **Importer required to file bill of entry in case of provisional assessment also**: The provisions of section 18 apply without prejudice to the provisions of Section 46. Hence, the bill of entry is required to be presented in accordance with the provisions of Section 46 even for the purposes of provisional assessment as well.

- **Finalisation of assessment**: When the duty leviable on such goods is assessed finally or re-assessed by the proper officer in accordance with the provisions of this Act, then -

  (a) If the goods are cleared for home consumption or exportation, the amount paid shall be adjusted against the duty finally assessed or re-assessed. In case the amount so paid falls short or is in excess of duty finally assessed or re-assessed, the importer or the exporter of the goods shall pay the deficiency or is entitled to a refund.

  (b) If the goods are warehoused and the duty finally assessed or re-assessed is in excess of the provisional duty, the customs officer may require the importer to execute a bond binding himself in a sum equal to twice the amount of the excess duty.

- **Interest of demand**: The importer or exporter shall be liable to pay interest, on any amount payable to Central Government, consequent to the final assessment order or reassessment order, at the rate specified in Section 28AA of the Customs Act, 1962 (i.e. @ 18% p.a.) from the first day of the month in which the duty is provisionally assessed till the date of payment thereof.

- **Interest on delayed refund:** If any amount refundable is not refunded within three months from the date of assessment of duty finally or reassessment of duty, as the case may be, there shall be paid an interest on such amount at the rate specified in section 27A of the customs Act, 1962 (i.e @6% p.a) till the fund of refund of such amount.

- **Circumstances under which refund can be granted:** The amount of duty and the interest shall be credited to Customer Welfare Fund. However, instead of being credited to Consumer Welfare Fund in the following cases it shall be paid to the importer or the exporter, if such amount is related to,-

  (a) the duty and interest, (if any, paid on such duty) paid by the importer, or the exporter, as the case may be, if he had not passed on the incidence of such duty and interest, to any other person;

  (b) duty and interest (If any, paid on such duty) on imports made by an individual for his personal use;

  (c) the duty and interest (if any, paid on such duty) borne by the buyer, if he had not passed on the incidence of such duty and interest, to any other person;

  (d) the export duty as specified in section 26;

  (e) drawback of duty payable under section 74 and 75.

4.17 BAGGAGE, COURIER AND IMPORT AND EXPORT THROUGH POST

4.17.1 General Provisions about Baggage

Section 2(3) states that baggage includes 'un-accompanied baggage' but does not include motor vehicles. Thus, baggage rules are also applicable in respect of baggage which comes separately and which is despatched from abroad before or after the traveller's departure. Section 79(1)(b) of Customs Act exempts bona fide baggage of passenger which is for use of the passenger or his family. Section 79(2) authorises Central Government to frame rules for prescribing conditions for granting exemption to baggage. In exercise of these powers, Central Government has issued Baggage Rules, 1998, making provisions in respect of baggage.

Baggage - The term has not been defined as such. However, following may be noted: (a) Baggage means all dutiable articles, imported by passenger or a member of a crew in his baggage (b) Un-accompanied baggage, if despatched previously or subsequently within prescribed period is also covered (c) baggage does not include motor vehicles, alcoholic drinks and goods imported through courier (d) Baggage does not include articles imported under an import licence for his own use or on behalf of others.

Bona fide Baggage Exempt from duty - Bona fide baggage accompanying passenger is exempt from duty. It includes wearing apparel, toilet requisites and other personal effects.

General prohibitions - Following are general prohibitions/restrictions - (a) Foreign and Indian currency can be taken out/ brought in only as per restrictions of RBI under FEMA (discussed later in this chapter). (b) Possession of narcotic drugs is strictly prohibited. (c) Domestic pets like dogs, cats, birds etc. can be brought as per strict health certificate regulations. (d) Taking out exotic birds, wind orchids and wild life, is strictly prohibited. (e) Endangered species or articles made from flora and fauna such as ivory, musk, reptile skins, furs, shahtoosh or antiques are prohibited.

Declaration by owner of baggage

Section 77 of Customs Act provides that owner of any baggage has to make declaration of its contents to Customs Officer. Rate of duty and tariff valuation shall be the rate and valuation in force on the date of declaration.

Green Channel - It is impractical to ask every traveller to declare contents of his baggage. Hence, customs have provided two channels at airports. If a person does not have any dutiable goods, he can go through green channel.

An incoming passenger has to submit disembarkation card, containing written declaration about his baggage. This should be collected when passenger goes through green channel. - MF(DR) circular No. 9/2001-Cus dated 22.2.2001.

Passenger who has nothing to declare can simply walk through green channel with baggage on basis of oral declaration/declaration on their disembarkation cards. Any passenger found walking through green channel with dutiable or prohibited goods (or found mis-declaring quantity, value or description while going through red channel) is liable to strict penal action of seizure and confiscation. He can even be arrested/ prosecuted.

Mere declaration does not absolve the passenger - Mere voluntary disclosure of goods to customs authorities does not preclude the authorities from adjudicating upon the nature of imports and whether the passenger is entitled to clear goods without payment of duty and without any licence - Goods can be confiscated if found that licence is required to import the goods in question - R Karuppan v. B Namachivayam 1998(99) ELT 214 (Mad HC DB).

Red Channel - Person carrying dutiable goods should pass through red channel and should submit declaration. The declaration of goods and value as given by passenger in disembarkation card is generally accepted, but baggage can be inspected by Customs Officer.

4.17.2 Rate of customs duty on baggage

Rate of duty on baggage is as follows:

General Rate on baggage - Baggage is classified in Customs Tariff in Chapter 9803, irrespective of actual classification as per Customs Tariff. The entry reads as "All dutiable articles, imported by passenger or member of crew in his baggage". Tariff rate is 100%. However, effective rate (i.e. specified by a notification) is 35% w,e.f. 1-3-2005. Baggage is exempt from CVD. However, education cess @ 2% and SAH education cess of 1% is payable. Thus, total customs duty on baggage is 36.05%,

This rate is not available to - fire arms, cartridge of fire arms exceeding 50, cigarettes, cigars or tobacco in excess of the quantity prescribed for importation free of duty under Baggage Rules and goods imported through courier service. [Notification No. 136/90 dated 20-3-90 as amended]. Since 'baggage' does not include motor vehicles, liquor and firearms, the rate is obviously not applicable for those goods.

Exemption to laptop computer - Laptop computer (notebook computer) brought as baggage by person over 18 years of age (other than member of crew) is fully exempt from customs duty - Notification No. 1 1/2004-Cus dated 8-1-2004.

A laptop is a small portable Personal Computer (in short 'PC'). A notebook computer is a laptop - CC v. Hewlett Packard India (Sales) P Ltd. (2007) 215 ELT 484 (SC).

Import for personal use - Dutiable articles imported by air or post, but not as baggage, intended for personal use, which are not prohibited under Foreign Trade (Development and Regulation) Act are classifiable under 9804 and general rate is 20%. The goods are exempt from additional duty (CVD). However, 9804 does not cover items brought as baggage. Thus, this covers goods sent by post or air by a person abroad to another person in India.

Relevant date for determining rate of duty and valuation - As per section 78 of Customs Act, 'relevant date' for rate of duty and baggage is date on which declaration is made in respect of baggage as required u/s 77 of Customs Act.

Valuation of baggage

In Naresh Lokumal Serai v. CC 2006 (203) ELT 580 (CESTAT), it was held that there are no separate provisions for valuation of baggage. Hence, valuation rules apply to valuation of baggage also. In baggage, most of items may be used. Hence, valuation on basis of best judgment assessment is appropriate. It was also held that valuation on basis of internet prices cannot be considered for valuation. Similarly, price tags on goods cannot be considered for valuation, since the price indicated is for sale within that country and not for export to India.

4.17.3 Exemptions/ Restrictions on Baggage

Tourists can be broadly classified as (a) Indian persons going abroad for a short trip and coming back (b) Indian persons gone abroad for work and coming back after few years (c) tourists visiting India for sight seeing or business purpose. Accordingly, 'Baggage Rules, 1998' contain different provisions for (a) Residents from India (b) Tourists visiting India and (c) Persons transferring their residence.

Exemption only to bona fide baggage - As per section 79(1) of Customs Act, bona fide baggage will be passed free of customs duty. Section 79(1) of Customs Act provides that (a) article in any baggage of passenger or crew will be allowed if it was in use for a period specified in rules and (b) bona fide gifts within the limits prescribed in rules.

Present Baggage Rules do not prescribe any limit for which the articles in baggage should be 'in use', but unused articles may not be held as 'bona fide' baggage.

Baggage declaration form prescribed that 'bona fide baggage' includes - * wearing apparel * personal and household effects meant for personal use of passenger or family members travelling with him and not for sale or gift * Jewellery including articles made wholly or mainly of gold, in reasonable quantity according to status of passenger ' Tools of draftsman * Instruments of physician or surgeon.

Personal effects

The term 'personal effects' has not been defined. Rule 11 of earlier baggage rules stated that the expression 'personal effects' means all clothings and other articles, new or used, which a tourist may personally and reasonably require taking into account all the circumstances of his visit but excluding all merchandise imported for commercial purpose.

Departmental clarification - Following will be covered in 'personal effects'. Only used personal effects are permitted. However, as long as it is not prima facie new goods in their original packings which can be disposed of off hand, it will be permitted. The list as given in MF(DR) circular No. 72/98-Cus dated 24-9-1998 is as follows

- Personal jewellery
- One camera with film-rolls not exceeding 20
- One video camera/camcorder with accessories and with video cassettes not exceeding 12
- One pair of binoculars
- One portable colour TV (not exceeding 15 cms in size)
- One music system including compact disc player
- One portable typewriter
- One perambulator
- One tent and other camping equipment
- One computer (laptop/note book) [Laptop/note book computer has been exempted from customs duty vide notification No. 11 /2004-Cus dated 8-1-2004]
- One electronic diary
- One portable wireless receiving set (transistor radio)
- Professional equipments, instruments and apparatus of appliances including professional audio/ video equipments
- Sports equipments such as one fishing outfit, one sporting firearm with 50 cartridges, one non-powered bicycles, one canoe or ranges less than 51 metres long, one pair of skids, two tennis rackets, one golf set (14 pieces with a dozen of golf balls)
- One cell phone

Bona fide luggage will not include - `Alcoholic liquor exceeding half pint * Perfumed spirit exceeding two ounces in open or unopened bottles' cigars or cheroots exceeding 50 ` Country bidis exceeding 200 " Un-manufactured or manufactured tobacco exceeding 4 ounces and snuff exceeding 10 tolas `Piano, pianola and radio * Carriage, motor car, motor cycle * Refrigerator' Cotton piece goods or textile materials in long lengths "Arms and ammunition except personal licensed gun, rifles, revolver or pistol' Wireless apparatus and dictaphone.

Since 'baggage' does not include motor vehicles, liquor and firearms, these cannot be considered as 'personal effects'.

Baggage fully exempt or at concessional rate of duty - Following baggage is fully exempt from customs duty, as per Notification No. 49/96-Cus dated 23-7-1996

(a) Personal property re-imported

(b) Free replacement under warranty of articles which are private personal property of passenger

(c) foodstuff upto ₹ 50,000

(d) Free gifts and donations to red cross, CARE or Government of India for relief and rehabilitation

(e) Samples, price lists, prototypes, commercial samples etc.

(f) Goods brought for display, exhibition, fair etc., subject to various conditions.

(g) Agricultural products or goods manufactured or produced in Nepal.

(h) Newspapers, drawing and designs and other goods as specified.

Exemption to minor amounts of customs duty - Customs duty is not payable if amount of duty is Equal to or less than ₹ 100. [Section 25(6)].

Export Certificate - If a person had gone abroad from India, he should take 'Export Certificate' while taking out jewellery, camera etc. Otherwise, customs duty will be leviable while bringing back the goods.

Goods cannot be imported in commercial quantity as 'Baggage'?

Import of consumer goods in commercial quantity is not permissible as per Foreign Trade policy and it cannot be treated as 'bona fide baggage. However, if passenger brings other goods also, that portion which is not in commercial quantity would be eligible to free baggage allowance. Only goods brought in commercial quantity will be liable for adjudication, penalty and confiscation.

4.17.4 Baggage of Indian resident or foreigner residing in India

Resident means a person holding Indian Passport and normally residing in India (i.e. Indian persons going abroad for short visit). The concession of free import of used personal effects and General Free Allowance is also available for foreign citizens residing in India.

Exempted baggage- Baggage Rules, 1998 allow following imports as duty free:

Used personal effects - Used articles of personal wear and articles in personal use of passengers for daily necessaries is fully exempt. Used personal effects are also exempt. (This allowance is also available to foreign citizens residing in India returning from abroad).

General Free Allowance

The free allowance as provided in Baggage Rules, 1998 is as follows:

General Free Allowance - In addition to personal effects (excluding jewellery) and a laptop computer, a passenger of 10 or more years of age is allowed general free allowance of ₹ 45,000, if the Indian Resident is returning from country other than Nepal, Bhutan, Myanmar or China [Hong Kong Special Administrative Region (HKSAR) is separate customs territory from China and hence allowance of ₹45,000 will be applicable to persons coming from Hong Kong - MF(DR) circular No. 25/2010-Cus dated 4-8-2010]

This allowance is also available to foreign citizens residing in India, after stay of more than three days. This allowance cannot be pooled with General Free Allowance of other passengers - e.g. husband and wife bringing one item of ₹90,000 will not be permitted duty free. This General Free Allowance is not applicable to un-accompanied baggage.

The limit of ₹45,000 is reduced as follows - (a) ₹17,500 for passengers after stay abroad of three days or less (This limit was ₹15,000 upto 10-7-2014). (b) If the passenger is upto 10 years of age and is returning from country other than Nepal, Bhutan, Myanmar or China (but not in case of Hong Kong), the allowance is ₹17,500, if a person is returning after stay of more than 3 days and ₹3,000, if his stay was

3 days or less. (c) If the passenger is returning from Pakistan by land route, as specified in Annexure IV of Baggage Rules, the general free allowance is ₹6,000 for passengers above 10 years and ₹1,500 for passengers upto 10 years of age.

Lower General Free allowance in case of certain countries - An Indian Resident or foreigner residing in India of age 10 or more is entitled to lower rate of General Free Allowance of ₹ 6,000, if he is returning from Nepal, Bhutan, Myanmar or China after stay of more than 3 days, by route other than land route. Passenger upto 10 years returning from these countries after stay of more than 3 days is entitled to General Free Allowance of ₹1500. There is no duty on personal effects. There is no general free allowance if a person is returning from these countries after stay of three days or less. There is no free allowance if passenger returns by land route from these countries, even if his stay abroad was more than 3 days. If the passenger is returning from Pakistan by land route as specified in Annexure IV of Baggage Rules, the general free allowance is ₹6000 for passengers above 10 years and ₹1500 for passengers upto 10 years of age.

No General Free allowance in certain cases - General Free Allowance is available to Indian Residents, foreigners who are residing in India and tourists of Indian origin. The allowance is also available if he is transferring his residence or returning after 3/12/24 months. A Non Resident Indian who does not hold Indian passport is also entitled to GFA if he is of Indian origin. The GFA is not available to foreign tourists.

No GFA on un-accompanied baggage - General Free Allowance is not allowed on unaccompanied baggage.

Restricted/Excluded items from General Free Allowance - The exemption is not allowed to items included in Annex Ito Baggage Rules, 1998. Items included in Annex I are : (1) fire arms; (2) cartridges of fire arms exceeding 50; (3) cigarettes exceeding 100 or cigars exceeding 25 or tobacco exceeding 125 Gms; (Alcoholic liquor or wines in excess of two liters (S) Gold or Silver in any form, other than ornaments.

Allowance to professionals returning to India

An Indian passenger who was engaged in his profession abroad for at least three months is allowed to import following duty free goods as additional allowance - (a) Used Household Articles upto ₹12,000 (e.g. linen, utensils, tableware, kitchen appliances, an iron etc.) (b) Professional equipment like portable equipments, apparatus and appliances required in such profession, upto ₹20,000. The limit will be increased to ₹40,000, if he was abroad for over 6 months. [This allowance is in addition to General Free Allowance].

This exemption of professional equipment is only for carpenters, plumbers, welders, masons and the like and not for items of common use like cameras, typewriter, cassette-recorder, computers, word processor etc. - Rule 5 of Baggage Rules, 1998 read with Appendix C.

Limited exemption to jewellery

Bringing jewellery duty free on transfer of residence - If the passenger was residing abroad for over one year, jewellery can be imported duty free upto ₹50,000 in case of gentleman passenger and ₹1,00,000 in case of lady passenger. [Appendix D to Baggage Rules, 1998].

Imported goods taken abroad and brought back

A tourist can take imported equipment like camera, cellular phone, note book computers etc. abroad. In such case, he should take 'Export Certificate' with him while going abroad. This will enable him to bring back the said goods without payment of duty on return. It is now provided that frequent travellers can get such certificate in advance. The certificate will be serially numbered with official seal of issuing authority giving details of the product. Such certificate will be valid for one year and can be obtained from any major customs house, international airport or seaport. - CBE&C circular No 66/96-Cus dated 26.12.1996.

Duty payable on balance un-exempted baggage - The baggage (including unaccompanied baggage) is exempt subject to limits mentioned above. The balance quantity is dutiable at rates explained above. Duty payable on Silver and Gold imported as baggage has been separately prescribed.

4.17.5 Concession to persons transferring his residence (TR)

A person who is transferring his residence to India is eligible to bring used personal and household articles to India without duty. The provisions are applicable to all - i.e. foreigners coming for residing in India as well as Indian resident coming after 2 years and who is transferring his residence to India.

Conditions for TR concession - The conditions for TR concession are:

(a) He should have been residing abroad for at least two years. During this period short visits not exceeding 6 months are permissible.

(b) The provision regarding 2 years' stay can be condoned upto 2 months by Assistant Commissioner, if the early return was due to terminal leave or vacation or other special circumstances.

(c) The provision regarding maximum 6 months stay during 2 years can be relaxed by Principal Commissioner or Commissioner in deserving cases.

(d) The passenger should not have availed this concession in preceding three years. (e) Goods in Annexure I and Annexure II are not allowed under this concession.

(e) Goods in Annexure III are fully exempt from customs duty, if within limit of ₹ five lakhs.

(f) Jewellery upto ₹50,000 for male passenger and ₹1,00,000 for female passenger can be imported free of customs duty. (Rule 8 of Baggage Rules, 1998, read with Appendix F).

Since 'baggage' does not include motor vehicles, liquor and firearms, the exemption is obviously not applicable for those goods.

Firearms cannot be imported as baggage without a license which is required under Arms Act, 1959 - Anirudh Singh Katochi v. U012O11 (266) ELT 321 (SC).

Limit on bringing jewellery duty free - The jewellery allowed to be imported duty free is limited to ₹50,000 for male passenger and ₹1,00,000 for female passenger. This limit is not applicable if the passenger produces evidence that the jewellery was, in fact, taken out of India by the passenger or his family.

New and unused goods not eligible for TR concession - New and unused goods are not eligible for transfer of residence benefit - Naresh Lokurnal Serai v. CC2OO6 (203) ELT 580 (CESTAT).

General Free Allowance - A passenger can also avail of 'General Free Allowance' as available to other residents, in addition to above. (Rule 8).

Condonation of shortfall in periods - While calculating the aforesaid period of two years (a) short visits to India totalling not more than six months during the period are ignored. This period can be extended by Principal Commissioner or Commissioner of Customs. (b) Minimum stay abroad of two years can be condoned upto two months by Assistant Commissioner if the early return is caused by his availing terminal leave or vacation or by special circumstances.

Personal and Household goods - The exemption is available only for 'personal and household goods' i.e. those required for use of the passenger or running the household.

Goods need not have been owned by the person? - The goods should be in possession of the person before he left for India. Ownership of goods is not the criteria for determining eligibility to TR concession - CCE v. Hameed Kunhipally Hussainar 2005 (187) ELT 502 (CESTAT) [If he is not owner, how goods will be in his possession?].

Concession for transfer of residence

A person transferring his residence to India after stay abroad for two years and who has not availed this concession in preceding three years is eligible for concession upto value of ₹5 lakhs exclusive of value of his personal effects and other household articles. This concession is available on all articles contained in Annex II and Annex III of Baggage Rules, 1998. [As against only ₹ 75,000 in case of Mini TR - inclusive of personal effects and other household articles - available to those who are coming after stay abroad for 365 days out of last two years].

Articles not allowed under TR - Transfer of Residence concession is not available to alcoholic liquor or wines (in excess of two litres), cigarettes (exceeding 100), cigars (exceeding 25), tobacco (exceeding 125 gms), Gold (other than ornaments), Silver (other than ornaments), fire arms and cartridges of fire arms exceeding 50 - Annex I of Baggage.

Allowance for persons returning after one year i.e. Mini TR

A person who was working abroad and is returning to India on termination of work and who was staying abroad for at least 365 days out of previous two years, is eligible to certain concessions. This is termed as 'mini TR' i.e. 'Mini Transfer of Residence'. He is entitled to bring personal effects and household articles upto ₹75,000 duty free [The limit was ₹30,000 upto 28-2-2002]. This allowance is in addition to General Free Allowance. The conditions are (a) These should be in possession of himself or his family and used for at least six months (b) He shall be allowed to avail himself of this exemption only once in three years. (c) Items in Annex I, Annex II or Annex III to Baggage Rules are not allowed under this rule. (d) Goods should be contained in his bona fide baggage.

Items under Annex I are already explained above. Items under Annex II and Annex III are as follows :

Items in Annexure II - (1) Colour/ monochrome TV (2) Digital Video Disc (DVD) player (3) Video Home Theatre system (4) Dish washer (5) Music system (6) Air conditioner (7) Domestic refrigerator above 300 litres or its equivalent (8) deep freezer (9) Microwave oven (10) Video camera or combination of video camera with TV, sound/video recording apparatus (11) word processing machine. (12) Fax machine. (13) Portable photocopying machine (14) Vessels (15) Aircrafts (16) Cinematograph films of 35 mm and above. (17) Gold or Silver in any form, other than ornaments.

Items in Annexure III - (1) VCR/VCP/VTR/VCDP (2) washing machine (3) Electrical/ LPG Cooking range (4) Personal Computer (Desktop Computer) (5) Laptop (Note Book) Computer (6) Domestic Refrigerators of capacity upto 300 litres or its equivalent.

In other words, the exemption of ₹75,000 is illusory as the items a person would like to bring after stay abroad are mostly not exempt. However, duty payable is 30% on items included in Annex II upto value of ₹1,50,000 in case of Mini TR.

Since 'baggage' does not include motor vehicles, liquor and firearms, the exemption is obviously not applicable for those goods.

Concessional Rate if person returning after stay of 365 days - The general rate of customs duty on baggage is reduced to 30% if a person holding Indian passport, returns to India after staying abroad for at least 365 days in last two years. He should be 'working abroad', i.e. mere stay with relatives or others is not enough to avail this concession. The person is eligible for following concession : duty payable is 30% plus education cess of 2% of duty, on CTV, VCR, VCP, cooking range, washing machines, A/C, Refrigerator, dish washers, musical systems, refrigerator, deep freeze, micro-wave oven, video camera, word processing machine and Fax machine.

Concession is available for one unit of these goods per family upto total value of ₹75,000, inclusive of value of other goods imported duty free under rule 5 of Baggage Rules. [Under these rules, household articles excluding those in Annex I and Annex II are permitted to be imported duty free].

This concession is available if goods were in his possession or were purchased at International airport in duty free shop at the time of his arrival but before customs clearance - probably this is to encourage purchases in duty free shops in our international airports. The concession is also available to un-accompanied baggage despatched later within prescribed period. No CVD is payable.

Rupee payment in duty free shops - Goods upto ₹5,000 per passenger per visit can be purchased against rupee payments in duty free shops at international airport.

4.17.6 Concessions to Tourists

Tourists visit India for various purposes and rules have been framed to allow them to bring goods to India.

Who is a Tourist - Tourist means (a) a person who is not normally resident of India (b) who enters India for stay of not more than six months in the course of twelve month period (c) he should come for legitimate non-immigrant purpose such as touring, recreation, sport, health, family reasons, study, religious pilgrimages or business. [Rule 2(iii) of Baggage Rules, 1998].

Thus, Non-Resident Indians who do not hold Indian passports arc also covered in this definition.

Exemption to Baggage of tourists - Following are the exemptions [Appendix E as amended w.e.f. 14-11-2011]-

(a) Used personal effects of tourist are allowed duty free. Personal effects should be for personal use of the tourist and these goods, other than consumed, should be re-exported when tourist leaves India for foreign destination.

(b) Tourists of Indian origin (even if holding foreign passport) other than those coming from Pakistan by land route as specified in Annexure IV of Baggage Rules, are entitled to General Free Allowance in addition to 'personal effects'.

(c) Foreign Tourists (including tourist of Nepalese or Bhutanese origin, but other than tourists of foreign origin) are permitted to bring articles upto ₹8,000 (₹6,000 if they are coming from Pakistan by land route) for making gifts and travel souvenir. However, articles in Annexure I (cigars, liquor, gold, silver, arms) will not be allowed duty free, Duty has to be paid for gifts over the value of ₹8,000/ 6,000.

(d) Tourists of Pakistani origin or foreign tourists coming from Pakistan (by land route or by air), foreign tourists coming by land route from Pakistan, tourists of Indian origin coming from Pakistan by land route as specified in Annexure IV of Baggage Rules, are entitled to bring used personal effects and articles upto value of ₹6,000 for personal use or as gifts and travel souvenir.

Tourist include tourists of Nepalese origin coming from Nepal or of Bhutanese origin coming from Bhutan - Earlier, tourist of Nepalese origin coming from Nepal and Bhutanese origin coming from Bhutan were not entitled to any exemption. Now, w.e.f. 14-11-2011, they will be eligible for exemption available to any other tourist of foreign origin.

Articles for use of passenger always exempt - As per section 79(1)(b) of Customs Act, articles of baggage for use of the passenger or his family are exempt from customs duty. Hence they will be exempt even if the tourist is of Pakistani origin.

Persona/Effects- The term 'travel souvenirs' are not defined. The term 'Personal effects' as specified in MF(DR) circular dated 24-9-1998 has been explained earlier in this chapter.

Travel Souvenirs - The term 'travel souvenirs' has neither been defined nor explained in the Baggage Rules.

Import by foreign experts - Foreign experts assigned to India under various UN schemes etc. are permitted to bring various articles, including VCR, video camera and Air conditioners. These are exempt from customs duty on obtaining certificate of undertaking from the expert. Duty will be paid by concerned ministry/department- CBE&C circular No. 70/95-Cus dated 20-6-1995.

Foreign nationals can make payment in Rs or foreign exchange in India – Foreign Nationals, including Persons of Indian Origin, while in India, can make payment for charges towards airline/train tickets, hotels, hospitals etc. either in Indian Rupees or in equivalent foreign exchange.

4.17.7 Other provisions of Baggage

Other provisions regarding baggage are explained below:

Crew member of vessel/aircraft - Crew member of vessel/aircraft can bring petty gifts like chocolates, cheese, cosmetics etc. upto ₹1,500 while returning from foreign journey, for their personal use or family use [The limit was ₹600 upto 1-3-2013] - Rule 10 of Baggage Rules.

Indian Government officers posted abroad - Baggage Rules, 1994 are fully applicable to

Indian diplomatic officers and their families as well as Government of India officers posted abroad, when they return to India. Some concessions were granted to them vide instructions dated 16-4-1951. These concessions have now been withdrawn. In specific cases, ad hoc exemption on merits may be granted - CBE & C Circular No. 4/95-Cus dated 12-1-1995.

Export of Baggage

There are very few restrictions in taking out personal baggage. Prohibited goods cannot be taken out as baggage. Foreign and Indian currency can be taken out within the limits prescribed by RBI under FEMA.

Goods even in commercial quantities can be taken out as accompanied or un-accompanied baggage, if the passenger is able to establish source of funds for buying these goods as foreign exchange brought by him on his arrival in India. - CBE&C circular No. 17/95-Cus dated 1-3-1995.

If a tourist purchases goods in free foreign currency and takes it out as tourist baggage, duty drawback and other export benefits are available. The exporter must submit relevant encashment document of foreign currency, shipping bill etc. - CBE&C circular No. 36/98-Cus dated 20-5-1998.

Unaccompanied Baggage

Baggage' includes un-accompanied baggage brought before or after arrival of passenger within the prescribed period. Bona fide unaccompanied luggage is also allowed under above rules and subject to aforesaid restrictions, if it was in his possession abroad. The baggage may be sent by him earlier or after his departure from abroad. The conditions are (A) If despatched before he starts from abroad: Un-accompanied baggage may arrive upto two months prior to his arrival. This limit can be increased, if passenger could not start due to genuine reasons like sudden illness or natural calamities or disturbed conditions or any other genuine reason to the satisfaction of Assistant Commissioner. (B) Goods despatched after he starts journey: The condition is that the goods should be in his possession when he was abroad and despatched within one month of arrival of passenger in India. This limit can be increased by Assistant Commissioner of Customs. (Rule 9 of Baggage Rules,1998).

General Free Allowance is not allowed for un-accompanied baggage. In other cases, concessions available to baggage under Baggage Rules are also available for 'unaccompanied baggage'.

Detention and Transshipment of baggage

It may happen that goods brought by a tourist may be prohibited in India. In such case, if he makes true declaration in respect of those goods, the goods can be temporarily detained by customs authorities. These will be returned to him when he leaves India. If he is not able to personally take the goods, he can authorise any other passenger leaving India to collect the goods. Alternately, the goods can also be returned as cargo consigned in his name - [section 80 of Customs Act].

Transshipment of baggage - It may happen that the un-accompanied baggage lands at once customs station but the passenger may like to clear the goods from another customs station. In such cases, such baggage may be permitted to be transported by air or passenger train, under Baggage (Transit to Customs Stations) Regulations, 1967. The baggage will be under supervision of officer of customs. The passenger will have make all arrangements for transport and pay for supervision charges. This facility is available only at Mumbai, Delhi, Kolkata, Chennai, Bangalore, Trivendrum, Hyderabad, Cochin, Ahmedabad, Goa, Calicut, Coimbatore, Lucknow or Amritsar. The baggage can come by air, passenger train or trucks.

Levy of fees on detained or seized baggage - If customs authorities decide to detain the baggage for inspection/payment of duty/clarification etc.; the same will be kept in store in custody of customs. In such cases, the passenger will have to pay fees as prescribed by Principal Commissioner or Commissioner of Customs. The fees will be prescribed depending on nature of articles contained in baggage and expenses for transportation of goods from landing place to storage place and other expenditure incurred.

Clearance of passenger's baggage for export - Baggage for export also should be allowed after clearance from Customs Officer. The passenger should pay export duty, where leviable and produce export license, if applicable.

No demurrage on baggage - In International Airport Authority of India v. Ashok Dhawan 1999(106) ELT 16 (SC), it has been held that 'baggage' is not 'cargo' and hence no demurrage can be levied upon baggage. Same principle applies in case of transshipment also.

Import of cars

Import of cars in bulk is permitted, but there are restrictions in FTP. However, import of car on individual basis is permitted in following cases: (a) Import of cars by persons returning to India. They should have been staying abroad for continuous period of two years. However, short visits to India during these two years is permitted. This facility of import of cars is permitted only to persons who are returning to India for permanent settlement. - CBE&C circular No. 96/95/CUS. VI dated 29-8-1995. (b) Foreign privileged persons (like diplomats etc.) can import cars. If they want to sell in India, such sale must be only to State Trading Corporation (STC). If the sale is within three years, STC has to pay customs duty on the car. (c) Air conditioned cars can be imported for tourism development. Authorisation /certificate from Director General, Tourism will be deemed to be import licence for this purpose. There is no condition regarding ceiling on value. The import duty can be paid in Indian rupees.

PRACTICAL PROBLEMS

Example 27: Mrs. & Mr. Menon visited Germany and brought following goods while returning to India after 6 days stay abroad on 8th April 2015.

(i) Their personal effects like clothes, etc., valued at ₹ 45,000.

(ii) A personal computer bought for ₹ 56,000.

(iii) A laptop computer bought for ₹ 95,000.

(iv) Two liters of liquor bought for ₹ 1,600.

(v) A new camera bought for ₹ 37,400.

What is the amount of customs duty payable?

Answer:

Their personal effects like clothes, etc., valued at ₹ 45,000.	exempt
A personal computer bought for ₹ 56,000.	56,000
A laptop computer bought for ₹ 95,000.	exempt
Two liters of liquor bought for ₹ 1,600.	1,600
A new camera bought for ₹ 37,400.	37,400
Total	95,000
Less: General Free Allowance ₹ 45,000 + ₹ 45,000	90,000
Baggage taxable	5,000

Customs Duty is ₹ 1,803 (i.e. 5,000 x 36.05%) payable by Mrs. & Mr. Menon.

Example 28: After visiting USA, Mrs. & Mr. Rao brought to India a laptop computer valued at ₹ 80,000 personal effects valued at ₹ 90,000 and a personal computer for ₹ 52,000. What is the customs Duty payable?

Answer: Duty payable on baggage = ₹ (52,000 – 45,000) x 36.05% = ₹ 2,524

Example 29: Mr. Ram an Indian resident, aged 45 years, returned to India after visiting USA on 10/05/2015. He had gone to USA on 1/05/2015. On his way back to India he brought following goods with him –

His personal effects like clothes etc. valued at ₹ 90,000:

2 liter of Wine worth ₹ 11,000;

A video camera worth ₹ 21,000;

A watch worth ₹ 23,000.

Find the customs duty payable by Mr. Ram

Answer :

2ltrs of wine	= ₹ 11,000
Video camera	= ₹ 21,000
Watch	= ₹ 23,000
Total	= ₹ 55,000
Less: GFA	= ₹ 45,000
Net value	= ₹ 10,000
Customs duty @ 36.05% on ₹ 10,000	= ₹ 3,605

Example 30: Mr. Venkatesh, an IT professional and a person of Indian origin, is residing in U.S.A. for the last 14 months. He wishes to bring a used microwave oven (costing approximately ₹ 11,200 and weighing 15 kg) with him during his visit to India. He purchased the oven in U.S.A. 6 months back and he has been using that oven for his personal use in his kitchen. He is not aware of Indian customs rules. Could you please provide him some advice in this regard?

Answer :

Free allowances to professionals in respect of their professional equipments upto ₹ 40,000 if Indian passenger returning to India after at least 6 months and in case of house hold articles it is upto ₹ 12,000.

In the given example Venkatesh brings the used household articles worth ₹ 11,200 which is free of duty. As per the rule 5 of the Baggage Rules, 1998 he is not liable to pay any duty.

Example 31: Mr. C is a Cost Accountant, Indian resident worked in USA for 4 months, brought with him the following items on his return to India.

Personal effects like clothes etc. of ₹ 5,50,000;

Jewellery of ₹ 25,000

A Camera for ₹ 50,000

Household articles of ₹ 30,000

Professional equipments like electronic diary, calculator and other items worth ₹ 40,000

A Laptop worth for ₹ 3,00,000

Compute the duty payable by Mr. C

Answer:		**Amount in ₹**
Jewellery	=	25,000
Camera	=	50,000
Household articles	=	30,000
Professional equipments	=	40,000
Subtotal	=	1,45,000
Less: GFA 45,000 + 12,000+20,000	=	77,000
Balance subject to duty	=	68,000

Basic Customs Duty ₹ 24,514 (i.e. ₹ 68,000 x 36.05%)

Example 32: Mr. Kishore is a Chartered Accountant (aged 40 years) an Indian resident goes to Nepal on tour. He purchased one computer for ₹ 50,000, one laptop computer for ₹ 1,50,000 and hair dryer of ₹2,000 in a duty free shop in Nepal and brings the same to India. What is the duty payable?

(i) If he returns on 3rd day by air

(ii) If he returns on 3rd day by land route

(iii) If he returns on 15th day by air

(iv) If he returns on 15th day by land route

Answer :

(i) If he returns on 3rd day by air:

Value of Computer and hair dryer is taxable @36.05% One laptop is exempt from duty

General Free Allowance not allowed

Customs Duty = ₹ 18,746 (i.e. 52,000 x 36.05%)

(ii) If he returns on 3rd day by land route:

Value of Computer and hair dryer is taxable @36.05% One laptop is exempt from duty

General Free Allowance not allowed

Customs Duty = ₹ 18,746 (i.e. 52,000 x 36.05%)

(iii) If he returns on 15th day by air (i.e. after 3 days of stay):

Value of Computer and hair dryer is taxable @36.05% One laptop is exempt from duty

General Free Allowance ₹ 6,000 is allowed

Customs Duty = ₹ 16,583 [i.e. (52,000 –6,000) x 36.05%]

(iv) If he returns on 15th day by land route:

Value of Computer and hair dryer is taxable @36.05% One laptop is exempt from duty

General Free Allowance not allowed

Customs Duty = ₹ 18,746 (i.e. 52,000 x 36.05%)

4.17.7 Import and Export through Courier – Postal Articles

As per sections 82 to 84 of the Customs Act, 1962, goods can be cleared by post. Any label or declaration accompanying the goods showing the description, quantity and value thereof, shall be treated as "an entry for import" under the Customs Act.

The rate of duty and tariff value applicable to goods imported by post shall be the rate and valuation in force on the date on which the postal authorities present to the proper officer a list containing the particulars of such goods for the purpose of assessment of duty.

The procedure for clearance:

(i) Post parcels are allowed to pass from port/airport to Foreign Parcel Department of Government Post Offices without payment of customs duty.

(ii) The Postmaster hands over to Principal Appraiser of Customs the memo showing Total number of parcels from each country of origin,

- Parcel bills or senders 'declaration,
- Customs declaration and dispatch notes, and
- Other information that may be required.

The mail bags are opened and scrutinized by Postmaster under supervision of Principal Postal Appraiser of Customs.

(iii) Packets suspected of containing dutiable goods are separated and presented to Customs Appraiser with letter mail bill and assessment memos.

(iv) The Customs Appraiser marks the parcels which are required to be detained if— necessary particulars are not available, or misdeclaration or undervaluation is suspected or goods are prohibited for import.

Appraiser has the power to examine any parcel. After inspection, the parcels are sealed with a distinctive seal. Any misdeclaration or undervaluation is noted or goods are prohibited goods for imports these be detained and the same intimated to Principal Commissioner or Commissioner of Customs.

If everything is in order after verification, goods will be handed over to Post Master, who will hand over the same to the addressee on receipt of customs duty.

4.17.8 Import through post

i. Label/declaration on postal article is treated as 'Entry'. Separate Bill of Entry is not required.

ii. Postal articles are sent to Foreign parcel Department of Post Office. The list is handed over to Principal Appraiser of Customs.

iii. He will inspect mail. Packets suspected of dutiable articles will be opened and examined by him. He will assess the goods and then seal the parcel.

iv. Goods will be handed by postmaster to addressee only on receipt of customs duty payable on the goods.

v. Gifts upto ₹ 10,000 are free. Post parcel is exempt if customs duty is upto ₹ 100.

4.17.9 Import of Samples

In the International trade it is considered often necessary that samples of the goods manufactured in one country be sent to another country for being shown or demonstrated for Customer appreciation. There are duty free imports of genuine commercial samples into the country for smooth flow of trade.

The commercial samples are basically specimens of goods that may be imported by the traders or representatives of manufacturers. However, goods which are prohibited under Foreign Trade (Development and Regulation) Act, 1992 are not allowed to be imported as samples (i.e. wild animals, wild birds and parts of wild animals, arms and ammunitions and so on).

Samples can be imported by the traders, industry, individuals, research institutes and so on. These samples can also be brought by the persons as part of their personal baggage or through port or in courier.

4.18 DRAWBACK

4.18.1 Basic concept

In ' duty drawback' , the excise duty and customs duty paid on inputs and service tax paid on input services is given back to the exporter of finished product by way of 'duty drawback'.

It may be noted that duty drawback under section 75 is granted when imported materials are used in the manufacture of goods which are then exported, while duty drawback under section 74 is applicable when imported goods are re-exported as it is, and article is easily identifiable.

Duty drawback rates are of following types - (a) All Industry Rate (b) Brand Rate and (c) Special Brand Rate. Duty drawback rates can be fixed with retrospective effect [rule 5(2) of Drawback Rules, 1995].

Comparison of the provision of section 74 and 75 is as follows:

Drawback allowable on re-export of duty paid goods – (Sec. 74)	Drawback on material used in the manufacture of exported goods (sec. 75)
(i) Drawback, in relation to any goods exported out of India, means refund of duty paid on importation of such goods in terms of section 74. Thus, drawback is allowed only if import duties of customs.	"Drawback" in relation to any goods manufactured in India and exported, means the rebate of duty or fact, as the case may be, chargeable on cay imported materials or excisable materials used or taxable services used as input services in the manufacture of such goods.
(ii) The identity of the goods exported should be established as the one, which was imported on payment of duty.	The goods exported under this section one different from the inputs as the inputs are manufactured, processed or any operations are carried on then before their export.
(iii) Drawback under this section is available on all goods (Identification is the only criterion)	Drawback under this section is available only on notified goods.
(iv) The exported goods should have been imported and customs duty by paid thereon.	The goods to be exported may be manufactured or processed from imported or indigenous inputs or by utilizing input services.

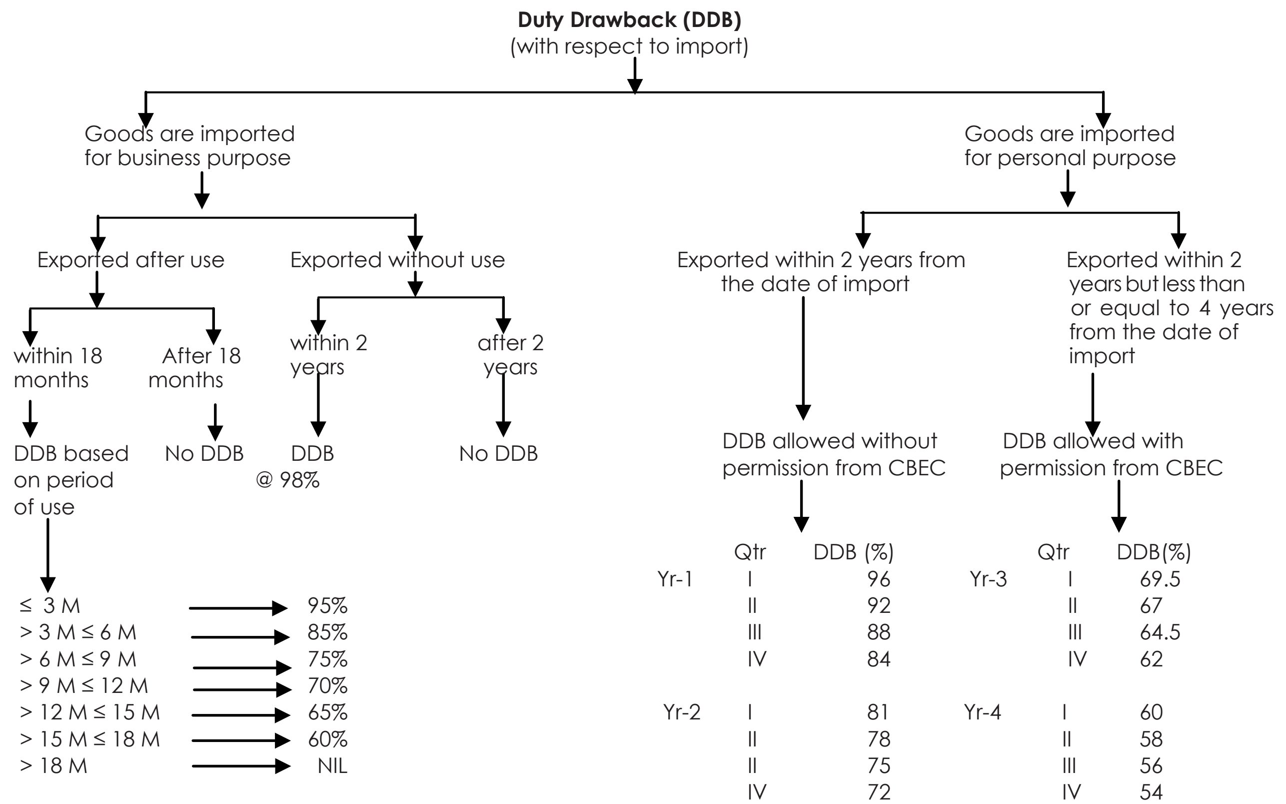
(v) The rate of drawback is 98% in case the goods are exported without use. The rate of drawback on goods taken into use is separately notified depending upon the period of use, depreciation in value and other relevant factors.	Drawback is allowed at All Industry Rate or Brand Rate or Special Brand Rate, as is applicable.
(vi) The goods should be exported within two years (or extended period) from the date of payment of duty or such extended time as the board may allow.	No such restrictions.
(vii) There is no criterion of minimum value addition, which is to be fulfilled before export for claim of drawback.	It has been specifically provided that there should not be negative value addition and in case where minimum value addition is specified the same should be achieved for claim of drawback.
(viii) No provision for recovery of export sale proceeds	The sale-proceeds in respect of such goods on which the drawback has been allowed, have to be received by the exporter or by any person on his behalf with the period as specified by RBI, except in exceptional circumstances
(ix) The drawbacks is governed by the Re-export of Imported Goods (Drawback of Customs Duties) Rules, 1995.	The drawback, in this case, is governed by the Customs, Central Excise Duties and Service Tax drawback Rules, 1995. The rules cover customs duty, central excise duty and service tax.

4.18.2 Duty Drawback on Re-Export – Section 74 of Customs Act, 1962 provide for drawback if the goods are re-exported as such or after use. This may happen in case like import for exhibitions, goods rejected or wrong shipment etc. The re-exported goods should be identifiable as having been imported and should be re-exported within two years from date of payment of duty when they were imported. This period (of two years) can be extended by CBE&C on sufficient cause being shown. These should be declared and inspected by Customs Officer. Original shipping bill under which the goods were imported should be produced. The goods can be exported as cargo by air or sea, or as baggage or by post. After inspection, export and submission of application with full details, 98% of the customs duty paid while importing the goods is repaid as drawback. @98% of import duty is allowed as Duty Drawback if re-exported without use.

Duty draw back in case of goods used after importation, allowed based on period of usage:

Period between date of clearance for home consumption and date to when goods are placed under customs control for export	**% of DDB on import duty**
≤ 3M	95%
> 3M ≤ 6M	85%
> 6M ≤ 9M	75%
> 9M ≤ 12M	70%
> 12M ≤ 15M	65%
> 15M ≤ 18M	60%
> 18M	NIL

Summary of duty drawback on re-export has been explained as follows —



All Industry Drawback Rates – All Industry Drawback rates are fixed by Directorate of Drawback, Dept. of Revenue, Ministry of Finance, Govt. of India, Jeevan Deep, Parliament Street, New Delhi-110001. The rates are periodically revised-normally on 1st June every year. The All Industry Drawback Rate is fixed under rule 3 of Drawback Rules by considering average quantity and value of each class of inputs imported or manufactured in India.

Duty drawback rate shall not exceed 33% of market price of export goods (Rule 8A of the Customs, Central Excise Duties and Service Tax Drawback Rules w.e.f. 15-2-2006).

Brand Rate of Duty Drawback – It is possible to fix All Industry Rate only for some standard products. It cannot be fixed for special type of products. In such cases, brand rate is fixed under rule 6 by furnishing the prescribed data within 3 months from the relevant date for determination of rate of duty and tariff valuation under section 16 or 83, to the Principal Commissioner or Commissioner of Central Excise and Customs stating all relevant facts including the proportion in which the materials or components or input services are used in the production or manufacture of goods and the duties paid on such materials or components or service tax paid on such input services.

Special Brand Rate of duty drawback – In case if the duty drawback as per all industry rate is less than 80% of the duties or taxes paid on the materials or components or input services, then the manufacturer or exporter, except where a claim for drawback under rule 3 or rule 4 has been made, can apply for special brand rate to the Principal Commissioner or Commissioner of Central Excise and Customs by furnishing the prescribed data within 3 months from the relevant date for determination of rate of duty and tariff valuation under section 16 or 83.

Practical Problems Related to Customs Duty

Example 33: Calculate the amount of duty drawback allowable under section 74 of the Customs Act, 1962 in following cases:

(a) Salman imported a motor car for his personal use and paid ₹ 5,00,000 as import duty. The car is re-exported after 6 months and 20 days.

(b) Nisha imported wearing apparel and paid ₹ 50,000 as import duty. As she did not like the apparel, these are re-exported after 20 days.

(c) Super Tech Ltd. imported 10 computer systems paying customs duty of ₹ 50 lakh. Due to some technical problems, the computer systems were returned to foreign supplier after 2 months without using them at all.

Answer :

(a) The amount of duty drawback is ₹ 4,40,000 (i.e. ₹ 5,00,000 x 88%), since these goods used in India.

(b) Duty drawback is not allowed on wearing apparel.

(c) Duty drawback is ₹ 49,00,000 (*i.e.* ₹ 50,00,000 x 98%), since these goods are re-exported without being used.

Example 34: Computation of duty drawback: 'A' exported a consignment under drawback claim consisting of the following items—

Particulars	Chapter Heading	FOB value (₹)	Drawback rate
200 pieces of pressure stoves mainly made of beans @₹ 80/piece	74.04	16,000	4% of FOB
200 Kgs. Brass utensils @₹ 200 per Kg.	74.13	40,000	₹ 24/Kg.
200 Kg. Artware of brass @₹ 300 per Kg.	74.22	60,000	17.50% of FOB subject to a maximum of ₹ 38 per Kg.

On examination in docks, weight of brass Artware was found to be 190 Kgs. and was recorded on shipping bill. Compute the drawback on each item and total drawback admissible to the party.

Answer:

The drawback on each item and total drawback admissible to the party shall be-

Particulars	FOB value (₹)	Drawback rate	Drawback Amount (₹)
200 pcs, pressure stoves made of brass	16,000	4% of FOB	640
200 Kgs. Brass utensils	40,000	₹ 24 per Kg.	4,800
200 kgs. Artware of brass, whose actual weight was 190 Kgs. only.	60,000	1 7.50% of FOB subject to maximum of ₹ 38 per Kg. (₹ 9,975 or ₹ 7,220 whichever is less)	7,220
Total Drawback admissible (in ₹)			12,660

Example 35: X Ltd has exported following goods: Product P, FOB value worth ₹ 1,00,000 and the rate of duty drawback on such export of goods is 0.75%. FOB value of product 'Q' worth ₹ 10,000 and the rate of duty drawback on such export of goods is 1%. Will X Ltd be entitled to any duty drawback?

Answer:

Duty drawback on product P allowed is ₹ 750 (*i.e.* 1,00,000 x 0.75%), since amount is more than ₹ 500.

Duty drawback on product Q is allowed, because the amount of duty drawback ₹ 100 (which is more than ₹ 50).

Example 36: Y Ltd has been exported following goods to USA. Discuss whether any duty drawback is admissible under section 75 of the Customs Act, 1962.

Product	FOB Value of Exported goods (₹)	Market Price of goods (₹)	Duty drawback rate
A	2,50,000	1,80,000	30% of FOB
B	1,00,000	50,000	0.75% of FOB
C	8,00,000	8,50,000	3.50% of FOB
D	2,000	2,100	1.50% of FOB

Note: Imported value of product C is ₹ 9,50,000.

Answer :

Duty draw back amount for all the products are as follows:

Product A:

Drawback amount = 2,50,000 x 30% = ₹ 75,000 or ₹ 1,80,000 x 1/3 = ₹ 60,000

Allowable duty draw back does not exceed 1/3 of the market value.

Hence, the amount of duty drawback allowed is ₹ 60,000

Product B:

Drawback amount allowed is ₹ 750 (i.e. ₹ 1,00,000 x .0.75%). Since, the amount is more than ₹ 500 even though the rate is less than 1%.

Product C:

No duty drawback is allowed, since the value of export is less than the value of import (i.e. negative sale)

Product D:

No duty drawback is allowed, since the duty drawback amount is ₹ 30 (which is less than ₹ 50). Though rate of duty drawback is more than 1%, no duty drawback is allowed.

4.19 OTHER PROVISIONS IN CUSTOMS

4.19.1 Person who had received any Show Cause Notice in Last Three Financial Years is Ineligible –

In order to ensure that scope of the scheme remains limited (and the scheme fails), it is provided that no case should be pending against them. Even show cause notice invoking penal provisions should not have been issued against them is last three financial years. Such importers can be probably counted on fingers. If this condition is insisted upon, the scheme is stillborn and will be a non-starter.

4.19.2 Application for Getting Accreditation

Importers desirous of availing the facility of 'Accredited Client' has to make application for registration in form given in MF (DR) circular No. 42/2005-Cus dated 24-11-2005. Application has to be accompanied by a CA certificate that the accounting system of applicant is as per accounting standards prescribed by ICAI.

4.19.3 Decision regarding ACP status within 30 days

In case of status holders, Customs will communicate decision on conferring ACP status (Accredited Client under Risk Management System of customs clearance, within 30 days from receipt of application by customs.

4.19.4 Risk Management Division in Systems Directorate

A risk management division has been created in Systems Directorate. Risk Management Committees will be constituted at National level and Local level –MF(DR) circular No. 23/2007-Cus dated 28-6-2007.

4.20 PROJECTS IMPORTS

4.20.1 Basic Concept

Project imports status is being granted to the green houses set up for protected cultivation of horticulture and floriculture product. As such, these projects would attract concessional rate of basic customs duty of 5%.

4.20.2 Salient Features of Project Imports

(i) 'Project Imports' is an Indian innovation to facilitate setting up of and expansion of industrial projects. Normally, imported goods are classified separately under different tariff headings and assessed to applicable Customs duty, but as a variety of goods are imported for setting up an industrial project their separate classification and valuation for assessment to duty becomes cumbersome. Further, the suppliers of a contracted project, do not value each and every item or parts of machinery which are supplied in stages. Hence, ascertaining values for different items delays assessment leading to demurrage and time and cost overruns for the project. Therefore, to facilitate smooth and quick assessment by a simplified process of classification and valuation, the goods imported under Project Import Scheme are placed under a single Tariff Heading 98.01 in the Customs Tariff Act, 1975. The Central Government has formulated the Project import Regulation, 1986 prescribing the procedure for effecting imports under this scheme.

(ii) The Project Import Scheme seeks to achieve the objective of simplifying the assessment in respect of import of capital goods and related items required for setting up of a project by classifying all goods under heading 98.01 of the Customs Tariff Act, 1975 and prescribing a uniform Customs duty rate for them even though other headings may cover these goods more specifically.

(iii) The different projects to which heading 98.01 applies are; irrigation project, power project, mining project, oil/mineral exploration projects, etc. Such an assessment is also available for an indus1nal plants used in the process of manufacture of a commodity. The Central Government can also notify projects in public interest keeping in view the economic development of the country to which this facility will apply. Thus, a number of notifications have been issued notifying a large number of projects for assessment under Tariff Heading 98.01. However, this benefit is not available to hotels, hospitals, photographic studios. Photographic film processing laboratories, photocopying studio, laundries, garages and workshops. This benefit is also not available to a single or composite machine.

(iv) Goods that can be imported under Project Import Scheme are machinery, prime movers, instruments, apparatus, appliances, control gear, transmission equipment, auxiliary equipment, equipment required for research and development purposes, equipment for testing and quality control, components, raw materials for the manufacture of these items, etc. In addition, raw material, spare parts, semi-finished material, consumables up to 10%, of the assessable value or goods can also be imported.

(v) The purposes for which such goods can be imported under the Project Import Scheme are for 'Initial setting up' or for 'Substantial expansion' of a unit of the project. The 'unit' is any self contained portion of the project having an independent function in the project. A project would fall under the category of 'substantial expansion' if the installed capacity of the unit is increased by not less than 25%. as per the Project Import Regulations.

4.20.3 Registration of Contracts

(i) In terms of Regulation 4 of the Project Import Regulations. 1986 (PIR) the basic requirement for availing the benefit of assessment under Tariff Heading No. 98.01 is that the importer should have entered into one or more contracts with the suppliers of the goods for setting up a project. Such contracts should be registered prior to clearance in the Customs House through which the goods are expected to be Imported The importer shall apply for such registration in writing to the proper officer of Customs.

(ii) Regulation 5 provides in the manner of registering contracts as follows:-

(a) Before any order is made by the proper officer of customs permitting the clearance of the goods for home consumption;

(b) In the case of goods cleared for home consumption without payment of duty subject to re-export in respect of fairs, exhibitions, demonstrations, seminars, congress and conferences, duly sponsored or approved by the Government of India or Trade Fair Authority of India, as the case may be, before the date of payment of duty.

(iii) To expedite registration, the importers are advised to submit the following documents along with the application for registration:-

(a) Original deed of contract together with true copy thereof.

(b) Industrial License and letter of intent, SSI Certificate granted by the appropriate authority with a copy thereof.

(c) Original Import license, if any, with a list of items showing the dimensions, specifications, quantity, quality, value of each item duly attested by the Licensing Authority and a copy thereof.

(d) Recommendatory letter for duty concession from the concerned Sponsoring Authority, showing the description, quantity, specification, quality, dimension of each item and indicating whether the recommendatory letter is for initial set up or substantial expansion, giving the installed capacity and proposed addition thereto.

(e) Continuity Bond with Cash Security Deposit equivalent to the 2% of CIF value of contract sought to be registered subject to the maximum of ₹ 50,00,000/- and the balance amount by Bank Guarantee backed by an undertaking to renew the same till the finalisation of the contract. The said continuity bond should be made out for an amount equal to the CIF value of the contract sought to be registered.

(f) Process flow chart, plant layout, drawings showing the arrangement of imported machines along with an attested copy of the Project Report submitted to the Sponsoring authorities, Financial Institution, etc.

(g) Write up, drawings, catalogues and literature of the items under import.

(h) Two attested copies of foreign collaboration agreement, technical agreement, know-how, basic/detailed engineering agreement, equipment supply agreement, service agreement, or any other agreement with foreign collaborators/suppliers/persons including the details of payment actually made or to be made.

(i) Such other particulars, as may be considered necessary by proper officer for the purpose of assessment under Heading No. 9801.

(iv) After satisfying that goods are eligible for project imports benefit and importer has submitted all the required documents, the contract is registered by the Custom House and as a token of registration the provisional duty bond is accepted by the Assistant/ Deputy Commissioner of Customs, Project Import Group. The details of the contracts are entered in the register kept for the purpose and a Project Contract Registration Number is assigned and communicated to the importer. The importer is required to refer to this number in all subsequent correspondence.

4.20.4 Clearance of Goods after Registrations

On every Bill of Entry filed for clearance of goods under the Project Import Scheme, the importer I CHA is required to indicate the Project Contract Registration Number allotted to it. After noting, the Bill of Entry is sent to the Project import Group, which is required to check the description, value and quantity of the goods imported vis-a-vis the description, value and quantity registered. In case these particulars are found in order, the Bill of Entry is assessed provisionally and handed over to the importer or his agent for payment of duty. The Project Import Group keeps a note of the description of the goods and their value in the Project Contract Register and in the file maintained in the Group for each project.

4.20.5 Finalisation of Contract

(i) Under Regulation 7 of the PIR, 1986 the importer is required to submit, within three months from the date of clearance of the last consignment or within such extended time as the proper officer may allow, the following documents for the purpose of finalisation of the assessment:-

   (a) A reconciliation statement i.e. a statement showing the description, quantity and value of goods imported along with a certificate from a registered Chartered Engineer certifying the installation of each of the imported items of machinery;

   (b) Copies of the Bills of Entry, invoices, and final payment certificate. The final payment certificate is insisted upon only in cases where the contract provides that the amount of the transaction will be finally settled after completion of the supplies.

(ii) To ensure that the imported goods have actually been used for the projects for which these were imported, plant site verification may be done in cases where value of the project contract exceeds ₹ 1 crore. In other cases plant site verification is normally done selectively.

(iii) In the normal course, after submission of the reconciliation statement and other documents by the importers, the provisional assessments are finalized within a period of three months where plant site verification is not required and within six months where plant site verification is required. In cases where a demand has been issued and confirmed on such finalization and importer has not paid the duly demanded, steps are taken as per law to realise the amount.

Benefit available in the absence of Restrictions of Registration before Warehousing:

Registration of contracts before an order is made permitting clearance for home consumption or before the deposit in warehouse to avail benefit of concessional rate of duty. Goods imported were warehoused awaiting registration cleared for home consumption only after registration. Restrictions of registration before warehousing being absent in present Regulations benefit is available. Regulations 4 and 5 of Project Import Regulations, 1986. [Para's 2, 3, 4)-Bharat Earth Movers Limited u. Commissioner of Customs, Mysore 2006 (201) ELT 60 (Tri.-Bang)

Project Imports benefit not to be denied merely because goods cleared before Registration of contract. Project Imports benefit available to expansion of computer software plant.-Collector v. DPS India (P) Ltd. 1997 (92) ELT A130 (SC)

No Replacement Imports form part of the Original Import:

Contract covering all the imports registered, all the formalities under the Project Imports Regulations fulfilled - Appellants submitted certain reasons for not getting free replacements from original supplier - Secretary to Government of Kerala, sponsoring authority of the project, issued the essentiality certificate for the replacements stating that items imported are entitled for concessional duty under Project Import

Regulations- Lower authorities' reasoning that since replacements are not free, therefore, project import benefit cannot be given has no legal basis - Damaged parts having been exported and no indication that Project Import Regulations have been misused by appellants - Appellants entitled for benefit of project import - Regulations 4, 5, 6 of Project Import Regulations, 1986. [Para 7)-'--BSES Kerala Power Limited v. Commissioner of Customs, Cochin 2006 (196) ELT 246 (Tri.-Bang)

Import of spares be considered under Project Imports:

Original assessment claimed on merits under respective headings - Assessee entitled to claim assessment as project import under Heading 98.01 of Customs Tariff when assessment is reopened- Import of spares to be considered under Project Imports.-Tata Hydro Electric Power Supply Co. Ltd. v. C.C., Mumbai 1999 (114) ELT 171 (Tri.-Bom)

Exemption from Customs duty under other notifications not deniable to Project Imports:

Exemption from Customs duty under other notifications is not deniable to Project Imports - Horological machinery imported without specifying the Tariff Heading but treated as Project Import under Chapter 98 - Notification dated 28-2-1985, exempts Horological machinery from duty in excess of 10% without specifying the Tariff Heading - HELD: Horological machines eligible to the benefit of notification dated 28-2-1985 even if cleared under Heading 98.01 of Customs Tariff since project import notification clearly specifies that exemption under other notifications will not be effected by it and moreover the exemption notification, dated 28-2-1985 did not specify the Heading for the goods exempted under it. -Abrol Watches Put. Ltd. u. Collector of Customs, Bombay 1997 (092) ELT 311 (SC)

No industrial license is necessary from the DGTD before the benefit of Heading 84.66 could be given to an importer:

There is nothing in the Project Imports (Registration of Contract) Regulations, 1965 [sub-regulations 3(a) and 3(c)] to indicate that there must be an industrial license necessarily from the DGTD before the benefit of Heading 84.66 could be given to an importer.-Collector of Customs u. Kodagu Coffee Growers Co-Op. Society Ltd. 1992 (61) ELT 300 (Tri.-Del)- This case was Approved in 1997 (94) ELT 476 (SC)

Project Import Regulations cannot be held as excessive delegated legislation to declare them invalid.

Project Imports Regulations, 1986 defined "industrial plant" so as to exclude service establishments like photographic studios from project import benefit. Note (2) to Chapter 98 of Customs Tariff Act, 1975 does not amount to excessive delegation - Section 157 of Customs Act, 1962. "We are, therefore, of the considered opinion that Chapter Note (2) cannot be faulted as an instance of excessive delegation of essential legislative function nor can the Project Imports Regulations be faulted on the ground of travelling beyond the purview of the statute." [1967 (3) S.C.R. 557, 1979 (1) SCR 845 and 1981 (2) SCR 742 followed].

Project Imports Regulations, 1986 are relatable not only to Section 157 of Customs Act, 1962 but also to express power conferred by Note (2) to Chapter 98 of Customs Tariff Act, 1975. Any alleged practice to the contrary is irrelevant. - Subhash Photographics v. Union of India 1993 (66) ELT 3 (SC)

Captive power plant a part of Project Imports

Zuari Industries Ltd v. CCE & C 2007-T/OL-55-SC-CUS (Dated: March 29, 2007)

Captive power plant - Part of project imports eligible for exemption - Heading 98.01 is a specific entry - Once an essentiality certificate was issued by the sponsoring authority, it was mandatory for the Revenue to register the contract.

4.21 OFFENCES, POWER AND PENALTIES UNDER CUSTOMS

4.21.1 Offences under Customs

The term Offence means a violation or breach of a law, like evasion of duty and breaking prohibitions under the Customs Act, 1962. However, offence not defined under Customs Act, 1962. Thereby, 'Offence' as any act or omission made punishable by any law for the time being in force.

There are basically two types of punishments namely civil penalty and criminal penalty. Civil penalty for violation of statutory provisions involving a penalty and confiscation of goods and can be exercised by the Department of Customs. Criminal punishment is of imprisonment and fine, which can be granted only in a criminal court after prosecution.

4.21.2 Evasion of duty or prohibition under section 135(1) of the Customs Act, 1962

If a person has nexus with misdeclaration of value or evasion of duty or handling in any manner goods liable for confiscation under section 111 (i.e. Confiscation of improperly imported goods) or section 113 (i.e. Export goods liable for confiscation), he shall be punishable in the following manner:

4.21.3 Imprisonment upto SEVEN years and FINE for the following four kinds of offences

i. Market value of offending goods exceeds ₹ 1 Crore

ii. Value of evasion of duty exceeds ₹ 30 lakhs

iii. Offence pertains to prohibited goods notified by Central Government of India

iv. Value of fraudulent availment of drawback/exemption exceeds ₹ 30 lakhs

For all other kind of offences imprisonment is upto THREE years or fine or both.

For repeat conviction, the imprisonment can be SEVEN years and FINE and in absences of special and adequate reasons, the punishment shall not be less than ONE year.

4.21.4 Cognizable and Non-cognizable Offence

Cognizable offence means an offence for which a police officer may arrest without warrant (i.e. without the order of a Magistrate). Non-cognizable offence means offences under Customs were a police officer cannot investigate cases without the order of a Magistrate.

Cognizance of Offences

As per Section 137(1) of the Customs Act, 1962, Court cannot take cognizance of offences under the Customs Act, 1962 in the following cases without previous sanction of the Principal Commissioner or Commissioner of Customs:

i. False declaration or documents (Section 132)

ii. Obstruction (i.e. stop the progress) of Officers of Customs (Section 133)

iii. Refusal to be X-rayed (Section 134)

iv. Evasion of duty or prohibitions (Section 135)

v. Preparation to do clandestine export (i.e. improper export) (Section 135A)

As per Section 137(2) of the Customs Act, 1962, for taking cognizance of an offence committed by a Customs officer under section 136 the Court needs previous sanction of the Central Government in respect of officers of the rank of Assistant or Deputy Commissioner and above and previous sanction of the Principal Commissioner or Commissioner of Customs in respect of officers lower in rank than Assistant or Deputy Commissioner.

4.21.5 Section 136 of the Customs Act deals with offences by Officers of Customs:

i. An officer of customs facilitated to do fraudulent export.

ii. Search of persons without reason to believe in the secreting of goods on them.

iii. Arrest of person without reason to believe that they are guilty.

iv. These are called *vexatious actions* of department officers.

4.21.6 Power

Section 100

i. Power to search suspected persons entering or leaving India.

ii. Search of person for any goods liable for confiscation by the proper officer in and around customs area.

iii. Burden of proof on department (section – 123).

Section 101

i. Power to search suspected person in certain other cases.

ii. Search is conducted by the officer of customs empowered by the Principal Commissioner or Commissioner.

iii. Search of person for notified goods which are liable for confiscation order by Principal Commissioner or Commissioner anywhere in India.

iv. Burden of proof, that goods not smuggled, or importer.

Section 105

i. Power to search premises.

ii. Search of place for goods liable for confiscation & documents useful for any proceeding under the Act.

iii. If notified goods, burden of proof that goods are not smuggled on importer.

Section 106

i. Power to stop and search conveyance.

ii. Stop and search conveyance for any smuggled goods.

iii. Refer section 115.

Section 110

i. Seizure of goods, documents & things.

ii. Seizure of goods & documents are liable to confiscation.

iii. Notice must be made by proper officer for confiscation of goods within 6 months.

Section 100, 101 & 105

i. For prohibited goods may give option to redemption fire (Except arms, RDX etc).

ii. For other goods must give an option.

iii. In both the above case, goods are smuggled goods.

4.21.7 Penalties under Custom Act

i. Smuggling in relation to goods is an act or omission which will make the goods liable to confiscation.

ii. Penalty can be imposed for improper import as well as attempt to improperly export goods. ‘Improper’ means without the knowledge of the customs officers.

iii. Monetary penalty upto value of goods or ₹ 5,000 whichever is higher can be imposed.

iv. Goods can be confiscated. Permission can be granted for re-export of offending goods.

v. In case of goods covered under section 123 of Customs Act, burden of proof that the goods are not smuggled goods is on the accused.

Following monetary penalties prescribed under section 112 of the customs Act, with regard to improper importation:

Imported Goods (A)	Value in (₹) (B)	Minimum Penalty in (₹) (C)	Minimum Penalty in (₹) (B) or (C)
Prohibited Goods	Value of prohibited goods	₹ 5,000	Whichever is higher
Dutiable goods (Other than prohibited goods)	Duty sought to be evaded on such goods x 10%	₹ 5,000	Whichever is higher
Misdeclaration of value	Value declared - Actual value = ₹ XXXX	₹ 5,000	Whichever is higher
Prohibited goods plus misdeclaration value	Value of prohibited goods or Value declared – Actual value whichever is higher	₹ 5,000	Whichever is higher
Dutiable goods plus misdeclaration of value	Duty sought to be evaded or Value declared – Actual value whichever is higher	₹ 5,000	Whichever is higher

4.21.8 Export Goods Liable for Confiscation (Section 113)

These are goods attempted to be improperly exported under clause of section 113.

(a) Goods attempted to be exported by Sea or Air from place other than customs port or customs airport.

(b) Goods attempted to be exported by land or inland water through unspecified route.

(c) Goods brought near land frontier or coast of India or near any bay, gulf, creek or tidal river for exporting from place other than customs port or customs station.

(d) Goods attempted to be exported contrary to prohibition under custom Act or any other law

(e) Goods concealed in any conveyance brought within limits of customs area for exportation.

(f) Goods loaded or attempted to be loaded for eventual export out of India, without permission of proper officer, in contravention of section 33 and 34 of the customs Act, 1962.

(g) Goods stored at un-approved place or loaded without supervision of customs officer.

(h) Goods not mentioned or found excess of those mentioned in shipping Bill or declaration in respect of baggage –

  (i) Any goods entered for exportation not corresponding in respect of value or any other particulars in shipping Bill or declaration of contents of baggage

  (ii) Goods entered for Export under claim for duty drawback which do not correspond in any material particular with any information provided for fixation of duty drawback.

(i) Goods imported without duty but being re-exported under claim for duty drawback.

(j) Goods cleared for exportation which are not loaded on account of willful act, negligence or default, or goods unloaded after loading for exportation, without permission.

(k) Provision in respect of 'specified goods' are contravened.

SECTION - B

4.22 ANTI-DUMPING DUTY - AN OVERVIEW

Trade Protection Measures under WTO

Under the WTO regime, international trade has been liberalized allowing free movement of goods and services between member countries by eliminating tariff and non-tariff barriers to a large extent. The liberalization has further being extended in cross-border transactions at regional levels by entering into various regional preferential trade agreements.

With the present low rate of import duty, a small deviation from fair trade practice on the part of the exporter or subsidy offered by exporting country will make it difficult for domestic industries to compete with imported products which are like products to the products manufactured by domestic industry.

The WTO agreements as an exceptional measure, depending upon the situation permit product specific imposition of Anti-dumping duty, safeguards duty and countervailing duty as the case may be for the protection of domestic industry from the injury caused by imported goods.

These three duties are exceptional in nature and are imposed on three different mutually exclusive conditions.

Basis of distinction	Anti-Dumping Duty	Countervailing Duty	Safeguard Duty
Applicability	Export Price < Price normally charged in domestic/home market	Exporting Government is giving subsidy to exporter in that foreign land for the purpose of exporting	In a situation, when there is a sudden and sharp increase in imports as a result of unforeseen developments causing injury to domestic industry
Act of conflict that leads to imposition	Alleged foul play on the part of the exporter	An alleged foul play on the part of the exporting country	Imposed purely for the protection of domestic industry on a no fault principle where domestic industry is temporarily unable to compete with imported products on account of these unforeseen developments.
	Product-specific and exporter specific duty	Product-specific duty imposed against imports coming from all sources irrespective of the exporter and country of origin	
Tenure of applicability	It can continue as long as dumping continues	It can also continue forever as long as subsidy continues	It can continue only for a temporary period not exceeding 10 years.

4.22.1 Anti-Dumping

Dumping means export of goods by exporters of one country/territory to the market of another country/territory at a price lower than the price prevailing in the country of export and the difference in such price is called margin of dumping. This is an unfair trade practice which can have a distortive effect on international trade and needs to be condemned under WTO law.

Anti-dumping is a measure to rectify the trade distortive effect of dumping and re-establish fair trade, which is achieved by imposition of a duty on dumped imports, not exceeding the margin of dumping.

4.22.2 The Salient Features

i. It is an instrument for ensuring fair trade and is not a measure of protection per se for the domestic industry

ii. It provides relief to the domestic industry against the injury caused by dumping and gives domestic industry a level playing field.

iii. The duty is imposed as a deterrent effect to discourage dumped imports, so that users can buy material from domestic industry from whom they were not buying earlier on account of availability of cheap dumped imports.

iv. The idea is to levy and collect extra tax, rather to take the landed value of imports to a level where domestic industry can fairly compete with imports and sell the product in the domestic market.

4.22.3 Application of Anti-Dumping

i. The Anti-dumping duty is levied and collected as a duty of Customs and charged over and above the National Customs Duty chargeable on the import of the item.

ii. Anti-dumping duty is not creditable

iii. It will be charged as an extra cost on dumped imports.

4.22.4 Authority for Anti-dumping Action against Unfair Trade Practices

i. Anti-dumping measure in India are administered by the Directorate General of Anti-dumping and Allied Duties (DGAD) functioning in the Department of Commerce, Ministry of Commerce and Industry, which is headed by the "Designated Authority".

ii. The Designated Authority's function is to conduct the Anti-dumping investigation and make recommendation to the Government for imposition of Anti-dumping duty.

iii. Such duty is finally imposed/levied by a Notification of the Ministry of Finance.

4.22.5 Termination of Investigation under Anti-Dumping

The Designated Authority may suspend or terminate the investigation under Anti-dumping in the following cases:

(1) If there is a request in writing from the domestic industry at whose instance the investigation was initiated

(2) When there is no sufficient evidence of dumping or injury

(3) If the margin of dumping is less than 2% of the export price

(4) The volume of dumped imports from a country is less than 3% of the total imports of the like article imported into India, unless the volume of dumped imports collectively from all such countries who individually account for less than 3%, is not more than 7% of total imports

(5) If injury is negligible.

4.22.6 Terminologies Used

1. **Designated Authority:** It is the authority appointed by the Government of India to investigate the existence, degree and effect of any alleged dumping in relation to any import of any article.

2. **Period of Investigation (POI):** It refers to the specific period, during which there is an action and application of dumping, injury and there exists a casual link between such dumping and injury. It is a period of not less than six months and not more than eighteen months.

3. **Interested Party:** A party/exporter, which is going to be affected if duties are imposed after investigation and those who has an interest in the investigation, is called interested party. Basically, they are the stakeholders.

4. **The Product under Consideration (PUC) or Article under Investigation:** It refers to that imported product which is alleged to have been imported at dumped price and on which Anti-dumping duty is proposed to be levied.

5. **Like Product:** It is a product, which is identical, i.e. alike in all respects with reference to the 'product under consideration' or in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the 'product under consideration'.

6. **Domestic Industry:** It refers to the domestic producers as a whole of the like products or those producers whose collective output of the like products constitutes a major proportion of the total domestic production of like products.

7. **Normal Value:** It is the price of the product under consideration, in the ordinary course of trade, when destined for consumption in the exporting country market. Example: Product A is being imported from Country Z. The import price is ₹100 (without any element of duty, freight, insurance, etc) while the price of this product if sold in Country Z is ₹60. So, the normal value of the goods is ₹60, i.e. the price at which it would have been sold in the exporting country.

8. **Export Price:** The export price is the transaction price/value at which the foreign producer sells the product to an importer in the importing country. As per the example given in earlier paragraph, the export Price is ₹100.

9. **Dumping Margin/ Margin of Dumping (DM):** In reference to an article, it means the difference between the normal value and its export price. Example: if the normal value is ₹60 and the export price is ₹100. The Margin of Dumping = Export Price (-) Normal Value = ₹ (100 – 60) = ₹40.

10. **Non-market Economies (NME):** The economies, where the government has a complete or substantial monopoly of its trade or government has a significant role in fixation of domestic prices of inputs and finished goods, are called non-market economies.

11. **Non Injurious Price (NIP):** It is the sale price which is constructed (i.e. arrived at/ ascertained) for the domestic industry, which will give a reasonable return on investment and if Domestic Industry is able to sale its product at that price it will claim no injury.

12. **Landed value of imports:** This refers to cost of the goods imported including all the expenses incurred during the course of importation upto the port including non-creditable duties of customs.

13. **Injury Margin (IM):** This represents the difference between Non Injurious Price (NIP) and Landed Value of Imports.

14. **Price Undercutting (by imports):** Sale value of domestic industry at factory gate (net of taxes) [-] landed value of imports.

Example 37: Sale value of domestic industry at factory gate ₹120 (net of taxes). Landed Value of imports ₹90. Hence, Price under cutting = ₹120 (-) ₹90 = ₹30. This is positive undercutting. It creates pressure on domestic industry from imports, as the imported goods are sold at ₹90, which is less than the price charged by domestic industry.

On the contrary, if the Sale value of domestic industry at factory gate (net of taxes) is ₹100 and the Landed value of imports ₹115, then, Price under cutting = ₹100 (-) ₹115 = ₹(15). This is negative undercutting. The domestic industry is in a comfortable position, as the price of imports is more than the price charged by the domestic industry.

15. Price Underselling (by exporters): Non Injurious Price (NIP)of Domestic Industry (-) Landed Value of Imports.

Example 38: Let NIP ₹150, Landed value of imports ₹120. Then, the price underselling by exporters = ₹150 – ₹120 = ₹ 30.

A positive price underselling shows the inability of the domestic industry to sell its product at a price which is non-injurious to it on account of pressure from imports coming into the country

On the contrary, if the NIP is ₹120 and the Landed value of imports ₹140, then the price underselling by exporters = ₹120 (-) ₹140 = ₹(20). This negative price underselling represents a comfortable position for the domestic industry, as the price of its products is lower than imported goods.

16. **Provisional Duty:** It is the duty which is levied/ imposed by the Central Government by a notification based on preliminary findings of Designated Authority, in a case, where a full-fledged investigation is pending.

17. **Final Duty:** It is the duty of Anti-dumping imposed by Central Government by a notification after completion of investigation.

18. **Circumvention of Duty:** When Anti-dumping Duty imposed on a product is being bypassed by exporters or importers by some malpractices like changing the description of product or by import of the product in an unassembled or disassembled form or by changing the country of origin of the product, it is construed that there is a circumvention of duty. In simple words, this is an act of evasion of duty by unfair trade practices.

19. **De-minimis margin of dumping:** Any exporter whose margin of dumping is less than 2% of the export price shall be excluded from the purview of anti-dumping duties. Example: Landed Value of Imports ₹100. Sale Price of like products in domestic market ₹ 101.50. Now, there is a margin of dumping to the extent of ₹ 1.50 (= ₹ 101.50 – ₹ 100). Since the margin of dumping ₹ 1.50 as a percentage on Landed value of imports (₹ 100) is measured to be 1.5%, hence the rule of de-minimis margin of dumping is applicable, and as the tolerance/deviation is less than 2%. Hence, this is not a case to be reviewed under Anti-dumping laws in India.

20. **De-minimus imports:** If the volume of dumped imports, actual or potential, from a particular country accounts for less than 3% of the total imports of the like products, then investigation under Anti-dumping laws should be suspended. However, in such a case, the cumulative imports of the like product from all these countries who individually account for less than 3% should not exceed 7% of the import of the like product.

4.22.7 Principles Governing the Determination of Normal Value, Export Price and Margin of Dumping

The designated authority while determining the normal value, export price and margin of dumping shall take into account inter alia, the following principles-

(1) The elements of costs referred to in the context of determination of normal value shall normally be determined on the basis of records kept by the exporter or producer under investigation, provided such records are in accordance with the generally accepted accounting principles of the exporting country, and such records reasonably reflect the cost associated with production and sale of the article under consideration.

(2) Sales of the like product in the domestic market of The exporting country, or sales to a third country at prices below per unit(fixed and variable) costs of production plus administrative, selling and general costs may be treated as not being in the ordinary course of trade by reason of price. The designated authority may disregard these sales, in determining normal value provided it has determined that:

    (i) such sales are made within a reasonable period of time (not less than six months) in substantial quantities, i.e. when the weighted average selling price of the article is below the weighted average per unit costs or when the volume of the sales below per unit costs represents not less than twenty per cent of the volume sold in transactions under consideration, and

(ii) such sales are at prices which do not provided for the recovery of all costs within a reasonable period of time.

(3) The said prices will be considered to provide for recovery of costs within a reasonable period of time if they are above weighted average per unit costs for the period of investigation, even though they might have been below per unit costs at the time of sale.

(i) The said authority in the course of investigation shall consider all available evidence on the proper allocation of costs, including that which is made available by the exporter or producer provided that such allocation has been historically utilized by the exporter or producer, in relation to establishing appropriate amortization and depreciation periods and allowances for capital expenditure and other development costs.

(ii) unless already reflected in allocation of costs referred to in clause(1) and sub-clause(i) above, the designated authority, will also make appropriate adjustments for those non-recurring items of cost which benefits further and/or current production, or for circumstances in which costs during the period of investigation are affected by start-up operation.

(4) The amounts for administrative, selling and general costs and for profits as referred to in sub-section(1) of section 9A of the Act, shall be based on actual data pertaining to production and sales in the ordinary course of trade, of the like article by the exporter or producer under investigation. When such amounts cannot be determined on this basis, the amounts may be determined on the basis of:

(i) the actual amount incurred and realise by the exporter or producer in question, in respect of production and sales in the domestic market of the country of origin of the same general category of article;

(ii) the weighted average of the actual amounts incurred and realized by other exporters or producers subject to investigation in respect of production and sales of the like article in the domestic market of the country of origin; or

(iii) any other reasonable method, provided that the amount for profit so established shall not exceed the profit normally realized by the exporters or producers on sales of products of the same general category in the domestic market of the country of origin.

(5) The designated authority, while arriving at a Constructed export price, shall give due allowance for costs including duties and taxes, incurred between importation and resale and for profits.

(6) (i) While arriving at margin of dumping the designated authority shall make a fair comparison between the export price and the normal value. The comparison shall be made at the same level of trade, normally at the ex- factory level, and in respect of sales made at as nearly as possible the same time. Due allowance shall be made in each case, on its merits, for differences which affect price comparability, including differences in conditions and terms of sale, taxation, levels of trade, quantities, physical characteristics, and any other differences which are demonstrated to affect price comparability.

(ii) In the cases where export price is a constructed price, the comparison shall be made only after establishing the normal value at equivalent level of trade.

(iii) When the comparison under this para requires a conversion of currencies, such conversion should be made by using the rate of exchange on the date of sale, provided that when a sale on foreign currency on forward markets is directly linked to the export sale involved the rate of exchange in the forward sale shall be used. Fluctuations in exchange rates shall be ignored and in an investigation the exporters shall be given at least sixty days to have adjusted their export prices to reflect sustained movements in exchange rates during the period of investigation.

(iv) Subject to the provisions governing comparison in this paragraph, the existence of margin of dumping during the investigation phase shall normally be established on the basis of a comparison of a weighted average normal value and export prices on a transaction-to-transaction basis. A normal value established on a weighted average basis may be compared to prices of individual export transactions if it is found that a pattern of export prices which differ significantly among different purchasers, regions or time period and if an explanation is provided as to why such differences cannot be taken into account appropriately by the use of a weighted average-to -weighted average or transaction-to-transaction comparison.

(7) In case of imports from non-market economy countries, normal value shall be determined on the basis of the price or constructed value in a market economy third country, or the price from such a third country to other countries, including India, or where it is not possible, on any other reasonable basis, including the price actually paid or payable in India for the like product, duly adjusted if necessary, to include a reasonable profit margin. An appropriate market economy third country shall be selected by the designated authority in a reasonable manner and due account shall be taken of any reliable information made available at the time of the selection. Account shall also be taken within time limits; where appropriate, of the investigation if any made in similar matter in respect of any other market economy third country. The parties to the investigation shall be informed without unreasonable delay the aforesaid selection of the market economy third country and shall be given a reasonable period of time to offer their comments.

4.22.8 Principles governing investigations

(1) The designated authority shall, after it has decided to initiate investigation to determine the existence, degree and effect of any alleged dumping of any article, issue a public notice notifying its decision and such public notice shall, inter alia, contain adequate information on the following :-

(i) the name of the exporting country or countries and the article involved;

(ii) the date of initiation of the investigation;

(iii) the basis on which dumping is alleged in the application;

(iv) a summary of the factors on which the allegation of injury is based;

(v) the address to which representations by interested parties should be directed; and

(vi) the time-limits allowed to interested parties for making their views known.

(2) A copy of the public notice shall be forwarded by the designated authority to the known exporters of the article alleged to have been dumped, the Governments of the exporting countries concerned and other interested parties.

(3) The designated authority shall also provide a copy of the application referred to in sub-rule (1) of Rule 5 to -

(i) the known exporters or to the concerned trade association where the number of exporters is large, and

(ii) the governments of the exporting countries : Provided that the designated authority shall also make available a copy of the application to any other interested party who makes a request therefore in writing.

(4) The designated authority may issue a notice calling for any information, in such form as may be specified by it, from the exporters, foreign producers and other interested parties and such information shall be furnished by such persons in writing within thirty days from the date of receipt of the notice or within such extended period as the designated authority may allow on sufficient cause being shown.

Explanation:

For the purpose of this sub-rule, the notice calling for information and other documents shall be deemed to have been received one week from the date on which it was sent by the designated authority or transmitted to the appropriate diplomatic representative of the exporting country.

(5) The designated authority shall also provide opportunity to the industrial users of the article under investigation, and to representative consumer organizations in cases where the article is commonly sold at the retail level, to furnish information which is relevant to the investigation regarding dumping, injury where applicable, and causality.

(6) The designated authority may allow an interested party or its representative to present the information relevant to the investigation orally but such oral information shall be taken into consideration by the designated authority only when it is subsequently reproduced in writing.

(7) The designated authority shall make available the evidence presented to it by one interested party to the other interested parties, participating in the investigation.

(8) In a case where an interested party refuses access to, or otherwise does not provide necessary information within a reasonable period, or significantly impedes the investigation, the designated authority may record its findings on the basis of the facts available to it and make such recommendations to the Central Government as it deems fit under such circumstances.

4.22.9 Principles for determination of non-injurious price [Rule 17(1)]

(1) The designated authority is required under sub-rule (1) of rule 17 to recommend the amount of anti-dumping duty which, if levied, would remove the injury where applicable to the domestic industry.

(2) For the purpose of making recommendation under clause (1), the designated authority shall determine the fair selling (notional) price or non-injurious price of the like domestic product taking into account the principles specified herein under.

(3) The non-injurious price is required to be determined by considering the information or data relating to cost of production for the period of investigation in respect of the producers constituting domestic industry. Detailed analysis or examination and reconciliation of the financial and cost records maintained by the constituents of the domestic industry are to be carried out for this purpose.

(4) The following elements of cost of production are required to be examined for working out the noninjurious price, namely: —

   (i) The best utilisation of raw materials by the constituents of domestic industry, over the past three years period and the period of investigation, and at period of investigation rates may be considered to nullify injury, if any, caused to the domestic industry by inefficient utilisation of raw materials.

   (ii) The best utilisation of utilities by the constituents of domestic industry, over the past three years period and period of investigation, and at period of investigation rates may be considered to nullify injury, if any, caused to the domestic industry by inefficient utilization of utilities.

   (iii) The best utilisation of production capacities, over the past three years period and period of investigation, and at period of investigation rates may be considered to nullify injury, if any, caused to the domestic industry by inefficient utilization of production capacities.

   (iv) The Propriety of all expenses, grouped and charged to the cost of production may be examined and any extra-ordinary or non-recurring expenses shall not be charged to the cost of production and salary and wages paid per employee and per month may also be reviewed and reconciled with the financial and cost records of the company.

   (v) To ensure the reasonableness of amount of depreciation charged to cost of production, it may be examined that no charge has been made for facilities not deployed on the production of the subject goods, particularly in respect of multi-product companies and the depreciation of re-valued assets, if any, may be identified and excluded while arriving at reasonable cost of production.

(vi) The expenses to the extent identified to the product are to be directly allocated and common expenses or overheads classified under factory, administrative and selling overheads may be apportioned on reasonable and scientific basis such as machine hours, vessel occupancy hours, direct labour hours, production quantity, sales value, etc., as applied consistently by domestic producers and the reasonableness and justification of various expenses claimed for the period of investigation may be examined and scrutinised by comparing with the corresponding amounts in the immediate preceding year.

(vii) The expenses, which shall not to be considered while assessing non-injurious price include,—

a) research and development Provisions (unless claimed and substantiated as related to the product specific research);

b) since non-injurious price is determined at ex-factory level, the post manufacturing expenses such as commission, discount, freight- outward etc. at ex-factory level;

c) excise duty, sales tax and other tax levies on sales;

d) expenses on job work done for other units;

e) royalty, unless it is related to technical know-how for the product;

f) trading activity of product under consideration; or

g) other non-cost items like bad debts, donations, loss on sale of assets, loss due to fire, flood, etc.

(viii) A reasonable return (pre-tax) on average capital employed for the product may be allowed for recovery of interest, corporate tax and profit. The average capital employed is the sum of "net fixed assets and net working capital which shall be taken on the basis of average of the same as on the beginning and at the end of period of investigation. For assessment of reasonable level of working capital requirement, all the elements of net working capital shall be scrutinized in detail. The impact of revaluation of fixed assets shall not be considered in the calculation of capital employed. Interest is allowed as an item of cost of sales and after deducting the interest, the balance amount of return is to be allowed as pre-tax profit to arrive at the non- injurious price.

(ix) Reasonableness of interest cost may be examined to ensure that no abnormal expenditure on account of interest has been incurred. Details of term loans, cash credit limits, short term loans, deposits and other borrowings taken by the company and interest paid thereon may be examined in detail along with the details of assets deployed.

(x) In case there is more than one domestic producer, the weighted averages of non-injurious price of individual domestic producers are to be considered. The respective share of domestic production of the subject goods may be taken as basis for computation of weighted average non-injurious price for the domestic industry as a whole".

4.22.10 Anti-dumping Application Proforma -

The following is an outline of application proforma under Anti-dumping laws in India:-

Part	Deals with
I	Imported Product Information
II	Indian Industry Profile
III	Evidence of Dumping 1. Estimates of Normal Value 2. Estimates of Export Price 3. Estimates of Dumping Margin
IV	Evidence of Injury
IVA	Injury Information on Domestic Industry
IVB	Country wise landed value
V	Evidence of Casual link
VI	Costing Information Format "A" – Statement of Raw Materials and Packing Materials Consumption and Reconciliation Format "B" – Statement of Raw Material Consumption Format "CI" - Statement of Cost of Production Format "CII" – Allocation and Apportionment of Expenditure Format "D" – Statement of Consumption of Utilities Format "E" – Statement of Sales Relations Format "F" – Certificate

4.22.11 Relevance of Cost Information for imposing anti dumping duty

(1) Description of the cost accounting system used by the company to record the production costs of the product concerned.

(2) Company's use of standard or budgeted costs.

(3) An explanation for allocation method used as well as for any significant or unusual cost-variances that occurred during investigation period.

(4) A list of direct and indirect cost centres.

(5) Method used to allocate cost among the company's organizational units.

(6) Description of Cost Accounting system to value the cost of sales and raw materials, WIP and finished goods inventories for the audited financial statements.

(7) A list of all costs which are valued and treated differently for cost and financial accounting purposes and the reasons treating them differently.

(8) Information regarding cost of production/trading.

4.22.12 Cost Accounting Standards (CASs) - relevance and application in the light of Anti-dumping Laws in India

The following are the Cost Accounting Standards issued by the Institute of Cost Accountants of India. Effective application of CASs brings about uniformity in the principles of measurement and valuation of goods.

CAS	Deals with
1	Classification of Cost
2	Capacity Determination
3	Overheads
4	Cost of Production for Captive consumption
5	Average (Equalized) cost of transportation
6	Material Cost
7	Employee Cost
8	Cost of Utilities
9	Packing Material Cost
10	Direct Expenses
11	Administrative Overheads
12	Repairs and Maintenance
13	Cost of Service Cost Centre
14	Pollution Control Cost
15	Selling and Distribution Overheads
16	Depreciation and Amortization
17	Interest and Financing Charges
18	Research and Development Costs
19	Joint Costs
20	Royalty and Technical Know-how Fee
21	Quality Control
22	Manufacturing Cost

4.22.13 Relevance of Cost Records

"***Cost Records** means books of accounts relating to utilization of material, labour and other items of cost as applicable to the production, processing, manufacturing and mining activities of the company*". It has also been clarified that such conformance to Generally Accepted Cost Accounting Principles (GACAP) and Cost Accounting Standards (CAS) are to be followed to the extent these are found to be relevant and applicable and the variations, if any, are required to be indicated and explained.

The basic purpose of maintenance of these cost records is to enable the company to exercise, as far as possible, control over the various operations and costs with a view to achieve optimum economies in utilization of resources. These records shall also provide necessary data which is required to be furnished under these rules.

4.22.14 Companies (Cost Records and Audit) Rules, 2014 - relevance and application in the light of Anti-dumping Laws in India

The following states the relevance of respective Para prescribed Cost Audit Reports and Cost Accounting Standards which may be used as reference for making an authentic assessment under Anti-dumping laws in India. Since the Cost Accounting Records are to be maintained by companies satisfying the prescribed parameters, a reference to the Cost Compliance Report or the Cost Audit Report may be an important tool for the stakeholders in ascertainment of injury margin. Further, application of generally accepted cost accounting principles and cost accounting standards would bring about a uniformity/standardization in the principles followed in measurement and valuation of cost.

<table>
<tr><th>Anti-dumping Application Proforma</th><th colspan="2">Reference to Para prescribed under Cost Audit Report Rules,2014
(Para Reference to CRA 3)</th><th>Reference to relevant Cost Accounting Standards</th></tr>
<tr><td rowspan="2">Format A - Statement of Raw Materials and Packing Materials Consumption and Reconciliation</td><td>Annexure 2A
- Details of Materials Consumed</td><td>Item No.1 & 2
Raw Material Consumption and Process Materials</td><td>CAS 6 – Material Cost</td></tr>
<tr><td>Annexure 2
- Abridged Cost Statement</td><td>Item No.16 and 23 – Primary Packing Cost Material and Secondary Packing Cost</td><td>CAS 9 – Packing Material Cost</td></tr>
<tr><td>Format B – Statement of Raw Material Consumption</td><td colspan="2">Annexure 2A
- Details of Materials Consumed</td><td>CAS – 6 – Material Cost</td></tr>
<tr><td>Format CI – Statement of Cost of Production

(to be certified by a Cost Accountant in Practice)</td><td colspan="2">Annexure 2A
- Details of Materials Consumed
Annexure 1 - Quantitative information
Annexure 2 - Abridged Cost Statement
Annexure 2B - Details of Utilities consumed</td><td>CAS 2 – Capacity Determination
CAS 6 – Material Cost
CAS 7 – Employee Cost
CAS 8 – Cost of Utilities
CAS 9 – Packing Material Cost
CAS 10 – Direct Expenses
CAS 12 – Repairs & Maintenance</td></tr>
<tr><td>Format CII – Allocation and Apportionment of Expenditure</td><td colspan="2">Annexure 1 - Quantitative information
Annexure 2 - Abridged Cost Statement</td><td>CAS 1 – Classification of Cost
CAS 2 – Capacity Determination
CAS 3 - Overheads</td></tr>
<tr><td>Format D – Statement of Consumption of Utilities</td><td colspan="2">Annexure 2B - Details of Utilities consumed</td><td>CAS 8 – Cost of Utilities</td></tr>
</table>

However, for the purpose of ascertaining the Normal Value, Non-injurious price or to determine price undercutting or price underselling, application of the specific Cost Accounting Standards in all relevant situations may be made which would be a safeguard for the stakeholders.

Illustration 1:

Example 37: FORMAT "CI" - STATEMENT OF COST OF PRODUCTION
Name of the Company: XYZ Limited

Installed Capacity	1,00,000 units							
Production in Installed capacity	65,000 units							
Capacity Utilization (%)	65%							
Production in Investigation Period	56,000 units							
Capacity Utilisation in Investigation period	56%							
Sales (quantity)	61,000 units				51,000 units			
Particulars	**Previous Accounting Year**				**Investigating Period**			
	Qty	Rate (₹)	Value (₹)	Cost per unit (₹)	Qty	Rate (₹)	Value (₹)	Cost per unit (₹)
Manufacturing Expenses: Raw Materials (specify the major raw materials) (MT) Utilities Depreciation Others (specify nature of expenditure)	 10,000	 100.00	 10,00,000 2,00,000 1,95,000	 15.38 3.08 3.00	 8,000	 120.00	 9,60,000 1,90,000 1,75,000	 17.14 3.39 3.13
Administrative Expenses Variable Fixed			 1,30,000 78,000	 2.00 1.20			 1,12,000 78,000	 2.00 1.39
Selling & Distribution Expenses Variable Fixed			 61,000 40,000	 1.00 0.62			 56,000 40,000	 1.10 0.71
Financial Expenses Variable Fixed			 1,30,000 21,000	 2.13 0.32			 35,700 21,000	 0.70 0.38
Less: Miscellaneous Income (from product concerned) – Sale of Scrap raw materials			(25,000)				(20,000)	
Total Cost to make and sell			**18,30,000**	**28.15**			**16,47,700**	**29.42**
Selling Price				**35.00**				**32.00**
Profit/Loss				**6.85**				**2.58**

Note: This Statement of Cost of Production is to be authenticated by a Cost Accountant in Practice

Example 38:

One of the major reasons for this decrease in the quantity of sales is identified to be import of like/similar goods by a foreign company to India. The selling price of such goods, in Indian market, as fixed by the foreign counterpart is ₹ 23, while the same goods are normally sold at that foreign country for ₹ 35. Landed Value of Imports ₹ 25. XYZ Ltd. being deceived requested the competent authority to have a review. Ascertain the injury margin and suggest the measure suitable to safeguard the Indian Industry.

Answer:

Particulars	Amount (₹)
Price of the "Product under Consideration (PUC) or "Article under Investigation" from the Exporting Country / Export Price	23.00
Normal Value of such product, when sold in the domestic market of the exporting country	35.00
Dumping Margin or Margin of Dumping (DM) = 35.00 – 25.00	10.00
Non Injurious Price (NIP) – this is the constructed sale price of the domestic industry which will give a reasonable return on investment and if the domestic industry is able to sale its product at that price, it will not claim any injury	30.00 (say)
Landed Value of Imports (including all the expenses incurred during the course of importation upto the port including the non-creditable duties of customs	25.00
Injury Margin (IM) = Non Injurious Price (-) Landed Value of Imports = 30.00 (-) 25.00	5.00

Thus, for XYZ Ltd. the Injury Margin is ascertained at ₹ 5 per unit. Accordingly, the Authorities shall cause to initiate necessary proceedings to levy additional duty of customs (under the aegis of Anti-dumping Laws) to safeguard the domestic industry.

Example 39: Following is the relevant extract from the Trial Balance of ABC Ltd. for the year ended 31.3.2015.

Particulars	Amount (₹)	Particulars	Amount (₹)
Raw Materials	5,00,000	Sales	10,95,000
Consumable Stores and Spares (Other Inputs)	3,00,000	Other Income	3,000
Utilities (Power, Fuel, Steam, Water, etc)	1,80,000		
Direct Labour	4,00,000		
Manufacturing Overheads	1,50,000		
Research & Development	60,000		
Administrative Overheads	90,000		
Selling & Distribution Cost	50,000		
Depreciation	30,000		
Financial expenses	10,000		
Other Miscellaneous Expenses	12,000		

Company deals with two products for which necessary information is furnished:

Particulars of Expenses	Product X_1	Product X_2
Raw Materials (Ratio of utilization)	60%	40%
Consumable Stores and Spares (Other Inputs)	in proportion to raw materials	
Utilities (Power, Fuel, Steam, Water, etc)	in proportion to raw materials	
Direct Labour	₹ 2,45,000	₹ 1,55,000
Manufacturing Overheads	30%	35%
Research & Development	35%	40%
Administrative Overheads	30%	40%
Selling & Distribution Cost	35%	50%
Depreciation	45%	55%
Financial expenses	50%	30%
Other Miscellaneous Expenses	25%	25%

Prepare Statement showing Allocation and Apportionment of Expenditure for assessment under Anti-dumping laws in India for Product X_1, which is the Product under Investigation.

Answer:

Format CII

Statement Showing Allocation and Apportionment of Expenditure for Product X_1

Sl. No.	Particulars of expenses	Total applicable to product under investigation	Share applicable to product under investigation	Share not allocation/ apportionment	Basis
1	Raw Materials (Ratio of utilization)	3,00,000	3,00,000	NIL	Actual Ratio
2	Consumable Stores and Spares (Other Inputs)	1,80,000	1,80,000	NIL	Raw Material Ratio
3	Utilities (Power, Fuel, Steam, Water, etc)	1,08,000	1,02,000	6,000	CAS 8
4	Direct Labour	2,45,000	2,41,000	4,000	CAS – 7 (Actual)
5	Manufacturing Overheads	45,000	38,000	7,000	Cost Driver
6	Research & Development	21,000	15,000	6,000	Wrong Basis
7	Administrative Overheads	27,000	24,000	3,000	CAS - 11
8	Selling & Distribution Cost	17,500	16,000	1,500	CAS -15

9	Depreciation	13,500	11,500	2,000	CAS-16, Value of Asset
10	Financial expenses	5,000	5,000	NIL	CAS-17, Actual utilization of borrowed funds
11	Other Miscellaneous Expenses	3,000	3,000	NIL	Actual
12	**Total Expenditure Total of (1) to (11)**	**9,65,000**	**9,35,500**	**29,500**	
13	Sales	10,95,000	10,95,000	NIL	
14	Other Income (Sale of Scrap of Product X_1)	3,000	3,000	NIL	
15	**Total Income (13+14)**	**10,98,000**	**10,98,000**	**NIL**	
16	**Profit/Loss**	**1,33,000**	**1,33,000**		

Note:

This statement is to be certified by a Practicing Cost Accountant.

Study Note - 5

FOREIGN TRADE POLICY

This Study Note includes

Foreign Trade Policy (FTP) is a set of guidelines or instructions or procedures or regularly requirements —

- issued or laid down by the Central Government
- in matters related to foreign trade viz. IMPORT/EXPORT OF GOODS OR SERVICES into, or from, India.

Need of Foreign Trade Policy: The foreign trade policy is needed to regulate the foreign trade. The FTP, in general, aims at -

(i) developing export potential,

(ii) improving export performance,

(iii) encouraging foreign trade,

(iv) creating favorable balance of payments position,

(v) improving efficiency and competitiveness of the Indian industries, etc.,

(vi) create self-reliance and self-sufficiency,

(vii) Ensure export led growth.

Legislation Governing Foreign Trade: The main legislation concerning foreign trade is the Foreign Trade (Development and Regulation) Act, 1992 [FT (D&R) Act], which replaced the earlier Import and Export (Control) Act, 1947.

FT (D&R) Act, confers powers on the Union Ministry of Commerce and Industry, Government of India to -

(a) make provisions for facilitating and controlling foreign trade;

(b) prohibit, restrict and regulate exports and imports, in all or specified cases as well as subject them to exemptions;

(c) formulate and announce an export and import policy and also amend the same from time to time, by notification in the Official Gazette;

(d) appoint a 'Director General of Foreign Trade' for the purpose of the Act, including formulation and implementation of the export-import policy.

The details of FTP 2015-2020 are discussed in following paragraphs.

5.1 LEGAL FRAMEWORK AND TRADE FACILITATION

A. LEGAL FRAMEWORK

Legal Basis of Foreign Trade Policy (FTP)

The Foreign Trade Policy, 2015-20, is notified by Central Government, in exercise of powers conferred under Section 5 of the Foreign Trade (Development & Regulation) Act, 1992 (No. 22 of 1992) [FT (D&R) Act], as amended.

Duration of FTP

The Foreign Trade Policy (FTP), 2015-2020, incorporating provisions relating to export and import of goods and services, shall come into force with effect from the date of notification and shall remain in force up to 31st March, 2020, unless otherwise specified. All exports and imports made upto the date of notification shall, accordingly, be governed by the relevant FTP, unless otherwise specified.

Amendment to FTP

Central Government, in exercise of powers conferred by Section 5 of FT (D&R) Act, 1992, as amended from time to time, reserves the right to make any amendment to the FTP, by means of notification, in public interest.

Hand Book of Procedures (HBP) and Appendices & Aayat Niryat Forms (AANF):

Director General of Foreign Trade (DGFT) may, by means of a Public Notice, notify Hand Book of Procedures, including Appendices and Aayat Niryat Forms or amendment thereto, if any, laying down the procedure to be followed by an exporter or importer or by any Licensing/Regional Authority or by any other authority for purposes of implementing provisions of FT (D&R) Act, the Rules and the Orders made there under and provisions of FTP.

Specific provision to prevail over the general

Where a specific provision is spelt out in the FTP/Hand Book of Procedures (HBP), the same shall prevail over the general provision.

Transitional Arrangements

(a) Any License / Authorisation / Certificate / Scrip / any instrument bestowing financial or fiscal benefit issued before commencement of FTP 2015-20 shall continue to be valid for the purpose and duration for which such License/Authorisation/ Certificate / Scrip / any instrument bestowing financial or fiscal benefit Authorisation was issued, unless otherwise stipulated.

(b) In case an export or import that is permitted freely under FTP is subsequently subjected to any restriction or regulation, such export or import will ordinarily be permitted, notwithstanding such restriction or regulation, unless otherwise stipulated. This is subject to the condition that the shipment of export or import is made within the original validity period of an irrevocable commercial letter of credit, established before the date of imposition of such restriction and it shall be restricted to the balance value and quantity available and time period of such irrevocable letter of credit. For operationalising such irrevocable letter of credit, the applicant shall have to register the Letter of Credit with jurisdictional Regional Authority (RA) against computerized receipt, within 15 days of the imposition of any such restriction or regulation.

B. TRADE FACILITATION & EASE OF DOING BUSINESS

Objective

Trade facilitation is a priority of the Government for cutting down the transaction cost and time, thereby rendering Indian exports more competitive. The various provisions of FTP and measures taken by the Government in the direction of trade facilitation are consolidated under this chapter for the benefit of stakeholders of import and export trade.

DGFT as a facilitator of exports/imports

DGFT has a commitment to function as a facilitator of exports and imports. Focus is on good governance, which depends on efficient, transparent and accountable delivery systems. In order to facilitate international trade, DGFT consults various Export Promotion Councils as well as Trade and Industry bodies from time to time.

Niryat Bandhu - Hand Holding Scheme for new export / import entrepreneurs

(a) DGFT is implementing the Niryat Bandhu Scheme for mentoring new and potential exporter on the intricacies of foreign trade through counselling, training and outreach programmes.

(b) Considering the strategic significance of small and medium scale enterprises in the manufacturing sector and in employment generation, 'MSME clusters' have been identified, based on the export potential of the product and the density of industries in the cluster, for focussed interventions to boost exports.

(c) Outreach activities shall be organized in a structured way with the help of Export Promotion Councils as 'industry partners' and other willing 'knowledge partners' in academia and research community to achieve the objective of Niryat Bandhu Scheme. Further, in order to ensure optimum utilization of resources, efforts would be made to associate all the stakeholders, including Customs, ECGC, Banks and concerned Ministries.

Citizen's Charter

DGFT has in place a Citizen's Charter, giving time schedules for providing various services to clients.

Online Complaint Registration and Monitoring System

An EDI Help Desk is available to assist the exporters in filing online applications on the DGFT portal and resolving other EDI related issues. For assistance an email may be sent at dgftedi@nic.in or Toll Free number 1800111550 can be used. Help Desk facility is also operational at the 4 DGFT Zonal Offices (details at http://dgft.gov.in). An Online Complaint registration and monitoring system allows users to register complaint and receive status/ reply online (details are at http://dgft.gov.in).

Issue of e-IEC (Electronic-Importer Exporter Code)

(a) Importer Exporter Code (IEC) is mandatory for export/import from/to India as detailed in paragraph 2.05 of this Policy. DGFT has recently introduced the facility of issuing Importer Exporter Code in electronic form (e-IEC). For issuance of e-IEC an application can be made online on DGFT website (http//:dgft.gov.in). Applicants can upload the documents and pay the required fee through Net banking.

(b) Processing of such applications by Regional Authority (RAs) of DGFT would be done online and a digitally signed e-IEC would normally be issued/ e-mailed to the applicant within 2 working days.

(c) In case the application is incomplete or otherwise ineligible, the same shall be rejected and a Rejection letter/email (with reasons for rejection) would be sent to the applicant.

(d) Application for issue of e-IEC can also be made from eBiz platform (https://www.ebiz.gov.in).

e-BRC

One prominent initiative in recent times has been the e-BRC (Electronic Bank Realisation Certificate) project and its successful implementation by DGFT. It has enabled DGFT to capture details of realisation of export proceeds directly from the Banks through secured electronic mode. This has facilitated the implementation of various export promotion schemes without any physical interface with the stake holders. So far more than one crore e-BRCs have been captured by this system.

MoU with State Governments for sharing of e-BRC data

MoU has been signed with state governments for sharing of e-BRC data to facilitate refund of VAT by the state governments to exporters. MoU has also been signed with Enforcement Directorate.

Exporter Importer Profile

An electronic procedure has been created to upload various documents in exporter importer profile. Once uploaded, there will be no need to submit these documents / copies of these documents to Regional Authority repeatedly with each application. It intends to reduce the transaction cost and time and is a step towards paperless processing of different applications in DGFT.

Reduction in mandatory documents required for Export and Import

The number of mandatory documents required for exports and imports of goods from/into India have been reduced to three each, as prescribed under paragraph heading, "Mandatory documents for export/import of goods from / into India."

Facility of online filing of applications

All the Regional Authorities (RA) of DGFT and extension counters have been networked with high speed internet. The applications are received and processed electronically. DGFT under the EDI initiatives has provided the facility of on line filing of applications to obtain Importer Exporter Code and various authorizations /scrips. DGFT is one of the first digital signature enabled organisation of the Government of India (GOI), which has introduced a higher level of Encrypted 2048 bit digital signature. There is a web interface for online filing of application after accessing DGFT website (http://dgft.gov.in). The application can be filed by exporter/CHA sitting at home or office in 24X7 environment. Application fee can also be paid online from linked banks. Efforts are being made to allow payment by debit/ credit cards as well. The applications are signed with a digital signature and submitted electronically to the concerned Regional Authority of DGFT, which are then processed on computer by the Regional Authority and authorisations/scrips are issued. Online filing has minimized the physical interface.

Online Inter-ministerial consultation

Presently, the exporters are required to file applications online on the website of DGFT under the Icon E-COM and are required to submit the duly signed and stamped printout of the online application along with all the necessary documents viz. technical specifications, literature etc. Now, a facility is being provided to upload copies of all the required documents including technical specifications, literature etc in PDF/JPG/JPEG/GIF format in the online filing system in respect of (a) Fixation of norms under Advance Authorisation by Norms Committees (b) Export of Restricted Items (c) Import of Restricted Items (d) SCOMET Items. The exporters would not be required to submit the hard copy of application except architectural drawings, machine drawings etc which may be difficult to scan and upload. The processing of the applications will also be done online.

Facility to upload documents by Chartered Accountant / Company Secretary / Cost Accountant

In order to move towards paperless processing, an electronic procedure is being developed to upload digitally signed documents by Chartered Accountant / Company Secretary / Cost Accountant. To start with, this facility would be created for Export From India Schemes. Such documents like Annexure Attached to ANF 3B, ANF 3C and ANF 3D, which are at present signed by these signatories, can be facilitated by this procedure. Exporter shall link digitally uploaded annexure with his online applications after creation of such facility. These facilities may be extended in phased manner to upload documents pertaining to other schemes like Advance Authorisation, DFIA and EPCG.

Electronic Data Interchange (EDI)

DGFT has put in place a robust EDI system for the purpose of export facilitation and good governance. DGFT has set up a secured EDI message exchange system for various documentation related activities including import and export authorizations established with other administrative departments, namely, Customs, Banks and EPCs. This has reduced the physical interface of exporters and importers with the Government Departments and is a significant measure in the direction of reduction of transaction cost. The endeavour of DGFT has been to enlarge the scope of EDI to achieve higher level of integration with partner departments.

Message Exchange with Community partners

Customs, Banks, Export Promotion Councils (EPCs) are major community partners of DGFT for message exchange. An effective message exchange system is in place with various community partners which is as follows:

(a) **Message Exchange with Customs**

(i) Importer Exporter Code Number.

(ii) Authorisations/Scrips for DFIA, AA, EPCG.

(iii) Shipping Bills for Duty Free Import Authorisation (DFIA), Advance Authorisation (AA), Export Promotion Capital Goods (EPCG), Reward Scrips.

(b) **Message Exchange with eBiz (https://www.ebiz.gov.in)**

(i) Application for Importer Exporter Code Number

(ii) Application for e-IEC.

(c) **Message Exchange with Banks**

(i) Application Fee

(ii) electronic Bank Realisation Certificate (e-BRC) data

(d) **Message Exchange with EPCs**

Registration cum Membership Certificate (RCMC) data.

Encouraging development of Third Party API

DGFT will encourage development of third party software for integration with its system to offer users multiple options for interfacing with the DGFT.

Forthcoming e-Governance Initiatives

DGFT is currently working on the following EDI initiatives:

(i) Message exchange for transmission of export reward scrips from DGFT to Customs.

(ii) Message exchange for transmission of Bills of Entry (import details) from Customs to DGFT.

(iii) Online issuance of Export Obligation Discharge Certificate (EODC).

(iv) Message exchange with Ministry of Corporate Affairs for CIN & DIN information.

(v) Message exchange with CBDT for PAN.

(vi) Acceptance of payment through debit / credit card for payment of application fee under FTP.

(vii) Open API for submission of e-IEC application.

(viii) Mobile Applications for FTP.

Free passage of Export consignment

Consignments of items meant for exports shall not be withheld/ delayed for any reason by any agency of Central/ State Government.

In case of any doubt, authorities concerned may ask for an undertaking from exporter and release such consignment.

No seizure of export related Stock

No seizure shall be made by any agency so as to disrupt manufacturing activity and delivery schedule of exports. In exceptional cases, concerned agency may seize the stock on the basis of prima facie evidence of serious irregularity. However, such seizure should be lifted within 7 days unless the irregularities are substantiated.

24 X 7 Customs clearance

(a) The facility of 24 X 7 Customs clearance for specified import viz. Goods covered by 'facilitated' Bills of Entry and specified exports viz. Factory stuffed containers and goods exported under free Shipping Bills has been made available, at the 18 sea ports at : Chennai, Cochin, Ennore, Gopalpur, JNPT, Kakinada, Kandla, Kolkata, Mumbai, New Mangalore, Marmagoa, Mundra, Okha, Paradeep, Pipavav, Sikka, Tuticorin, Vishakapatnam.

(b) The facility of 24 X 7 Customs clearance for specified imports viz. Goods covered by 'facilitated' Bills of Entry and all exports viz. Goods covered by all Shipping Bills has also been made available at the 17 air cargo complexes at: Ahmedabad, Amritsar, Bangalore, Chennai, Coimbatore, Cochin, Calicut, Delhi, Goa, Hyderabad, Indore, Jaipur, Kolkata, Mumbai, Nashik, Thiruvananthapuram, Vishakhapatnam.

Single Window in Customs

(a) To facilitate trade, the importer and exporter would lodge their clearance documents at a single point only. Required permission if any, from other regulatory agencies would be obtained online without the trader having to approach these agencies. This would reduce interface with Governmental agencies, dwell time and cost of doing business.

(b) Single Window provides a common platform to trade to meet requirements of all regulatory agencies (such as Animal Quarantine, Plant Quarantine, Drug Controller, Textile Committee, etc) involved in exim trade through message exchange. Single Window Scheme is basically a network of cooperating facilities bound by trust and set of agreed interface specifications in which trade has seamless access to regulatory services delivered through electronic means. Benefits of Single Window Scheme include reduced cost of doing business, enhances transparency, integration of regulatory requirements at one common platform reduces duplicity and cost of compliance, optimal utilization of manpower.

Self-Assessment of Customs Duty

Self-Assessment of Customs duty by importers or exporters was introduced vide Finance Act, 2011. The system is trust based. The objective is to expedite release of imported / export goods. The system operates on an electronic Risk Management System (RMS).

Authorised Economic Operator (AEO) Programme

Based upon WCO's SAFE Framework of Standards (FoS), 'Authorised Economic Operator (AEO) programme' has been developed by Indian Customs to enable business involved in the international trade to reap the following benefits:

(i) Secure supply chain from point of export to import;

(ii) Ability to demonstrate compliance with security standards when contracting to supply overseas importers / exporters;

(iii) Enhanced border clearance privileges in Mutual Recognition Agreement (MRA) partner countries;

(iv) Minimal disruption to flow of cargo after a security related disruption;

(v) Reduction in dwell time and related costs; and

(vi) Customs advise / assistance if trade faces unexpected issues with Customs of countries with which India have MRA.

The AEO programmes have been implemented by other Customs administrations that give AEO status holders preferential Customs treatment in terms of reduced examination, faster clearances and other benefits. Thus, the AEO programme is expected to result in Mutual Recognition Agreements (MRA) with these Customs administrations. MRAs would ensure export goods get due Customs facilitation at the point of entry in the foreign country. Apart from securing supply chain, the benefits include reduction in dwell time and consequent cost of doing business. Indian Customs has signed MRA with Hong Kong Customs to recognise respective AEO Programmes to enable trade to get benefits on reciprocal basis. Indian Customs is also engaged in finalising MRA with other counties such as South Korea, Taiwan, USA etc.

Prior filing facility for Shipping Bills

To facilitate processing of shipping bills before actual shipment, prior online filing facility for shipping bills has been provided by the Customs - 7 days for air shipments & ICDs and 14 days for shipments by sea.

Cutting down delay in filing of Export General Manifest (EGM) for duty drawback

To facilitate quicker filing of EGMs and quicker rectification of EGM errors, there is a mechanism of monthly monitoring of EGMs by Chief Commissioners of Customs to ensure that facilitation does not lag on this account (Instruction No. 603/01/2011-DBK dated 31.07.2013).

Facility of Common Bond / LUT against authorizations issued under different EP Schemes

CBEC Circular 11(A)/2011-Cus dated 25.02.2011 has provided the financial year-wise facility of executing common Bond/LUT against Advance Authorization (AA)/Export Promotion Capital Goods (EPCG) Authorisation which is usable across all EDI ports/locations.

Exemption from Service Tax on Services received abroad

For all goods and services exported from India, services received / rendered abroad, where ever possible, shall be exempted from service tax.

Export of perishable agricultural Products

To reduce transaction and handling costs, a single window system to facilitate export of perishable agricultural produce has been introduced. The system will involve creation of multi-functional nodal agencies to be accredited by Agricultural and Processed Food Products Export Development Authority (APEDA), New Delhi. The detailed procedure has been notified at Appendix 1C to Appendices & ANFs.

Time Release Study (TRS)

Central Board of Excise and Customs has decided to undertake 'Time Release Study' (TRS) as per WCO guidelines at major Customs locations on six monthly basis. WCO Time Release Study (TRS) is a unique tool and method for measuring the actual performance of Customs. The underlying objectives of Time Release Study are:

(i) Identifying bottlenecks in the international supply chain / or constraints affecting Customs release.

(ii) Establishing baseline trade facilitation performance measurement.

Towns of Export Excellence (TEE)

(a) **Objective:** Development and growth of export production centres. A number of towns have emerged as dynamic industrial clusters contributing handsomely to India's exports. It is necessary to grant recognition to these industrial clusters with a view to maximize their potential and enable them to move up the value chain and also to tap new markets.

(b) Selected towns producing goods of ₹ 750 Crore or more may be notified as TEE based on potential for growth in exports. However for TEE in Handloom, Handicraft, Agriculture and Fisheries sector, threshold limit would be ₹150 Crore. The following facilities will be provided to such TEE's:

   (i) Recognized associations of units will be provided financial assistance under MAI scheme, on priority basis, for export promotion projects for marketing, capacity building and technological services.

(ii) Common Service Providers in these areas shall be entitled for EPCG scheme.

(c) Notified Towns (TEEs) are listed in Appendix 1 B of Appendices & ANFs.

Director General of Commercial Intelligence and Statistics (DGCI&S), Kolkata as the provider of trade data

DGCI&S is an ISO certified organization under the administrative control of DGFT and it is the provider of trade data which is a source of guidance and direction for export & import trade and which help the exporters and importers formulate their trade strategy. Foreign trade data is disseminated by DGCI&S through (i) Monthly & Quarterly publications in CD form and (ii) Generation of data from the Foreign Trade database as per user's request. The DGCI&S has a Priced Information System (PIS) for disseminating data except for purely Central and State Governments and United Nations bodies. DGCI&S has put in place a Data Suppression Policy. The aim of this policy is to maintain confidentiality of importer's and exporter's commercially sensitive business data. Transaction level data would not be made publicly available to protect privacy. DGCI&S trade data shall be made available at aggregate level with a minimum possible time lag on commercial criteria. DGCI&S can be visited at http://dgciskol.nic.in.

5.2 GENERAL PROVISIONS REGARDING IMPORTS AND EXPORTS

Objective

The general provisions governing import and export of goods and services are dealt with in this heading.

Exports and Imports – 'Free', unless regulated

(a) Exports and Imports shall be 'Free' except when regulated by way of 'prohibition', 'restriction' or 'exclusive trading through State Trading Enterprises (STEs)' as laid down in Indian Trade Classification (Harmonised System) [ITC (HS)] of Exports and Imports. The list of 'Prohibited', 'Restricted' and 'STE' items can be viewed by clicking on 'Downloads' at http://dgft.gov.in.

(b) Further, there are some items which are 'free' for import/export, but subject to conditions stipulated in other Acts or in law for the time being in force.

Indian Trade Classification (Harmonised System) [ITC (HS)] of Exports and Imports

(a) ITC (HS) is a compilation of codes for all merchandise / goods for export/ import. Goods are classified based on their group or sub-group at 2/4/6/8 digits.

(b) ITC (HS) is aligned at 6 digit level with international Harmonized System goods nomenclature maintained by World Customs Organization (http://www. wcoomd.org). However, India maintains national Harmonized System of goods at 8 digit level which may be viewed by clicking on 'Downloads' at http://dgft.gov.in.

(c) The import/export policies for all goods are indicated against each item in ITC (HS). Schedule 1 of ITC (HS) lays down the Import Policy regime while Schedule 2 of ITC (HS) details the Export Policy regime.

(d) Except where it is clearly specified, Schedule 1 of ITC (HS), Import Policy is for new goods and not for the Second Hand goods. For Second Hand goods, the Import Policy regime is given in this FTP.

Compliance of Imports with Domestic Laws

(a) Domestic Laws/ Rules/ Orders/ Regulations / Technical specifications/ environmental/ safety and health norms applicable to domestically produced goods shall apply, mutatis mutandis, to imports, unless specifically exempted.

(b) However, goods to be utilized/ consumed in manufacture of export products, as notified by DGFT, may be exempted from domestic standards/quality specifications.

Authority to specify Procedures

DGFT may specify procedure to be followed by an exporter or importer or by any licensing/Regional Authority (RA) or by any other authority for purposes of implementing provisions of FT (D&R) Act, the Rules and the Orders made there under and FTP. Such procedure, or amendments, if any, shall be published by means of a Public Notice.

IMPORTER-EXPORTER CODE / e-IEC

Importer-Exporter Code (IEC)

(I) An IEC is a 10-digit number allotted to a person that is mandatory for undertaking any export/import activities. Now the facility for IEC in electronic form or e-IEC has also been operationalised.

(a) **Application for IEC/e-IEC:**

Application for obtaining IEC can be filed manually and submitting the form in the office of Regional Authority (RA) of DGFT. Alternatively, an application for e-IEC may be filed online in ANF 2A, on payment of application fee of ₹ 500/-, to be paid online through net banking or credit/debit card (to be operationalised shortly). Documents/ details required to be uploaded/ submitted along with the application form are listed in the Application Form (ANF 2A).

(b) When an e-IEC is approved by the competent authority, applicant is informed through e-mail that a computer generated e-IEC is available on the DGFT website. By clicking on "Application Status" after having filled and submitted the requisite details in "Online IEC Application" webpage, applicant can view and print his e-IEC.

(c) Briefly, following are the requisite details /documents (scanned copies) to be submitted/ uploaded along with the application for IEC:

(i) Details of the entity seeking the IEC:

(1) PAN of the business entity in whose name Import/Export would be done (Applicant individual in case of Proprietorship firms).

(2) Address Proof of the applicant entity.

(3) LLPIN /CIN/ Registration Certification Number (whichever is applicable).

(4) Bank account details of the entity. Cancelled Cheque bearing entity's preprinted name or Bank certificate in prescribed format ANF2A(I).

(ii) Details of the Proprietor/ Partners/ Directors/ Secretary or Chief Executive of the Society/ Managing Trustee of the entity:

(1) PAN (for all categories)

(2) DIN/DPIN (in case of Company /LLP firm)

(iii) Details of the signatory applicant:

(1) Identity proof

(2) PAN

(3) Digital photograph

(d) In case the applicant has digital signature, the application can also be submitted online and no physical application or document is required. In case the applicant does not possess digital signature, a print out of the application filed online duly signed by the applicant has to be submitted to the concerned jurisdictional RA, in person or by post.

(e) Detailed guidelines for applying for e-IEC are available at <http://dgft.gov.in/exim/2000/iec_anf/iecanf.htm>.

(II) No Export/Import without IEC:

(i) No export or import shall be made by any person without obtaining an IEC number unless specifically exempted.

(ii) Exempt categories and corresponding permanent IEC numbers are given in Para 2.07 of Handbook of Procedures.

(III) Only one IEC against one Permanent Account Number (PAN)

Only one IEC is permitted against on Permanent Account Number (PAN). If any PAN card holder has more than one IEC, the extra IECs shall be disabled.

Mandatory documents for export/import of goods from/into India

(a) Mandatory documents required for export of goods from India:

1. Bill of Lading/Airway Bill
2. Commercial Invoice cum Packing List*
3. Shipping Bill/Bill of Export

(b) Mandatory documents required for import of goods into India

1. Bill of Lading/Airway Bill
2. Commercial Invoice cum Packing List*
3. ill of Entry

[**Note:** *(i) As per CBEC Circular No. 01/15-Customs dated 12/01/2015. (ii) Separate Commercial Invoice and Packing List would also be accepted.]

(c) For export or import of specific goods or category of goods, which are subject to any restrictions/ policy conditions or require NOC or product specific compliances under any statute, the regulatory authority concerned may notify additional documents for purposes of export or import.

(d) In specific cases of export or import, the regulatory authority concerned may electronically or in writing seek additional documents or information, as deemed necessary to ensure legal compliance.

(e) The above stipulations are effective from 1st April, 2015.

Principles of Restrictions

DGFT may, through a Notification, impose restrictions on export and import, necessary for: -

(a) Protection of public morals;

(b) Protection of human, animal or plant life or health;

(c) Protection of patents, trademarks and copyrights, and the prevention of deceptive practices;

(d) Prevention of use of prison labour;

(e) Protection of national treasures of artistic, historic or archaeological value;

(f) Conservation of exhaustible natural resources;

(g) Protection of trade of fissionable material or material from which they are derived;

(h) Prevention of traffic in arms, ammunition and implements of war.

Export/Import of Restricted goods/Services

Any goods /service, the export or import of which is 'Restricted' may be exported or imported only in accordance with an Authorisation / Permission or in accordance with the procedure prescribed in a Notification / Public Notice issued in this regard.

Export of SCOMET Items

Export of Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET), as indicated in Appendix-3 of Schedule 2 of ITC(HS) Classification of Export & Import Items, shall be governed by the specific provisions of (i) Chapter IV A of the FT(D&R) Act, 1992 as amended from time to time (ii) Sl. No. 4 & 5 of Table A and Appendix-3 of Schedule 2 of ITC(HS) Classification of Export & Import Items (iii) Para 2.16, Para 2.17, Para 2.18 of FTP given in this study note under the heading "Prohibition on Import and Export of Arms and related material from / its Iraq", "Prohibition on Direct or Indirect import and export from / to Democratic People's Republic of Korea" and "Prohibition on Direct or Indirect Import and Export from / to Iran" respectively and (iv) Para 2.73-2.82 of Hand Book of Procedures, in addition to the other provisions of FTP and Handbook of Procedures governing export authorizations.

Actual User Condition

Goods which are importable freely without any 'Restriction' may be imported by any person. However, if such imports require an Authorisation, actual user alone may import such good(s) unless actual user condition is specifically dispensed with by DGFT.

Terms and Conditions of an Authorisation

Every Authorisation shall, inter alia, include such terms and conditions as may be specified by RA along with the following:

(a) Description, quantity and value of goods;

(b) Actual User condition (as defined in Chapter 9);

(c) Export Obligation;

(d) Minimum Value addition to be achieved;

(e) Minimum export/import price;

(f) Bank guarantee/ Legal undertaking / Bond with Customs Authority/RA.

(g) Validity period of import/export as specified in Handbook of Procedures.

Application Fee

Application for IEC/ Authorisation / License / Scrips must be accompanied by application fees as indicated in the Appendix 2K of Appendices and Aayat Niryat Forms.

Clearance of Goods from Customs against Authorization

Goods already imported / shipped / arrived, in advance, but not cleared from Customs may also be cleared against an Authorisation issued subsequently. This facility will however be not available to "restricted" items or items traded through STEs.

Authorisation - not a Right

No person can claim an Authorisation as a right and DGFT or RA shall have power to refuse to grant or renew the same in accordance with provisions of FT (D&R) Act, Rules made there under and FTP.

Penal action and placing of an entity in Denied Entity List (DEL)

(a) If an Authorisation holder violates any condition of such Authorisation or fails to fulfill export obligation, or fails to deposit the requisite amount within the period specified in demand notice issued by Department of Revenue and /or DGFT, he shall be liable for action in accordance with FT (D&R) Act, the Rules and Orders made there under, FTP and any other law for time being in force.

(b) With a view to raising ethical standards and for ease of doing business, DGFT has provided for self certification system under various schemes. In such cases, applicants shall undertake self certification with sufficient care and caution in filling up information/particulars. Any information / particulars subsequently found untrue/ incorrect will be liable for action under FTDR Act, 1992 and Rules therein in addition to penal action under any other Act/Order.

(c) A firm may be placed under Denied Entity List (DEL), by the concerned RA, under the provision of Rule 7 of Foreign Trade (Regulation) Rules, 1993. On issuance of such an order, for reasons to be recorded in writing, a firm may be refused grant or renewal of a license, certificate, scrip or any instrument bestowing financial or fiscal benefits. If a firm is placed under DEL all new licences, scrips, certificates, instruments, etc will be blocked from printing / issue / renewal.

(d) DEL orders may be placed in abeyance, for reasons to be recorded in writing by the concerned RA. DEL order can be placed in abeyance, for a period not more than 60 days at a time.

(e) A firm's name can be removed from DEL, by the concerned RA for reasons to be recorded in writing, if the firm completes Export Obligation/ pays penalty/ fulfills requirement of Demand Notice(s) issued by the RA/submits documents required by the RA.

PROHIBITIONS (Country and Product Specific):

Prohibition on Import and Export of 'Arms and related material' from / to Iraq

Notwithstanding the policy on Arms and related materials in Chapter 93 of ITC(HS), the import/export of Arms and related material from/to Iraq is 'Prohibited'. However, export of Arms and related material to Government of Iraq shall be permitted subject to 'No Objection Certificate' from the Department of Defence Production.

Prohibition on Direct or Indirect Import and Export from / to Democratic People's Republic of Korea

Direct or indirect export and import of following items, whether or not originating in Democratic People's Republic of Korea (DPRK), to / from, DPRK is 'Prohibited':

All items, materials, equipment, goods and technology including as set out in lists in documents

INFCIRC/254/Rev.11/Part 1 and INFCIRC/254/ Rev.8/Part 2 (IAEA documents), S/2012/947, S/2009/364 and S/2006/853 (UN Security Council documents) and Annex III to UN Security Council resolution 2094 (2013) which could contribute to DPRK's nuclear-related, ballistic missile-related or other weapons of mass destruction-related programmes; Luxury goods, including but not limited to the items specified in Annex IV to UN Security Council resolution 2094 (2013).

Prohibition on Direct or Indirect Import and Export from/ to Iran

(a) Direct or indirect export and import of all items, materials, equipment, goods and technology which could contribute to Iran's enrichment-related, reprocessing or heavy water related activities, or to development of nuclear weapon delivery systems, as mentioned below, whether or not originating in Iran, to/from Iran is 'Prohibited':

  (i) Items listed in INFCIRC/254/Rev.9/Part 1 and INFCIRC/254/Rev.7/Part 2 (IAEA Documents).

  (ii) Items listed in S/2006/263 (UN Security Council document).

(b) All the UN Security Council Resolutions/Documents and IAEA Documents referred to above are available on the UN Security Council website (www.un.org/Docs/sc) and IAEA website (www.iaea.org).

Prohibition on Import of Charcoal from Somalia

Direct or indirect import of charcoal is prohibited from Somalia, irrespective of whether or not such charcoal has originated in Somalia [United Nations Security Council Resolution 2036 (2012)]. Importers of charcoal shall submit a declaration to Customs that the consignment has not originated in Somalia.

IMPORT / EXPORT THROUGH STATE TRADING ENTERPRISES:

State Trading Enterprises (STEs)

(a) State Trading Enterprises (STEs) are governmental and non-governmental enterprises, including marketing boards, which deal with goods for export and / or import. Any good, import or export of which is governed through exclusive or special privilege granted to State Trading Enterprises (STE), may be imported or exported by the concerned STE as per conditions specified in ITC (HS).

(b) Such STE (s) shall make any such purchases or sales involving imports or exports solely in accordance with commercial considerations, including price, quality, availability, marketability, transportation and other conditions of purchase or sale in a non discriminatory manner and shall afford enterprises of other countries adequate opportunity, in accordance with customary business practices, to compete for participation in such purchases or sales.

(c) DGFT may, however, grant an authorization to any other person to import or export any of the goods notified for exclusive trading through STEs.

TRADE WITH SPECIFIC COUNTRIES:

Trade with neighbouring Countries

DGFT may issue instructions or frame schemes as may be required to promote trade and strengthen economic ties with neighbouring countries.

Transit Facility

Transit of goods through India from/ or to countries adjacent to India shall be regulated in accordance with bilateral treaties between India and those countries and will be subject to such restrictions as may be specified by DGFT in accordance with International Conventions.

Trade with Russia under Debt-Repayment Agreement

In case of trade with Russia under Debt Repayment Agreement, DGFT may issue instructions or frame schemes as may be required, and anything contained in FTP, in so far as it is inconsistent with such instructions or schemes, shall not apply.

IMPORT OF SPECIFIC CATEGORIES OF GOODS:

Import of Samples

Import of samples shall be governed by para 2.65 of Handbook of Procedures.

Import of Gifts

Import of gifts shall be 'free' where such goods are otherwise freely importable under ITC (HS). In other cases, such imports shall be permitted against an authorisation issued by DGFT.

Passenger Baggage

(a) Bona-fide household goods and personal effects may be imported as part of passenger baggage as per limits, terms and conditions thereof in Baggage Rules notified by Ministry of Finance.

(b) Samples of such items that are otherwise freely importable under FTP may also be imported as part of passenger baggage without an Authorisation.

(c) Exporters coming from abroad are also allowed to import drawings, patterns, labels, price tags, buttons, belts, trimming and embellishments required for export, as part of their passenger baggage without an Authorisation.

Re – import of goods repaired abroad

Capital goods, equipments, components, parts and accessories, whether imported or indigenous, except those restricted under ITC (HS) may be sent abroad for repairs, testing, quality improvement or upgradation or standardization of technology and re-imported without an Authorisation.

Import of goods used in projects abroad

Project contractors after completion of projects abroad, may import without an Authorisation, goods including capital goods used in the project, provided they have been used for at least one year.

Import of Prototypes

Import of new / second hand prototypes / second hand samples may be allowed on payment of duty without an Authorisation to an Actual User (industrial) engaged in production of or having industrial licence / letter of intent for research in item for which prototype is sought for product development or research, as the case may be, upon a self- declaration to that effect, to satisfaction of customs authorities

Import through courier service

Imports through a registered courier service are permitted as per Notifications issued by DoR. However, importability / exportability of such items shall be regulated in accordance with this FTP/ ITC(HS).

IMPORT POLICY FOR SECOND HAND GOODS :

Second Hand Goods

S. No.	Categories of Second Hand Goods	Import Policy	Conditions, if any
I	Second Hand Capital Goods		
(a)	i. Personal computers/ laptops including their refurbished / reconditioned spares ii. Photocopier machines/ Digital multifunction Print & Copying Machines iii. Air conditioners iv. Diesel generating sets.	Restricted	Importable against authorization
(b)	Refurbished / re-conditioned spares of Capital Goods	Free	Subject to production of Chartered Engineer certificate to the effect that such spares have at least 80% residual life of original spare.
(c)	All other second hand capital goods {other than (a) & (b) above}	Free	
II	Second Hand Goods other than capital goods	Restricted	Importable against Authorization

IMPORT POLICY FOR METALLIC WASTE AND SCRAPS

Import of Metallic waste and Scrap

(a) Import of any form of metallic waste, scrap will be subject to the condition that it will not contain hazardous, toxic waste, radioactive contaminated waste/scrap containing radioactive material, any types of arms, ammunition, mines, shells, live or used cartridge or any other explosive material in any form either used or otherwise as detailed in para 2.54 of Handbook of Procedures.

(b) The types of metallic waste and scrap which can be imported freely and the procedure of import in the shredded form; unshredded compressed and loose form, is laid down in para 2.54 of Handbook of Procedures.

Removal of Scrap/waste from SEZ

A SEZ unit/Developer/ Co-developer may be allowed to dispose of in DTA any waste or scrap, including any form of metallic waste and scrap, generated during manufacturing or processing activity, without an authorization, on payment of applicable Customs Duty.

OTHER PROVISIONS RELATED TO IMPORTS:

Import under Lease Financing

No specific permission of RA is required for lease financed capital goods.

Execution of Legal Undertaking (LUT) / Bank Guarantee (BG)

(a) Wherever any duty free import is allowed or where otherwise specifically stated, importer shall execute, Legal Undertaking (LUT) / Bank Guarantee (BG) / Bond with the Customs Authority, as prescribed, before clearance of goods.

(b) In case of indigenous sourcing, Authorisation holder shall furnish LUT/BG/Bond to RA concerned before sourcing material from indigenous supplier/ nominated agency as prescribed in Chapter 2 of Handbook of Procedures.

Private/Public Bonded Warehouses for Imports

(a) Private/ Public bonded warehouses may be set up in DTA as per terms and conditions of notification issued by DoR. Any person may import goods except prohibited items, arms and ammunition, hazardous waste and chemicals and warehouse them in such bonded warehouses.

(b) Such goods may be cleared for home consumption in accordance with provisions of FTP and against Authorisation, wherever required. Customs duty as applicable shall be paid at the time of clearance of such goods.

(c) If such goods are not cleared for home consumption within a period of one year or such extended period as the customs authorities may permit, importer of such goods shall re-export the goods.

Special provision for Hides Skins and semi-finished goods

Hides, Skins and semi-finished leather may be imported in the Public Bonded warehouse for the purpose of DTA sale and the unsold items thereof can be re-exported from such bonded warehouses at 50% of the applicable export duty. However, this facility shall not be allowed for import under Private Bonded warehouse.

Sale on High Seas

Sale of goods on high seas for import into India may be made subject to FTP or any other law in force.

EXPORTS:

Free Exports

All goods may be exported without any restriction except to the extent that such exports are regulated by ITC (HS) or any other provision of FTP or any other law for the time being in force. DGFT may, however, specify through a public notice such terms and conditions according to which any goods, not included in ITC (HS), may be exported without an Authorisation.

Exemption / Remission of Service Tax in DTA on goods & services exported

For all goods and services which are exported from units in DTA and units in EOU / EHTP / STP / BTP, exemption / remission of service tax levied and related to exports, shall be allowed, as per prescribed procedure in Chapter 4 of Handbook of Procedures.

Benefits for Supporting Manufacturers

For any benefit to accrue to the supporting manufacturer, the names of both supporting manufacturer as well as the merchant exporter must figure in the concerned export documents, especially in ARE-1 / ARE-3 / Shipping Bill / Bill of Export/ Airway Bill.

Third Party Exports

Third party exports (except Deemed Export) as defined in Chapter 9 shall be allowed under FTP. In such cases, export documents such as shipping bills shall indicate name of both manufacturing exporter/ manufacturer and third party exporter(s). Bank Realisation Certificate (BRC), export order and invoice should be in the name of third party exporter.

EXPORTS OF SPECIFIC CATEGORIES

Export of Samples

Export of Samples and Free of charge goods shall be governed by provisions given in para 2.66 of Handbook of Procedures.

Export of Gifts

Goods including edible items, of value not exceeding ₹ 5,00,000 in a licensing year, may be exported as a gift. However, items mentioned as restricted for exports in ITC (HS) shall not be exported as a gift, without an Authorisation.

Export of Passenger Baggage

(a) Bona-fide personal baggage may be exported either along with passenger or, if unaccompanied, within one year before or after passenger's departure from India. However, items mentioned as restricted in ITC (HS) shall require an Authorisation. Government of India officials proceeding abroad on official postings shall, however, be permitted to carry along with their personal baggage, food items (free, restricted or prohibited) strictly for their personal consumption.

(b) Samples of such items that are otherwise freely exportable under FTP may also be exported as part of passenger baggage without an Authorisation.

Import for export

I. (a) Goods imported, in accordance with FTP, may be exported in same or substantially the same form without an Authorisation provided that item to be imported or exported is not restricted for import or export in ITC (HS).

(b) Goods, including capital goods (both new and second hand), may be imported for export provided:

(i) Importer clears goods under Customs Bond;

(ii) Goods are freely exportable, i.e., are not "Restricted"/ "Prohibited"/ subject to "exclusive trading through State Trading Enterprises" or any conditionality/ requirement as may be required under Schedule 2 – Export Policy of the ITC (HS);

(iii) Export is against freely Convertible currency.

(c) Goods in (b) above will include 'Restricted' goods for import (except 'Prohibited' items).

(d) Capital goods, which are freely importable and freely exportable, may be imported for export on execution of LUT/BG with Customs Authority.

II. (a) Goods imported against payment in freely convertible currency would be permitted for export only against payment in freely convertible currency, unless otherwise notified by DGFT.

(b) Export of such goods to the notified countries (presently only Iran) would be permitted against payment in Indian Rupees, subject to minimum 15% value addition.

(c) However, re-export of food, medicine and medical equipments, namely, items covered under ITC(HS) Chapters 2 to 4, 7 to 11, 15 to 21, 23, 30 and items under headings 9018, 9019, 9020, 9021 & 9022 of Chapter-90 of ITC(HS) will not be subject to minimum value addition requirement for export to Iran. Exports of these items to Iran shall, however, be subject to all other conditions of FTP 2015-20 and ITC (HS) 2012, as applicable. Bird's eggs covered under ITC (HS) 0407 & 0408 and Rice covered under ITC (HS) 1006 are not covered under this dispensation, as at II (a) above.

(d) Exports under this dispensation, as at II(b) and (c) above shall not be eligible for any export incentives.

Export through Courier Service

Exports through a registered courier service are permitted as per Notification issued by DoR. However, importability / exportability of such items shall be regulated in accordance with FTP/ ITC (HS).

Export of Replacement Goods

Goods or parts thereof on being exported and found defective/damaged or otherwise unfit for use may be replaced free of charge by the exporter and such goods shall be allowed clearance by Customs authorities, provided that replacement goods are not mentioned as restricted items for exports in ITC (HS).

Export of Repaired Goods

(i) "Goods or parts thereof, except restricted under ITC (HS), on being exported and found defective, damaged or otherwise unfit for use may be imported for repair and subsequent re-export. Such goods shall be allowed clearance without an Authorisation and in accordance with customs notification.

(ii) However, re-export of such defective parts/spares by the Companies/firms and Original Equipment Manufacturers shall not be mandatory if they are imported exclusively for undertaking root cause analysis, testing and evaluation purpose."

Export of Spares

Warranty spares (whether indigenous or imported) of plant, equipment, machinery, automobiles or any other goods, [except those restricted under ITC (HS)] may be exported along with main equipment or subsequently but within contracted warranty period of such goods, subject to approval of RBI.

Private Bonded Warehouses for Exports

(a) Private bonded warehouses exclusively for exports may be set up in DTA as per terms and conditions of notifications issued by Department of Revenue.

(b) Such warehouses shall be entitled to procure goods from domestic manufacturers without payment of duty. Supplies made by a domestic supplier to such notified warehouses shall be treated as physical exports provided payments are made in free foreign exchange.

PAYMENTS AND RECEIPTS ON IMPORTS / EXPORTS

Denomination of Export Contracts

(a) All export contracts and invoices shall be denominated either in freely convertible currency or Indian rupees but export proceeds shall be realized in freely convertible currency.

(b) However, export proceeds against specific exports may also be realized in rupees, provided it is through a freely convertible Vostro account of a non resident bank situated in any country other than a member country of Asian Clearing Union (ACU) or Nepal or Bhutan. Additionally, rupee payment through Vostro account must be against payment in free foreign currency by buyer in his non-resident bank account. Free foreign exchange remitted by buyer to his nonresident bank (after deducting bank service charges) on account of this transaction would be taken as export realization under export promotion schemes of FTP.

(c) Contracts (for which payments are received through Asian Clearing Union (ACU) shall be denominated in ACU Dollar. Central Government may relax provisions of this paragraph in appropriate cases. Export contracts and invoices can be denominated in Indian rupees against EXIM Bank/Government of India line of credit.

Export to Iran – Realisations in Indian Rupees to be eligible for FTP benefits / incentives

Notwithstanding the provisions contained in above para (a) above, export proceeds realized in Indian

Rupees against exports to Iran are permitted to avail exports benefits / incentives under the Foreign Trade Policy (2015-20), at par with export proceeds realized in freely convertible currency.

Non-Realisation of Export Proceeds

(a) If an exporter fails to realize export proceeds within time specified by RBI, he shall, without prejudice to any liability or penalty under any law in force, be liable to return all benefits / incentives availed against such exports and action in accordance with provisions of FT (D&R) Act, Rules and Orders made there under and FTP.

(b) In case an Exporter is unable to realise the export proceeds for reasons beyond his control (force-majeure), he may approach RBI for writing off the unrealised amount as per procedure laid down in para 2.87 of Handbook of Procedures.

(c) The payment realized through insurance cover, would be eligible for benefits under FTP. The procedure to be followed in such cases is laid down in para 2.85 of Handbook of Procedures.

EXPORT PROMOTION COUNCILS

Recognition of Export Promotion Councils (EPCs) to function as Registering Authority for issue of RCMC.

(a) Export Promotion Councils (EPCs) are organizations of exporters, set up with the objective to promote and develop Indian exports. Each Council is responsible for promotion of a particular group of products/ projects/services as given in Appendix 2T of AANF.

(b) EPCs are also eligible to function as Registering Authorities to issue Registration-cum-Membership Certificate (RCMC) to its members. The criteria for EPCs to be recognized as Registering Authorities for issue of RCMC to its members are detailed in para 2.92 of the Handbook of Procedures.

Registration-cum-Membership Certificate (RCMC)

Any person, applying for:

(a) An Authorisation to import/export (except items) listed as 'Restricted' items in ITC (HS)

Or

(b) Any other benefit or concession under FTP shall be required to furnish or upload on DGFT's website in the Importer Exporter Profile, the RCMC granted by competent authority in accordance with procedure specified in HBP, unless specifically exempted under FTP. Certificate of Registration as Exporter of Spices (CRES) issued by Spices Board shall be treated as Registration-Cum-Membership Certificate (RCMC) for the purposes under this Policy.

POLICY INTERPRETATION AND RELAXATIONS:

Interpretation of Policy

(a) The decision of DGFT shall be final and binding on all matters relating to interpretation of Policy, or provision in Handbook of Procedures, Appendices and Aayat Niryat Forms or classification of any item for import / export in the ITC (HS).

(b) A Policy Interpretation Committee (PIC) may be constituted to aid and advise DGFT. The composition of the PIC would be as follows:

   (i) DGFT: Chairman

   (ii) All Additional DGFTs in Headquarters : Members

   (iii) All Joint DGFTs in Headquarters looking after Policy matters : Members

   (iv) Joint DGFT (PRC/PIC) : Member Secretary

   (v) Any other person / representative of the concerned Ministry / Department, to be co-opted by the Chairman.

Exemption from Policy/ Procedures

DGFT may in public interest pass such orders or grant such exemption, relaxation or relief, as he may deem fit and proper, on grounds of genuine hardship and adverse impact on trade to any person or class or category of persons from any provision of FTP or any procedure. While granting such exemption, DGFT may impose such conditions as he may deem fit after consulting the Committees as under:

Sl. No.	Description	Committee
(a)	Fixation / modification of product norms	Norms Committees
(b)	Nexus with Capital Goods (CG) and benefits under under all schemes EPCG Schemes	EPCG Committee
(c)	All other issues	Policy Relaxation Committee (PRC)

Personal Hearing by DGFT for Grievance Redressal

(a) Government is committed to easy and speedy redressal of grievances from Trade and Industry. Provision of FTP provides for relaxation of Policy and Procedures on grounds of genuine hardship and adverse impact on trade. DGFT may consider request for relaxation after consulting concerned Norms Committee, EPCG Committee or Policy Relaxation Committee (PRC).

(b) As a last resort to redress grievances of Importers/ Exporters, DGFT may provide an opportunity for Personal Hearing (PH) before PRC. For such PH, a specific request along with the prescribed application fee has to be made to DG, if following conditions are satisfied:

(i) If an importer/exporter is aggrieved by any decision taken by Policy Relaxation Committee (PRC), or a decision/order by any authority in the Directorate General of Foreign Trade and

(ii) A request for review before the said Committee or Authority has been filed.

(iii) Such Committee or Authority has considered the request for a review, and

(iv) The exporter / importer continues to be aggrieved.

(c) The decision conveyed in pursuance to the personal hearing shall be final and binding.

(d) The opportunity for Personal Hearing will not apply to a decision/order made in any proceeding, including an adjudication proceeding, whether at the original stage or at the appellate stage, under the relevant provisions of FT (D&R) Act, 1992, as amended from time to time.

Regularization of EO default and settlement of Customs duty and interest through Settlement Commission

With a view to providing assistance to firms who have defaulted under FTP for reasons beyond their control as also facilitating merger, acquisition and rehabilitation of sick units, it has been decided to empower Settlement Commission in Central Board of Excise and Customs to decide such cases also with effect from 01.04.2005.

SELF CERTIFICATION OF ORIGINATING GOODS

Approved Exporter Scheme for Self Certification of Certificate of Origin.

(i) Currently, Certificates of Origin under various Preferential Trade Agreements [PTA], Free Trade Agreements [FTAs], Comprehensive Economic Cooperation Agreements [CECA] and Comprehensive Economic Partnerships Agreements [CEPA] are issued by designated agencies as per Appendix 2B of Appendices and Aayat and Niryat Forms. A new optional system of self certification is being introduced with a view to reducing transaction cost.

(ii) The Manufacturers who are also Status Holders shall be eligible for Approved Exporter Scheme. Approved Exporters will be entitled to self-certify their manufactured goods as originating from India with a view to qualifying for preferential treatment under different PTAs/FTAs/CECAs/CEPAs which are in operation. Self-certification will be permitted only for the goods that are manufactured as per the Industrial Entrepreneurial's Memorandum (IEM) / Industrial Licence (IL)/Letter of Intent (LOI) issued to manufacturers.

(iii) Status Holders will be recognized by DGFT as Approved Exporters for self-certification based on availability of required infrastructure, capacity and trained manpower as per the details in Para 2.109 of Handbook of Procedures 2015-20 read with Appendix 2F of Appendices & Aayaat Niryaat Forms.

(iv) The details of the Scheme, along with the penalty provisions, are provided in Appendix 2F of Appendices and Aayaat Niryaat Forms and will come into effect only when India incorporates the scheme into a specific agreement with its partner/s and the same is appropriately notified by DGFT.

5.3 EXPORTS FROM INDIA SCHEMES

Objective

The objective of schemes under this heading is to provide rewards to exporters to offset infrastructural inefficiencies and associated costs involved and to provide exporters a level playing field.

Exports from India Schemes

There shall be following two schemes for exports of Merchandise and Services respectively:

(i) Merchandise Exports from India Scheme (MEIS).

(ii) Service Exports from India Scheme (SEIS).

Nature of Rewards

Duty Credit Scrips shall be granted as rewards under MEIS and SEIS. The Duty Credit Scrips and goods imported / domestically procured against them shall be freely transferable. The Duty Credit Scrips can be used for :

(i) Payment of Customs Duties for import of inputs or goods, except certain items.

(ii) Payment of excise duties on domestic procurement of inputs or goods, including capital goods as per DoR notification.

(iii) Payment of service tax on procurement of services as per DoR notification.

(iv) Payment of Customs Duty and fee as per paragraph heading, "Facility of payment of custom duties in case of E.O. defaults and fee through duty credit scrip." of this Policy.

Merchandise Exports from India Scheme (MEIS)

Objective

Objective of Merchandise Exports from India Scheme (MEIS) is to offset infrastructural inefficiencies and associated costs involved in export of goods/products, which are produced/manufactured in India, especially those having high export intensity, employment potential and thereby enhancing India's export competitiveness.

Entitlement under MEIS

Exports of notified goods/products with ITC[HS] code, to notified markets as listed in Appendix 3B, shall be rewarded under MEIS. Particular Appendix [3B of Appendices and Aayat Niryat Forms or AANF] lists the rate(s) of rewards on various notified products [ITC (HS) code wise]. The basis of calculation of reward would be on realised FOB value of exports in free foreign exchange, or on FOB value of exports as given in the Shipping Bills in free foreign exchange, whichever is less, unless otherwise specified.

Export of goods through courier or foreign post offices using e-Commerce

(i) Exports of goods through courier or foreign post office using e-commerce, as notified in Appendix 3C of AANF, of FOB value upto ₹ 25,000 per consignment shall be entitled for rewards under MEIS.

(ii) If the value of exports using e-commerce platform is more than ₹ 25,000 per consignment then MEIS reward would be limited to FOB value of ₹ 25,000 only.

(iii) Such goods can be exported in manual mode through Foreign Post Offices at New Delhi, Mumbai and Chennai.

(iv) Export of such goods under Courier Regulations shall be allowed manually on pilot basis through Airports at Delhi, Mumbai and Chennai as per appropriate amendments in regulations to be made by Department of Revenue. Department of Revenue shall fast track the implementation of EDI mode at courier terminals.

Ineligible categories under MEIS

The following exports categories /sectors shall be ineligible for Duty Credit Scrip entitlement under MEIS

(i) EOUs / EHTPs / BTPs/ STPs who are availing direct tax benefits / exemption.

(ii) Supplies made from DTA units to SEZ units

(iii) Export of imported goods covered under paragraph heading, 'Import for Export' of FTP;

(iv) Exports through trans-shipment, meaning thereby exports that are originating in third country but trans shipped through India;

(v) Deemed Exports;

(vi) SEZ/EOU/EHTP/BPT/FTWZ products exported through DTA units;

(vii) Items, which are restricted or prohibited for export under Schedule-2 of Export Policy in ITC (HS), unless specifically notified in Appendix 3B of AANF.

(viii) Service Export.

(ix) Red sanders and beach sand.

(x) Export products which are subject to Minimum export price or export duty.

(xi) Diamond Gold, Silver, Platinum, other precious metal in any form including plain and studded jewellery and other precious and semi-precious stones.

(xii) Ores and concentrates of all types and in all formations.

(xiii) Cereals of all types.

(xiv) Sugar of all types and all forms.

(xv) Crude / petroleum oil and crude / primary and base products of all types and all formulations.

(xvi) Export of milk and milk products.

(xvii) Export of Meat and Meat Products.

(xviii) Products wherein precious metal/diamond are used or Articles which are studded with precious stones.

(xix) Exports made by units in FTWZ.

SERVICE EXPORTS FROM INDIA SCHEME (SEIS)

Objective

Objective of Service Exports from India Scheme (SEIS) is to encourage export of notified Services from India.

Eligibility

(a) Service Providers of notified services, located in India, shall be rewarded under SEIS, subject to conditions as may be notified. Only Services rendered in the manner provided under this policy shall be eligible. The notified services and rates of rewards are listed in Appendix 3D of AANF.

(b) Such service provider should have minimum net free foreign exchange earnings of US$15,000 in preceding financial year to be eligible for Duty Credit Scrip. For Individual Service Providers and sole proprietorship, such minimum net free foreign exchange earnings criteria would be US$10,000 in preceding financial year.

(c) Payment in Indian Rupees for service charges earned on specified services, shall be treated as receipt in deemed foreign exchange as per guidelines of Reserve Bank of India. The list of such services is indicated in Appendix 3E of AANF.

(d) Net Foreign exchange earnings for the scheme are defined as under:

Net Foreign Exchange = Gross Earnings of Foreign Exchange minus Total expenses / payment / remittances of Foreign Exchange by the IEC holder, relating to service sector in the Financial year.

(e) If the IEC holder is a manufacturer of goods as well as service provider, then the foreign exchange earnings and Total expenses / payment / remittances shall be taken into account for service sector only.

(f) In order to claim reward under the scheme, Service provider shall have to have an active IEC at the time of rendering such services for which rewards are claimed.

Ineligible categories under SEIS

(1) Foreign exchange remittances other than those earned for rendering of notified services would not be counted for entitlement. Thus, other sources of foreign exchange earnings such as equity or debt participation, donations, receipts of repayment of loans etc. and any other inflow of foreign exchange, unrelated to rendering of service, would be ineligible.

(2) Following shall not be taken into account for calculation of entitlement under the scheme

(a) Foreign Exchange remittances:

I. Related to Financial Services Sector

(i) Raising of all types of foreign currency Loans;

(ii) Export proceeds realization of clients;

(iii) Issuance of Foreign Equity through ADRs / GDRs or other similar instruments;

(iv) Issuance of foreign currency Bonds;

(v) Sale of securities and other financial instruments;

(vi) Other receivables not connected with services rendered by financial institutions; and

II. Earned through contract/regular employment abroad (e.g. labour remittances);

(b) Payments for services received from EEFC Account;

(c) Foreign exchange turnover by Healthcare Institutions like equity participation, donations etc.

(d) Foreign exchange turnover by Educational Institutions like equity participation, donations etc.

(e) Export turnover relating to services of units operating under SEZ / EOU / EHTP / STPI / BTP Schemes or supplies of services made to such units;

(f) Clubbing of turnover of services rendered by SEZ / EOU /EHTP / STPI / BTP units with turnover of DTA Service Providers;

(g) Exports of Goods.

(h) Foreign Exchange earnings for services provided by Airlines, Shipping lines service providers plying from any foreign country X to any foreign country Y routes not touching India at all.

(i) Service providers in Telecom Sector.

Entitlement under SEIS

Service Providers of eligible services shall be entitled to Duty Credit Scrip at notified rates (as given in Appendix 3D of AANF) on net foreign exchange earned.

Remittances through Credit Card and other instruments for MEIS and SEIS

Free Foreign Exchange earned through international credit cards and other instruments, as permitted by RBI shall also be taken into account for computation of value of exports.

Effective date of schemes (MEIS and SEIS)

The schemes shall come into force with effect from the date of notification of this Policy, i.e. the rewards under MEIS/SEIS shall be admissible for exports made/services rendered on or after the date of notification of this Policy.

Special Provisions

(a) Government reserves the right in public interest, to specify export products or services or markets, which shall not be eligible for computation of entitlement of duty credit scrip.

(b) Government reserves the right to impose restriction / change the rate/ceiling on Duty Credit Scrip under this chapter.

(c) Government may also notify goods in Appendix 3A of AANF which shall not be allowed for debiting through Duty Credit Scrips in case of import.

(d) Government may prescribe value cap of any kind for a product(s) or limit total reward per IEC holder under this chapter at any time.

COMMON PROVISIONS FOR EXPORTS FROM INDIA SCHEMES (MEIS AND SEIS)

Transitional Arrangement

For the goods exported or services rendered upto the date of notification of this Policy, which were otherwise eligible for issuance of scrips under erstwhile Chapter 3 of the earlier Foreign Trade Policy(ies) and scrip is applied / issued on or after notification of this Policy against such export of goods or services rendered, the then prevailing policy and procedure regarding eligibility, entitlement, transferability, usage of scrip and any other condition in force at the time of export of goods or rendering of the services, shall be applicable to such scrips.

CENVAT/ Drawback

Additional Customs duty/excise duty/Service Tax paid in cash or through debit under Duty Credit scrip shall be adjusted as CENVAT Credit or Duty Drawback as per DoR rules or notifications. Basic Custom duty paid in cash or through debit under Duty Credit scrip shall be adjusted for Duty Drawback as per DoR rules or notifications.

Import under lease financing

Utilization of Duty Credit Scrip shall be permitted for payment of duty in case of import of capital goods under lease financing in terms of provision in paragraph heading, "Import under Lease Financing" of FTP.

Transfer of export performance

(a) Transfer of export performance from one IEC holder to another IEC holder shall not be permitted. Thus, a shipping bill containing name of applicant shall be counted in export performance / turnover of applicant only if export proceeds from overseas are realized in applicant's bank account and this shall be evidenced from e - BRC / FIRC.

(b) However, MEIS, rewards can be claimed either by the supporting manufacturer (along with disclaimer from the company / firm who has realized the foreign exchange directly from overseas) or by the company/ firm who has realized the foreign exchange directly from overseas.

Facility of payment of custom duties in case of E.O. defaults and fee through duty credit scrips

(a) Duty Credit Scrip can be utilised / debited for payment of Custom Duties in case of EO defaults for Authorizations issued under this Policy. Such utilization /usage shall be in respect of those goods which are permitted to be imported under the respective reward schemes. However, penalty / interest shall be required to be paid in cash.

(b) Duty credit scrips can also be used for payment of composition fee under FTP, for payment of application fee under FTP, if any and for payment of value shortfall in EO under para 4.49 of HBP 2015-20.

Risk Management System

(a) A Risk Management System shall be in operation whereby every month Computer system in DGFT Headquarters, on random basis, will select 10% of cases for each RA where scrips have already been issued, under each scheme. RA in turn may call for original documents in all such selected cases for further examination in detail. In case any discrepancy and/ or over claim is found on such examination, the applicant shall be under obligation to rectify such discrepancy and/or refund over claim in cash with interest at the rate prescribed under section 28 A A of the Customs Act 1962, from the date of issue of scrip in the relevant Head of Account of Customs within one month. The original holder of scrip, however, may refund such over claim by surrendering the same scrip whether partially utilized or fully unutilized, without interest.

(b) Regional Authority may ask for original proof of landing certificate, annexures attached to ANFs or any other document, which has been uploaded digitally at any time within three years from the date of issue of scrip. Failure to submit such documents in original would make applicant liable to refund the reward granted along with interest at the rate prescribed under section 28 A A of the Customs Act 1962, from the date of issuance of scrip. It would be the responsibility of applicant to maintain such documents, certificate etc. for a period of at least three years from the date of issuance of scrips.

Status Holder

(a) Status Holders are business leaders who have excelled in international trade and have successfully contributed to country's foreign trade. Status Holders are expected to not only contribute towards India's exports but also provide guidance and handholding to new entrepreneurs.

(b) All exporters of goods, services and technology having an import-export code (IEC) number shall be eligible for recognition as a status holder. Status recognition depends upon export performance. An applicant shall be categorized as status holder upon achieving export performance during current and previous two financial years. The export performance will be counted on the basis of FOB value of export earnings in free foreign exchange.

(c) For deemed export, FOR value of exports in Indian Rupees shall be converted in US$ at the exchange rate notified by CBEC, as applicable on 1st April of each Financial Year.

(d) For granting status, export performance is necessary in at least two out of three years.

Status Category

Status Category	Export Performance FOB / FOR (as converted) Value (in US $ million)
One Star Export House	3
Two Star Export House	25
Three Star Export House	100
Four Star Export House	500
Five Star Export House	2000

Grant of double weightage

(a) The exports by IEC holders under the following categories shall be granted double weightage for calculation of export performance for grant of status.

(i) Micro, Small & Medium Enterprises (MSME) as defined in Micro, Small & Medium Enterprises Development (MSMED) Act 2006.

(ii) Manufacturing units having ISO/BIS.

(iii) Units located in North Eastern States including Sikkim and Jammu & Kashmir.

(iv) Units located in Agri Export Zones.

(b) Double Weightage shall be available for grant of One Star Export House Status category only. Such benefit of double weightage shall not be admissible for grant of status recognition of other categories namely Two Star Export House, Three Star Export House, Four Star export House and Five Star Export House.

(c) A shipment can get double weightage only once in any one of above categories.

Other conditions for grant of status

(a) Export performance of one IEC holder shall not be permitted to be transferred to another IEC holder. Hence, calculation of exports performance based on disclaimer shall not be allowed.

(b) Exports made on re-export basis shall not be counted for recognition.

(c) Export of items under authorization, including SCOMET items, would be included for calculation of export performance.

Privileges of Status Holders

A Status Holder shall be eligible for privileges as under:

(a) Authorisation and Customs Clearances for both imports and exports may be granted on self-declaration basis;

(b) Input-Output norms may be fixed on priority within 60 days by the Norms Committee;

(c) Exemption from furnishing of Bank Guarantee for Schemes under FTP, unless specified otherwise anywhere in FTP or HBP;

(d) Exemption from compulsory negotiation of documents through banks. Remittance/receipts, however, would be received through banking channels;

(e) Two star and above Export houses shall be permitted to establish Export Warehouses as per Department of Revenue guidelines.

(f) Three Star and above Export House shall be entitled to get benefit of Accredited Clients Programme (ACP) as per the guidelines of CBEC (website: http://cbec.gov.in).

(g) The status holders would be entitled to preferential treatment and priority in handling of their consignments by the concerned agencies.

(h) Manufacturers who are also status holders (Three Star/Four Star/Five Star) will be enabled to self-certify their manufactured goods (as per their IEM/IL/LOI) as originating from India with a view to qualify for preferential treatment under different preferential trading agreements (PTA), Free Trade Agreements (FTAs), Comprehensive Economic Cooperation Agreements (CECA) and Comprehensive Economic Partnership Agreements (CEPA). Subsequently, the scheme may be extended to remaining Status Holders.

(i) Manufacturer exporters who are also Status Holders shall be eligible to self-certify their goods as originating from India as per para 2.108 (d) of Hand Book of Procedures.

(j) Status holders shall be entitled to export freely exportable items on free of cost basis for export promotion subject to an annual limit of ₹ 10 lakh or 2% of average annual export realization during preceding three licencing years whichever is higher.

5.4 DUTY EXEMPTION / REMISSION SCHEMES

Objective

Schemes under this Chapter enable duty free import of inputs for export production, including replenishment of input or duty remission.

Schemes

(a) Duty Exemption Schemes.

The Duty Exemption schemes consist of the following:

(i) Advance Authorisation (AA) (which will include Advance Authorisation for Annual Requirement).

(ii) Duty Free Import Authorisation (DFIA).

(b) Duty Remission Scheme.

Duty Drawback (DBK) Scheme, administered by Department of Revenue.

Applicability of Policy & Procedures

Authorisation under this Chapter shall be issued in accordance with the Policy and Procedures in force on the date of issue of the Authorisation.

Advance Authorisation

(a) Advance Authorisation is issued to allow duty free import of input, which is physically incorporated in export product (making normal allowance for wastage). In addition, fuel, oil, catalyst which is consumed / utilised in the process of production of export product, may also be allowed.

(b) Advance Authorisation is issued for inputs in relation to resultant product, on the following basis:

(i) As per Standard Input Output Norms (SION) notified (available in Hand Book of Procedures); OR

(ii) On the basis of self declaration as per paragraph 4.07 of Handbook of Procedures.

Advance Authorisation for Spices

Duty free import of spices covered under Chapter-9 of ITC (HS) shall be permitted only for activities like crushing / grinding / sterilization / manufacture of oils or oleoresins. Authorisation shall not be available for simply cleaning, grading, re-packing etc.

Eligible Applicant / Export / Supply

(a) Advance Authorisation can be issued either to a manufacturer exporter or merchant exporter tied to supporting manufacturer.

(b) Advance Authorisation for pharmaceutical products manufactured through Non-Infringing (NI) process (as indicated in paragraph 4.18 of Handbook of Procedures) shall be issued to manufacturer exporter only.

(c) Advance Authorisation shall be issued for:

   (i) Physical export (including export to SEZ);

   (ii) Intermediate supply; and/or

   (iii) Supply of goods to the categories mentioned in paragraph named, "Categories of Supply" with point (b), (c), (e), (f), (g) and (h) of this FTP.

   (iv) Supply of 'stores' on board of foreign going vessel / aircraft, subject to condition that there is specific Standard Input Output Norms in respect of item supplied.

Advance Authorisation for Annual Requirement

(i) Advance Authorisation for Annual Requirement shall only be issued for items notified in Standard Input Output Norms (SION), and it shall not be available in case of adhoc norms under (b)(ii) of paragraph heading, "Advance Authorisation" of FTP.

(ii) Advance Authorisation for Annual Requirement shall also not be available in respect of SION where any item of input appears in Appendix 4-J of AANF.

Eligibility Condition to obtain Advance Authorisation for Annual Requirement

(i) Exporters having past export performance (in at least preceding two financial years) shall be entitled for Advance Authorisation for Annual requirement.

(ii) Entitlement in terms of CIF value of imports shall be upto 300% of the FOB value of physical export and / or FOR value of deemed export in preceding financial year or ₹ 1 crore, whichever is higher.

Value Addition

Value Addition for the purpose of this Chapter (except for Gems and Jewellery sector for which value addition is prescribed in different heading of this study note shall be:-

A - B

VA = x 100, where

B

A = FOB value of export realized / FOR value of supply received.

B = CIF value of inputs covered by Authorisation, plus value of any other input used on which benefit of DBK is claimed or intended to be claimed.

Minimum Value Addition

(i) Minimum value addition required to be achieved under Advance Authorisation is 15%.

(ii) Export Products where value addition could be less than 15% are given in Appendix 4D of AANF.

(iii) For physical exports for which payments are not received in freely convertible currency, value addition shall be as specified in Appendix 4C of AANF.

(iv) Minimum value addition for Gems & Jewellery Sector is given in paragraph 4.61 of Handbook of Procedures.

(v) In case of Tea, minimum value addition shall be 50%.

Import of Mandatory Spares

Import of mandatory spares which are required to be exported / supplied with the resultant product shall be permitted duty free to the extent of 10% of CIF value of Authorisation.

Ineligible categories of import on Self Declaration basis

(a) Import of following products shall not be permissible on self-declaration basis:

- (i) All vegetable / edible oils classified under Chapter-15 and all types of oilseeds classified under Chapter-12 of ITC (HS) book;
- (ii) All types of cereals classified under Chapter–10 of ITC (HS) book;
- (iii) All Spices other than light black pepper (light berries) having a basic customs duty of more than 30%, classified under Chapter-9 and 12 of ITC (HS) book;
- (iv) All types of fruits/ vegetables having a duty of more than 30%, classified under Chapter-7 and Chapter-8 of ITC (HS) book;
- (v) Horn, hoof and any other organ of animal;
- (vi) Honey;
- (vii) Rough Marble Blocks/Slabs; and
- (viii) Rough Granite.
- (ix) Vitamins except for use in pharmaceutical industry.

(b) For export of perfumes, perfumery compounds and various feed ingredients containing vitamins, no Authorisation shall be issued by Regional Authority under paragraph 4.07 of Handbook of Procedures and applicants shall be required to apply under paragraph 4.06 of Hand Book of Procedures to the Norms Committee.

(c) Where export and/or import of biotechnology items and related products are involved, Authorisation under paragraph 4.07 of Handbook of Procedures shall be issued by Regional Authority only on submission of a "No Objection Certificate" from Department of Biotechnology.

Accounting of Input

(i) Wherever SION permits use of either (a) a generic input or (b) alternative input, unless the name of the specific input [which has been used in manufacturing the export product] gets indicated/ endorsed in the relevant shipping bill and these inputs, so endorsed, match the description in the relevant bill of entry, the concerned Authorisation will not be redeemed. In other words, the name/ description of the input used (or to be used) in the Authorisation must match exactly with the name/description endorsed in the shipping bill.

(ii) In addition, if in any SION, a single quantity has been indicated against a number of inputs (more than one input), then quantities of such inputs to be permitted for import shall be in proportion to the quantity of these inputs actually used/consumed in production, within overall quantity against such group of inputs. Proportion of these inputs actually used/consumed in production of export product shall be clearly indicated in shipping bills.

(iii) At the time of discharge of export obligation (issue of EODC) or at the time of redemption, Regional Authority shall allow only those inputs which have been specifically indicated in the shipping bill.

(iv) The above provisions will also be applicable for supplies to SEZs and supplies made under Deemed export. Details as given above will have to be indicated in the relevant Bill of Export, ARE-3, Central Excise certified Invoice / import document / document for domestic procurement/supply.

Pre-import condition in certain cases

(i) DGFT may, by Notification, impose pre-import condition for inputs under this Chapter.

(ii) Import items subject to pre-import condition are listed in Appendix 4-J of AANF or will be as indicated in Standard Input Output Norms (SION).

(iii) Import of drugs from unregistered sources shall have pre-import condition.

Details of Duties exempted

Imports under Advance Authorisation are exempted from payment of Basic Customs Duty, Additional Customs Duty, Education Cess, Anti-dumping Duty, Safeguard Duty and Transition Product Specific Safeguard Duty, wherever applicable. However, Import against supplies covered under previous paragraph with point (c), (d) and (g) of FTP will not be exempted from payment of applicable Anti-dumping Duty, Safeguard Duty and Transition Product Specific Safeguard Duty, if any.

Admissibility of Drawback

Drawback as per rate determined and fixed by Central Excise authority shall be available for duty paid imported or indigenous inputs (not specified in the norms) used in the export product. For this purpose, applicant shall indicate clearly details of duty paid input in the application for Advance Authorisation. As per details mentioned in the application, Regional Authority shall also clearly endorse details of such duty paid inputs in the condition sheet of the Advance Authorisation.

Actual User Condition for Advance Authorisation

(i) Advance Authorisation and / or material imported under Advance Authorisation shall be subject to 'Actual User' condition. The same shall not be transferable even after completion of export obligation. However, Authorisation holder will have option to dispose of product manufactured out of duty free input once export obligation is completed.

(ii) In case where CENVAT credit facility on input has been availed for the exported goods, even after completion of export obligation, the goods imported against such Advance Authorisation shall be utilized only in the manufacture of dutiable goods whether within the same factory or outside (by a supporting manufacturer). For this, the Authorisation holder shall produce a certificate from either the jurisdictional Central Excise Authority or Chartered Accountant, at the option of the exporter, at the time of filing application for Export Obligation Discharge Certificate to Regional Authority concerned.

(iii) Waste / scrap arising out of manufacturing process, as allowed, can be disposed off on payment of applicable duty even before fulfillment of export obligation.

Validity Period for Import

(i) Validity period for import of Advance Authorisation shall be 12 months from the date of issue of Authorisation.

(ii) Advance Authorisation for Deemed Export shall be co-terminus with contracted duration of project execution or 12 months from the date of issue of Authorisation, whichever is more.

Importability / Exportability of items that are Prohibited/Restricted/ STE

(i) No export or import of an item shall be allowed under Advance Authorisation / DFIA if the item is prohibited for exports or imports respectively. Export of a prohibited item may be allowed under Advance Authorisation provided it is separately so notified, subject to the conditions given therein.

(ii) Items reserved for imports by STEs cannot be imported against Advance Authorisation / DFIA. However those items can be procured from STEs against ARO or Invalidation letter. STEs are also allowed to sell goods on High Sea Sale basis to holders of Advance Authorisation / DFIA holder. STEs are also permitted to issue "No Objection Certificate (NOC)" for import by Advance Authorisation / DFIA holder. Authorisation Holder would be required to file Quarterly Returns of imports effected against such NOC to concerned STE and STE would submit half-yearly import figures of such imports to concerned administrative Department for monitoring with a copy endorsed to DGFT.

(iii) Items reserved for export by STE can be exported under Advance Authorisation / DFIA only after obtaining a 'No Objection Certificate' from the concerned STE.

(iv) Import of restricted items shall be allowed under Advance Authorisation/ DFIA.

(v) Export of restricted / SCOMET items however, shall be subject to all conditionalities or requirements of export authorisation or permission, as may be required, under Schedule 2 of ITC (HS).

Free of Cost Supply by Foreign Buyer

Advance Authorisation shall also be available where some or all inputs are supplied free of cost to exporter by foreign buyer. In such cases, notional value of free of cost input shall be added in the CIF value of import and FOB value of export for the purpose of computation of value addition. However, realization of export proceeds will be equivalent to an amount excluding notional value of such input.

Domestic Sourcing of Inputs

(i) Holder of an Advance Authorisation / Duty Free Import Authorisation can procure inputs from indigenous supplier/ State Trading Enterprise in lieu of direct import. Such procurement can be against Advance Release Order (ARO), Invalidation Letter, Back-to-Back Inland Letter of Credit.

(ii) When domestic supplier intends to obtain duty free material for inputs through Advance Authorisation for supplying resultant product to another Advance Authorisation / DFIA / EPCG Authorisation, Regional Authority shall issue Invalidation Letter.

(iii) Regional Authority shall issue Advance Release Order if the domestic supplier intends to seek refund of duty through Deemed Exports mechanism.

(iv) Regional Authority may issue Advance Release Order or Invalidation Letter at the time of issue of Authorisation simultaneously or subsequently.

(v) Advance Authorisation holder under DTA can procure inputs from EOU / EHTP / BTP / STP / SEZ units without obtaining Advance Release Order or Invalidation Letter.

(vi) Duty Free Import Authorisation holder shall also be eligible for Advance Release Order / Invalidation Letter facility.

(vii) Validity of Advance Release Order / Invalidation Letter shall be co-terminous with validity of Authorisation.

Currency for Realisation of Export Proceeds

(i) Export proceeds shall be realized in freely convertible currency except otherwise specified. Provisions regarding realization of export proceeds are given this study note.

(ii) Export to Rupee Payment Area (RPA) (for which payments are not received in freely convertible currency) shall be subject to minimum value addition as specified in Appendix-4C of AANF.

(iii) Export to SEZ Units shall be taken into account for discharge of export obligation provided payment is realised from Foreign Currency Account of the SEZ unit.

(iv) Export to SEZ Developers / Co-developers can also be taken into account for discharge of export obligation even if payment is realised in Indian Rupees.

(v) Authorisation holder needs to file Bill of Export for export to SEZ unit / developer / co-developer in accordance with the procedures given in SEZ Rules, 2006.

Export Obligation

(i) Period for fulfilment of export obligation under Advance Authorisation shall be 18 months from the date of issue of Authorisation or as notified by DGFT.

(ii) In cases of supplies to turnkey projects in India under deemed export category or turnkey projects abroad, the Export Obligation period shall be co-terminus with contracted duration of the project execution or 18 months whichever is more.

(iii) Export Obligation for items falling in categories of defence, military store, aerospace and nuclear energy shall be 24 months from the date of issue of authorization or co-terminus with contracted duration of the export order whichever is more.

(iv) Export Obligation Period for specified inputs, from the date of clearance of each consignment, is given in Appendix 4-J of AANF.

Export Obligation Period (EOP) Extension for units under BIFR/ Rehabilitation.

A company holding Advance Authorisation and registered with BIFR / Rehabilitation Department of State Government or any firm / company acquiring a unit holding Advance Authorisation which is under BIFR / Rehabilitation, may be permitted export obligation extension for the Advance Authorisation(s) held by the acquired unit, as per rehabilitation package prepared by operating agency and approved by BIFR / Rehabilitation Department of State Government. If time-period upto which EO extension is to be granted is not specifically mentioned in the BIFR order, EO extension of two years from the date of expiry of EOP (including extended period) or the date of BIFR order, whichever is later, shall be granted without payment of composition fee.

Re-import of exported goods under Duty Exemption / Remission Scheme

Goods exported under Advance Authorisation / Duty Free Import Authorisation may be re-imported in same or substantially same form subject to such conditions as may be specified by Department of Revenue. Authorisation holder shall also inform about such re-importation to the Regional Authority which had issued the Authorisation within one month from date of re-import.

DUTY FREE IMPORT AUTHORISATION SCHEME (DFIA)

DFIA Scheme

Duty Free Import Authorisation is issued to allow duty free import of inputs. In addition, import of oil and catalyst which is consumed / utilised in the process of production of export product, may also be allowed.

Duties Exempted and Admissibility of Cenvat and Drawback

(i) Duty Free Import Authorisation shall be exempted only from payment of Basic Customs Duty.

(ii) Additional customs duty/excise duty, being not exempt, shall be adjusted as CENVAT credit as per DoR rules.

(iii) Drawback as per rate determined and fixed by Central Excise authority shall be available for duty paid inputs, whether imported or indigenous, used in the export product. However, in case such drawback is claimed for inputs not specified in SION, the applicant should have indicated clearly details of such duty paid inputs also in the application for Duty Free Import Authorization, and as per the details mentioned in the application, the Regional Authority should also have clearly endorsed details of such duty paid inputs in the condition sheet of the Duty Free Import Authorization.

Eligibility

(i) Duty Free Import Authorisation shall be issued on post export basis for products for which Standard Input Output Norms have been notified.

(ii) Merchant Exporter shall be required to mention name and address of supporting manufacturer of the export product on the export document viz. Shipping Bill / Airway Bill / Bill of Export / ARE-1 / ARE-3.

(iii) Application is to be filed with concerned Regional Authority before effecting export under Duty Free Import Authorisation.

Minimum Value Addition

Minimum value addition of 20% shall be required to be achieved. For items where higher value addition has been prescribed under Advance Authorisation in Appendix 4C of AANF, the same value addition shall be applicable for Duty Free Import Authorisation also.

Validity & Transferability of DFIA

(i) Applicant shall file online application to Regional Authority concerned before starting export under DFIA.

(ii) Export shall be completed within 12 months from the date of online filing of application and generation of file number.

(iii) While doing export/supply, applicant shall indicate file number on the export documents viz. Shipping Bill / Airway Bill/ Bill of Export / ARE-1 / ARE-3, Central Excise certified Invoice.

(iv) After completion of exports and realization of proceeds, request for issuance of transferable Duty Free Import Authorisation may be made to concerned Regional Authority within a period of twelve months from the date of export or six months (or additional time allowed by RBI for realization) from the date of realization of export proceeds, whichever is later.

(v) Applicant shall be allowed to file application beyond 24 months from the date of generation of file number as per paragraph 9.03 of Hand Book of Procedures.

(vi) Separate DFIA shall be issued for each SION and each port.

(vii) Exports under DFIA shall be made from from a single port as mentioned in paragraph 4.37 of Handbook of Procedures.

(viii) No Duty Free Import Authorisation shall be issued for an export product where SION prescribes 'Actual User' condition for any input.

(ix) Regional Authority shall issue transferable DFIA with a validity of 12 months from the date of issue. No further revalidation shall be granted by Regional Authority.

Sensitive Items under Duty Free Import

Authorisation

(a) In respect of resultant products requiring following inputs, exporter shall be required to provide declaration with regard to technical characteristics, quality and specification in Shipping Bill:

"Alloy steel including Stainless Steel, Copper Alloy, Synthetic Rubber, Bearings, Solvent, Perfumes / Essential Oil/ Aromatic Chemicals, Surfactants, Relevant Fabrics, marble, Articles made of polypropylene, Articles made of Paper and Paper Board, Insecticides, Lead Ingots, Zinc Ingots, Citric Acid, Relevant Glass fibre reinforcement (Glass fibre, Chopped / Stranded Mat, Roving Woven Surfacing Mat), Relevant Synthetic Resin (unsaturated polyester resin, Epoxy Resin, Vinyl Ester Resin, Hydroxy Ethyl Cellulose), Lining Material".

(b) While issuing Duty Free Import Authorisation, Regional Authority shall mention technical characteristics, quality and specification in respect of above inputs in the Authorisation.

SCHEMES FOR EXPORTERS OF GEMS AND JEWELLERY

Import of Input

Exporters of gems and Jewellery can import / procure duty free input for manufacture of export product.

Items of Export

Following items, if exported, would be eligible:

(i) Gold jewellery, including partly processed jewellery and articles including medallions and coins (excluding legal tender coins), whether plain or studded, containing gold of 8 carats and above;

(ii) Silver jewellery including partly processed jewellery, silverware, silver strips and articles including medallions and coins (excluding legal tender coins and any engineering goods) containing more than 50% silver by weight;

(iii) Platinum jewellery including partly processed jewellery and articles including medallions and coins (excluding legal tender coins and any engineering goods) containing more than 50% platinum by weight.

Schemes

The schemes are as follows:

(i) Advance Procurement / Replenishment of Precious Metals from Nominated Agencies;

(ii) Replenishment Authorisation for Gems;

(iii) Replenishment Authorisation for Consumables;

(iv) Advance Authorisation for Precious Metals.

Advance Procurement/ Replenishment of Precious Metals from Nominated Agencies

(i) Exporter of gold / silver / platinum jewellery and articles thereof including mountings and findings may obtain gold / silver / platinum as an input for export product from Nominated Agency, in advance or as replenishment after export in accordance with the procedure specified in this behalf.

(ii) The export would be subject to wastage norms and minimum value addition as prescribed in paragraph 4.60 and 4.61 respectively in the Handbook of Procedures.

Replenishment Authorisation for Gems

(i) Exporter may obtain Replenishment Authorisation for Gems from Regional Authority in accordance with procedure specified in Handbook of Procedures.

(ii) Replenishment Authorisation for Gems may be issued against export including that made against supply by Nominated Agency and against supply by foreign buyer.

(iii) In case of plain or studded gold / silver / platinum jewellery and articles, value of such Authorisation shall be determined with reference to realisation in excess of prescribed minimum value addition. Replenishment Authorisation for Gems shall be freely transferable.

(iv) Replenishment Rate and item of import will be as prescribed in Appendix 4G of AANF.

Replenishment Authorisation for Consumables

(i) Replenishment authorization for duty free import of Consumables, Tools and other items namely, Tags and labels, Security censor on card, Staple wire, Poly bag (as notified by Customs) for Jewellery made out of precious metals (other than Gold & Platinum) equal to 2% and for Cut and Polished Diamonds and Jewellery made out of Gold and Platinum equal to 1% of FOB value of exports of the preceding year, may be issued on production of Chartered Accountant Certificate indicating the export performance. However, in case of Rhodium finished Silver jewellery, entitlement will be 3% of FOB value of exports of such jewellery. This Authorisation shall be non-transferable and subject to actual user condition.

(ii) Application for import of consumables as given above shall be filed online to the concerned Regional Authority in ANF 4H of AANF.

Advance Authorisation for Precious Metals.

(a) Advance Authorisation shall be granted on pre-import basis with 'Actual User' condition for duty free import of:

  (i) Gold of fineness not less than 0.995 and mountings, sockets, frames and findings of 8 carats and above;

(ii) Silver of fineness not less than 0.995 and mountings, sockets, frames and findings containing more than 50% silver by weight;

(iii) Platinum of fineness not less than 0.900 and mountings, sockets, frames and findings containing more than 50% platinum by weight.

(b) Advance Authorization shall carry an export obligation which shall be fulfilled as per procedure indicated in Chapter 4 of Handbook of Procedures.

(c) Value Addition shall be as per previous paragraph of this study note and 4.61 of Handbook of Procedures.

Value Addition

Minimum Value Addition norms for gems and jewellery sector are given in paragraph 4.61 of Handbook of Procedures. It would be calculated as under:

A - B

VA = x 100, where

B

A = FOB value of the export realised / FOR value of supply received.

B = Value of inputs (including domestically procured) such as gold / silver / platinum content in export product plus admissible wastage along with value of other items such as gemstone etc. Wherever gold has been obtained on loan basis, value shall also include interest paid in free foreign exchange to foreign supplier.

Wastage Norms

Wastage or manufacturing loss for gold / silver / platinum jewellery shall be admissible as per paragraph 4.60 of Handbook of Procedures.

DFIA not available

Duty Free Import Authorisation scheme shall not be available for Gems and Jewellery sector.

Nominated Agencies

(i) Exporters may obtain gold / silver / platinum from Nominated Agency. Exporter in EOU and units in SEZ would be governed by the respective provisions of Chapter-6 of FTP / SEZ Rules, respectively.

(ii) Nominated Agencies are MMTC Ltd, The Handicraft and Handlooms Exports Corporation of India Ltd, The State Trading Corporation of India Ltd, PEC Ltd, STCL Ltd, MSTC Ltd, and Diamond India Limited

(iii) Four Star Export House from Gems & Jewellery sector and Five Star Export House from any sector may be recognized as Nominated Agency by Regional Authority.

(iv) Reserve Bank of India can authorize any bank as Nominated Agency.

(iv) Procedure for import of precious metal by Nominated Agency (other than those authorized by Reserve Bank of India and the Gems & Jewellery units operating under EOU and SEZ schemes) and the monitoring mechanism thereof shall be as per the provisions laid down in Hand Book of Procedures.

(v) A bank authorised by Reserve Bank of India is allowed export of gold scrap for refining and import standard gold bars as per Reserve Bank of India guidelines.

Import of Diamonds for Certification / Grading & Re-export

Following agencies are permitted to import diamonds to their laboratories without any import duty, for the purpose of certification / grading reports, with a condition that the same should be re-exported with the certification/grading reports, as per the procedure laid down in Hand Book of Procedures:

(1) Gemological Institute of America (GIA), Mumbai, Maharashtra.

(2) Indian Diamond Institute, Surat, Gujarat, India.

(3) International Institute of Diamond Grading & Research India Pvt Ltd., Surat, Gujarat, India.

Export of Cut & Polished Diamonds for Certification/ Grading & Re-import

List of authorized laboratories for certification / grading of diamonds of 0.25 carat and above are given in paragraph 4.74 of Handbook of Procedures.

Export of Cut & Polished Diamonds with Re-import Facility at Zero Duty

An exporter (with annual export turnover of ₹ 5 crores for each of the last three years) may export cut & polished diamonds (each of 0.25 carat or above) to any of the agencies/laboratories mentioned under paragraph 4.74 of Handbook of Procedures with re-import facility at zero duty within 3 months from the date of export. Such facility of re-import at zero duty will be subject to guidelines issued by Central Board of Customs & Excise, Department of Revenue.

Export against Supply by Foreign Buyer

(i) Where export orders are placed on nominated agencies / status holder / exporters of three years standing having an annual average turnover of Rupees five crores during preceding three financial years, foreign buyer may supply in advance and free of charge, gold / silver / platinum, alloys, findings and mountings of gold / silver / platinum for manufacture and export.

(ii) Such supplies can also be in advance and may involve semi-finished jewellery including findings / mountings / components for repairs / re-make and export subject to minimum value addition as prescribed under paragraph 4.61 of Handbook of Procedures. In such cases of export, wastage norms as per paragraph 4.60 of Handbook of Procedures shall apply.

(iii) Exports may be made by nominated agencies directly or through their associates or by status holder / exporter. Import and Export of findings shall be on net to net basis.

Export Promotion Tours/ Export of Branded Jewellery

(i) Nominated Agencies and their associates, with approval of Department of Commerce and with approval of Gem & Jewellery Export Promotion Council (GJEPC), may export gold / silver / platinum jewellery and articles thereof for exhibitions abroad.

(ii) Personal carriage of gold / silver / platinum jewellery, precious, semi-precious stones, beads and articles and export of branded jewellery is also permitted, subject to conditions as in Handbook of Procedures.

Personal Carriage of Export / Import Parcels

Personal carriage of gems and jewellery export parcels by foreign bound passengers and import parcels by an Indian importer/foreign national may be permitted as per the Handbook of Procedures.

Export by Post

Export of jewellery through Foreign Post Office including via Speed Post is allowed. The jewellery parcel shall not exceed 20 kgs by weight.

Private / Public Bonded Warehouse

Private / Public Bonded Warehouses may be set up in SEZ/DTA for import and re-export of cut and polished diamonds, cut and polished coloured gemstones, uncut & unset precious & semi-precious stones, subject to achievement of minimum value addition of 5% by DTA units.

Diamond & Jewellery Dollar Accounts

(a) Firms and companies dealing in purchase / sale of rough or cut and polished diamonds / precious metal jewellery plain, minakari and / or studded with / without diamond and / or other stones with a track record of at least two years in import or export of diamonds / coloured gemstones / diamond and coloured gemstones studded jewellery / plain gold jewellery and having an average annual turnover of ₹3 crore or above during preceding three licensing years may also carry out their business through designated Diamond Dollar Accounts (DDA).

(b) Dollars in such accounts available from bank finance and / or export proceeds shall be used only for:

(i) Import / purchase of rough diamonds from overseas/ local sources;

(ii) Purchase of cut and polished diamonds, coloured gemstones and plain gold jewellery from local sources;

(iii) Import / purchase of gold from overseas / nominated agencies and repayment of dollar loans from the bank; and

(iv) Transfer to Rupee Account of exporter.

Details of this DDA Scheme are given in Handbook of Procedures.

(c) A non DDA holder is also permitted to supply cut and polished diamonds to DDA holder, receive payment in dollars and convert the same into Rupees within 7 days. Cut and polished diamonds and coloured gemstones so supplied by non-DDA holder will also be counted towards discharge of his export obligation and/ or entitle him to replenishment Authorisation.

Export of cut & polished precious and semi precious stones for treatment and re-import

Gems and Jewellery exporters shall be allowed to export cut and polished precious and semi-precious stones for the treatment and re-import as per customs rules and regulations. In case of re-export, the exporter shall be entitled for duty drawback as per rules.

Re-import of rejected Jewellery

Gems & Jewellery exporters shall be allowed to re-import rejected precious metal jewellery as per paragraph 4.91 of Handbook of Procedures.

Export and import on consignment basis

Gems & Jewellery exporters shall be allowed to export and import diamond, gemstones & jewellery on consignment basis as per Handbook of Procedures and Customs Rules and Regulations.

5.5 EXPORTS PROMOTION CAPITAL GOODS (EPCG) SCHEME

Objective

The objective of the EPCG Scheme is to facilitate import of capital goods for producing quality goods and services to enhance India's export competitiveness.

EPCG Scheme

(a) EPCG Scheme allows import of capital goods for pre-production, production and post-production at Zero customs duty. Alternatively, the Authorisation holder may also procure Capital Goods from indigenous sources. Capital goods for the purpose of the EPCG scheme shall include:

(i) Capital Goods as defined in Chapter 9 including in CKD/SKD condition thereof;

(ii) Computer software systems;

(iii) Spares, moulds, dies, jigs, fixtures, tools & refractories for initial lining and spare refractories; and

(iv) catalysts for initial charge plus one subsequent charge.

(b) Import of capital goods for Project Imports notified by Central Board of Excise and Customs is also permitted under EPCG Scheme.

(c) Import under EPCG Scheme shall be subject to an export obligation equivalent to 6 times of duty saved on capital goods, to be fulfilled in 6 years reckoned from date of issue of Authorisation.

(d) Authorisation shall be valid for import for 18 months from the date of issue of Authorisation. Revalidation of EPCG Authorisation shall not be permitted.

(e) In case countervailing duty (CVD) is paid in cash on imports under EPCG, incidence of CVD would not be taken for computation of net duty saved, provided CENVAT is not availed.

(f) Second hand capital goods shall not be permitted to be imported under EPCG Scheme.

(g) Authorisation under EPCG Scheme shall not be issued for import of any Capital Goods (including Captive plants and Power Generator Sets of any kind) for

(i) Export of electrical energy (power)

(ii) Supply of electrical energy (power) under deemed exports

(iii) Use of power (energy) in their own unit, and

(iv) Supply/export of electricity transmission services

(h) Import of items which are restricted for import shall be permitted under EPCG Scheme only after approval from Exim Facilitation Committee (EFC) at DGFT Headquarters.

(i) If the goods proposed to be exported under EPCG authorisation are restricted for export, the EPCG authorisation shall be issued only after approval for issuance of export authorisation from Exim Facilitation Committee at DGFT Headquarters.

Coverage

(a) EPCG scheme covers manufacturer exporters with or without supporting manufacturer(s), merchant exporters tied to supporting manufacturer(s) and service providers. Name of supporting manufacturer(s) shall be endorsed on the EPCG authorisation before installation of the capital goods in the factory / premises of the supporting manufacturer (s). In case of any change in supporting manufacturer (s) the RA shall intimate such change to jurisdictional Central Excise Authority of existing as well as changed supporting manufacturer (s) and the Customs at port of registration of Authorisation.

(b) Export Promotion Capital Goods (EPCG) Scheme also covers a service provider who is designated / certified as a Common Service Provider (CSP) by the DGFT, Department of Commerce or State Industrial Infrastructural Corporation in a Town of Export Excellence subject to provisions of Foreign Trade Policy/Handbook of Procedures with the following conditions:-

(i) Export by users of the common service, to be counted towards fulfilment of EO of the CSP shall contain the EPCG authorisation details of the CSP in the respective Shipping bills and concerned RA must be informed about the details of the Users prior to such export;

(ii) Such export will not count towards fulfilment of specific export obligations in respect of other EPCG authorisations (of the CSP/User); and

(iii) Authorisation holder shall be required to submit Bank Guarantee (BG) which shall be equivalent to the duty saved. BG can be given by CSP or by any one of the users or a combination thereof, at the option of the CSP.

Actual User Condition

Import of capital goods shall be subject to Actual User condition till export obligation is completed.

Export Obligation (EO)

Following conditions shall apply to the fulfilment of EO:-

(a) EO shall be fulfilled by the authorisation holder through export of goods which are manufactured by him or his supporting manufacturer / services rendered by him, for which the EPCG authorisation has been granted.

(b) EO under the scheme shall be, over and above, the average level of exports achieved by the applicant in the preceding three licensing years for the same and similar products within the overall EO period including extended period, if any; except for categories mentioned in paragraph 5.13(a) of HBP. Such average would be the arithmetic mean of export performance in the preceding three licensing years for same and similar products.

(c) In case of indigenous sourcing of Capital Goods, specific EO shall be 25% less than the EO stipulated.

(d) Shipments under Advance Authorisation, DFIA, Drawback scheme or reward schemes; would also count for fulfillment of EO under EPCG Scheme.

(e) Export shall be physical export. However, deemed exports as specified in points (a), (b), (e), (f) & (h) of paragraph, "Categories of Supplies" of FTP shall also be counted towards fulfillment of export obligation, alongwith usual benefits available under paragraph named, "Benefits for Deemed Exports" of FTP.

(f) EO can also be fulfilled by the supply of ITA-I items to DTA, provided realization is in free foreign exchange.

(g) Royalty payments received by the Authorisation holder in freely convertible currency and foreign exchange received for R&D services shall also be counted for discharge under EPCG.

(h) Payment received in rupee terms for such Services as notified in Appendix 3E of AANF shall also be counted towards discharge of export obligation under the EPCG scheme.

Provision for units under BIFR /Rehabilitation

A company holding EPCG authorisation and registered with BIFR / Rehabilitation Department of State Government or any firm/ company acquiring a unit holding EPCG authorisation which is under BIFR / Rehabilitation, may be permitted EO extension for the EPCG authorisation(s) held by the acquired unit, as per rehabilitation package prepared by operating agency and approved by BIFR / Rehabilitation Department of State Government. If time-period upto which EO extension is to be granted is not specifically mentioned in the BIFR order, EO extension of 3 years from the date of expiry of EOP (including extended period) or the date of BIFR order, whichever is later, shall be granted without payment of composition fee.

LUT/Bond/BG in case of Agro units

LUT/Bond or 15% BG, as applicable, may be furnished for EPCG authorisation granted to units in Agri-Export Zones provided EPCG authorisation is taken for export of primary agricultural product(s) notified or their value added variants.

Indigenous Sourcing of Capital Goods and benefits to Domestic Supplier

A person holding an EPCG authorisation may source capital goods from a domestic manufacturer. Such domestic manufacturer shall be eligible for deemed export benefit. Such domestic sourcing shall also be permitted from EOUs and these supplies shall be counted for purpose of fulfilment of positive NFE by said EOU.

Calculation of Export Obligation

In case of direct imports, EO shall be reckoned with reference to actual duty saved amount. In case of domestic sourcing, EO shall be reckoned with reference to notional Customs duties saved on FOR value.

Incentive for early EO fulfilment

With a view to accelerating exports, in cases where Authorisation holder has fulfilled 75% or more of specific export obligation and 100% of Average Export Obligation till date, if any, in half or less than half the original export obligation period specified, remaining export obligation shall be condoned and the Authorisation redeemed by RA concerned. However no benefit under para 5.21 of HBP shall be permitted where incentive for early EO fulfilment has been availed.

Reduced EO for Green Technology Products

For exporters of Green Technology Products, Specific EO shall be 75% of EO. There shall be no change in average EO imposed, if any. The list of Green Technology Products is given in Para 5.29 of HBP.

Reduced EO for North East Region and Jammu & Kashmir

For units located in Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, Tripura and Jammu & Kashmir, specific EO shall be 25% of the EO. There shall be no change in average EO imposed, if any.

Post Export EPCG Duty Credit Scrip(s)

(a) Post Export EPCG Duty Credit Scrip(s) shall be available to exporters who intend to import capital goods on full payment of applicable duties in cash and choose to opt for this scheme.

(b) Basic Customs duty paid on Capital Goods shall be remitted in the form of freely transferable duty credit scrip(s).

(c) Specific EO shall be 85% of the applicable specific EO under the EPCG Scheme. However, average EO shall remain unchanged.

(d) Duty remission shall be in proportion to the EO fulfilled.

(e) All provisions for utilization of scrips issued shall also be applicable to Post Export EPCG Duty Credit Scrip (s).

(f) All provisions of the existing EPCG Scheme shall apply insofar as they are not inconsistent with this scheme.

5.6 EXPORT ORIENTED UNITS (EOUs), ELECTRONICS HARDWARE TECHNOLOGY PARKS (EHTPs), SOFTWARE TECHNOLOGY PARKS (STPs) AND BIO-TECHNOLOGY PARKS (BTPs)

Introduction and Objective

(a) Units undertaking to export their entire production of goods and services (except permissible sales in DTA), may be set up under the Export Oriented Unit (EOU) Scheme, Electronics Hardware Technology Park (EHTP) Scheme, Software Technology Park (STP) Scheme or Bio-Technology Park (BTP) Scheme for manufacture of goods, including repair, re-making, reconditioning, re-engineering, rendering of services, development of software, agriculture including agro-processing, aquaculture, animal husbandry, biotechnology, floriculture, horticulture, pisciculture, viticulture, poultry and sericulture. Trading units are not covered under these schemes.

(b) Objectives of these schemes are to promote exports, enhance foreign exchange earnings, attract investment for export production and employment generation.

Export and Import of Goods

(a) An EOU / EHTP / STP / BTP unit may export all kinds of goods and services except items that are prohibited in ITC (HS).

(b) Export of Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET) shall be subject to fulfilment of the conditions indicated in ITC (HS). In respect of an EOU, permission to export a prohibited item may be considered, by BOA, on a case to case basis, provided such raw materials are imported and there is no procurement of such raw material from DTA.

(c) Procurement and supply of export promotion material like brochure / literature, pamphlets, hoardings, catalogues, posters etc up to a maximum value limit of 1.5% of FOB value of previous years exports shall also be allowed.

(d) An EOU / EHTP / STP / BTP unit may import and / or procure, from DTA or bonded warehouses in DTA / international exhibition held in India, without payment of duty, all types of goods, including capital goods, required for its activities, provided they are not prohibited items of import in the ITC (HS). Any permission required for import under any other law shall be applicable. Units shall also be permitted to import goods including capital goods required for approved activity, free of cost or on loan / lease from clients. Import of capital goods will be on a self-certification basis. Goods imported by a unit shall be with actual user condition and shall be utilized for export production.

(e) State Trading regime shall not apply to EOU manufacturing units. However, in respect of Chrome Ore / Chrome concentrate, State Trading Regime as stipulated in export policy of these items, will be applicable to EOUs.

(f) EOU / EHTP / STP / BTP units may import / procure from DTA, without payment of duty, certain specified goods for creating a central facility. Software EOU / DTA units may use such facility for export of software.

(g) An EOU engaged in agriculture, animal husbandry, aquaculture, floriculture, horticulture, pisciculture, viticulture, poultry or sericulture may be permitted to remove specified goods in connection with its activities for use outside bonded area.

(h) Gems and jewellery EOUs may source gold / silver / platinum through nominated agencies on loan / outright purchase basis. Units obtaining gold / silver / platinum from nominated agencies, either on loan basis or outright purchase basis shall export gold / silver / platinum within 90 days from date of release.

(i) EOU / EHTP / STP / BTP units, other than service units, may export to Russian Federation in Indian Rupees against repayment of State Credit/ Escrow Rupee Account of buyer subject to RBI clearance, if any.

(j) Procurement and export of spares / components, upto 5% of FOB value of exports, may be allowed to same consignee / buyer of the export article, subject to the condition that it shall not count for NFE and direct tax benefits.

(k) BOA may allow, on a case to case basis, requests of EOU / EHTP / STP/ BTP units in sectors other than Gems & Jewellery, for consolidation of goods related to manufactured articles and export thereof along with manufactured article. Such goods may be allowed to be imported / procured from DTA by EOU without payment of duty, to the extent of 5% FOB value of such manufactured articles exported by the unit in preceding financial year. Details of procured / imported goods and articles manufactured by the EOU will be listed separately in the export documents. In such cases, value of procured / imported goods will not be taken into account for calculation of NFE and DTA sale entitlement. Such procured / imported goods shall not be allowed to be sold in DTA. BOA may also specify any other conditions.

Secondhand Capital goods

Second hand capital goods, without any age limit, may also be imported duty free.

Leasing of Capital Goods

(a) An EOU / EHTP / STP / BTP unit may, on the basis of a firm contract between parties, source capital goods from a domestic / foreign leasing company without payment of customs / excise duty. In such a case, EOU / EHTP / STP / BTP unit and domestic / foreign leasing company shall jointly file documents to enable import / procurement of capital goods without payment of duty.

(b) An EOU / EHTP / BTP / STP unit may sell capital goods and lease back the same from a Non Banking Financial Company (NBFC), subject to the following conditions:

   (i) The unit should obtain permission from the jurisdictional Deputy / Assistant Commissioner of Customs or Central Excise, for entering into transaction of 'Sale and Lease Back of Assets', and submit full details of the goods to be sold and leased back and the details of NBFC;

   (ii) The goods sold and leased back shall not be removed from the unit's premises;

   (iii) The unit should be NFE positive at the time when it enters into sale and lease back transaction with NBFC;

   (iv) A joint undertaking by the unit and NBFC should be given to pay duty on goods in case of violation or contravention of any provision of the notification under which these goods were imported or procured, read with Customs Act, 1962 or Central Excise Act, 1944, and that the lien on the goods shall remain with the Customs / Central Excise Department, which will have first charge over the said goods for recovery of sum due from the unit to Government under provision of Section 142(b) of the Customs Act, 1962 read with the Customs (Attachment of Property of Defaulters for Recovery of Govt. Dues) Rules, 1995.

Net Foreign Exchange Earnings

EOU / EHTP / STP / BTP unit shall be a positive net foreign exchange earner except for sector specific provision of Appendix 6 B of Appendices & ANFs, where a higher value addition shall be required. NFE Earnings shall be calculated cumulatively in blocks of five years, starting from commencement of production. Whenever a unit is unable to achieve NFE due to prohibition / restriction imposed on export of any product mentioned in LoP, the five year block period for calculation of NFE earnings may be suitably extended by BoA. Further, wherever a unit is unable to achieve NFE due to adverse market condition or any grounds of genuine hardship having adverse impact on functioning of the unit, the five year block period for calculation of NFE earnings may be extended by BOA for a period of upto one year, on a case to case basis.

Letter of Permission / Letter of Intent and Legal Undertaking

(a) On approval, a Letter of Permission (LoP) / Letter of Intent (LoI) shall be issued by DC / designated officer to EOU/ EHTP / STP / BTP unit. LoP / LoI shall have an initial validity of 2 years to enable the Unit to construct the plant & install the machinery and by this time the unit should have commenced production. In case the unit is not able to commence production in initial validity of 2 years, an extension of one year may be given by the DC for valid reasons to be recorded in writing. Subsequent extension of one year may be given by the Unit Approval Committee subject to condition that two-thirds of activities including construction, relating to the setting up of the Unit are complete and Chartered Engineer's certificate to this effect is submitted by the Unit. Further extension, if necessary, will be granted by the Board of Approval. Once unit commences production, LoP / LoI issued shall be valid for a period of 5 years for its activities. This period may be extended further by DC for a period of 5 years at a time.

(b) LoP / LoI issued to EOU / EHTP / STP / BTP units by concerned authority, subject to compliance of provision in Para 6.01 above, would be construed as an Authorisation for all purposes.

(c) Unit shall execute an LUT with DC concerned. Failure to ensure positive NFE or to abide by any of the terms and conditions of LoP / LoI / IL / LUT shall render the unit liable to penal action under provisions of the FT (D&R) Act, as amended, and Rules and Orders made thereunder, without prejudice to action under any other law / rules and cancellation or revocation of LoP / LoI / IL.

Investment Criteria

Only projects having a minimum investment of ₹ 1 Crore in plant & machinery shall be considered for establishment as EOUs. However, this shall not apply to existing units, units in EHTP / STP / BTP, and EOUs in Handicrafts / Agriculture / Floriculture / Aquaculture / Animal Husbandry / Information Technology, Services, Brass Hardware and Handmade jewellery sectors. BOA may allow establishment of EOUs with a lower investment criteria.

Applications & Approvals

(a) Applications for setting up of units under EOU scheme shall be approved or rejected by the Units Approval Committee within 15 days as per criteria indicated in Handbook of Procedures (HBP).

(b) In other cases, approval may be granted by BOA set up for this purpose as indicated in HBP.

(c) Proposals for setting up EOU requiring industrial licence may be granted approval by DC after clearance of proposal by BOA and DIPP within 45 days.

(d) Applications for conversion into an EOU / EHTP / STP / BTP unit from existing DTA units, having an investment of ₹ 50 crores and above in plant and machinery or exporting ₹ 50 crores and above annually, shall be placed before BOA for a decision.

DTA Sale of Finished Products / Rejects / Waste/ Scrap / Remnants and By-products

Entire production of EOU / EHTP / STP / BTP units shall be exported subject to following:

(a) Units, other than gems and jewellery units, may sell goods upto 50% of FOB value of exports, subject to fulfilment of positive NFE, on payment of concessional duties. Within entitlement of DTA sale, unit may sell in DTA, its products similar to goods which are exported or expected to be exported from units. However, units which are manufacturing and exporting more than one product can sell any of these products into DTA, upto 90% of FOB value of export of the specific products, subject to the condition that total DTA sale does not exceed the overall entitlement of 50% of FOB value of exports for the unit, as stipulated above. No DTA sale at concessional duty shall be permissible in respect of motor cars, alcoholic liquors, books, tea (except instant tea), pepper & pepper products, marble and such other items as may be notified from time to time.

Such DTA sale shall also not be permissible to units engaged in activities of packaging / labelling / segregation / refrigeration / compacting / micronisation / pulverization / granulation / conversion of monohydrate form of chemical to anhydrous form or vice-versa. Sales made to a unit in SEZ shall also be taken into account for purpose of arriving at FOB value of export by EOU provided payment for such sales are made from Foreign Currency Account of SEZ unit. Sale to DTA would also be subject to mandatory requirement of registration of pharmaceutical products (including bulk drugs). An amount equal to Anti Dumping duty under section 9A of the Customs Tariff Act, 1975 leviable at the time of import, shall be payable on the goods used for the purpose of manufacture or processing of the goods cleared into DTA from the unit.

(b) For services, including software units, sale in DTA in any mode, including on line data communication, shall also be permissible up to 50% of FOB value of exports and /or 50% of foreign exchange earned, where payment of such services is received in foreign exchange.

(c) Gems and jewellery units may sell upto 10% of FOB value of exports of the preceding year in DTA, subject to fulfilment of positive NFE. In respect of sale of plain jewellery, recipient shall pay concessional rate of duty as applicable to sale from nominated agencies. In respect of studded jewellery, duty shall be payable as applicable.

(d) Unless specifically prohibited in LoP, rejects within an overall limit of 50% may be sold in DTA on payment of duties as applicable to sale under Sub - para 6.08 (a) on prior intimation to Customs authorities. Such sales shall be counted against DTA sale entitlement. Sale of rejects upto 5% of FOB value of exports shall not be subject to achievement of NFE.

(e) Scrap / waste / remnants arising out of production process or in connection therewith may be sold in DTA, as per SION notified under Duty Exemption Scheme, on payment of concessional duties as applicable, within overall ceiling of 50% of FOB value of exports. Such sales of scrap / waste / remnants shall not be subject to achievement of positive NFE. In respect of items not covered by norms, DC may fix ad-hoc norms for a period of six months and within this period, norms should be fixed by Norms Committee. Ad-hoc norms will continue till such time norms are fixed by Norms Committee. Sale of waste / scrap / remnants by units not entitled to DTA sale, or sales beyond DTA sale entitlement, shall be on payment of full duties. Scrap / waste / remnants may also be exported.

(f) There shall be no duties / taxes on scrap / waste / remnants, in case same are destroyed with permission of Customs authorities.

(g) By-products included in LoP may also be sold in DTA subject to achievement of positive NFE, on payment of applicable duties, within the overall entitlement of Sub - para (a) of para heading, "DTA Sale of finished products/Rejects/Waste/Scrap/Remnants and by-products. Sale of by-products by units not entitled to DTA sales, or beyond entitlements of Sub-para (a) of para heading, "DTA Sale of finished products/Rejects/Waste/Scrap/Remnants and by-products, shall also be permissible on payment of full duties.

(h) EOU / EHTP / STP / BTP units may sell finished products, except pepper and pepper products and marble, which are freely importable under FTP in DTA, under intimation to DC, against payment of full duties, provided they have achieved positive NFE. An amount equal to Anti Dumping duty under section 9A of the Customs Tariff Act, 1975 leviable at the time of import, shall be payable on the goods used for the purpose of manufacture or processing of the goods cleared into DTA from the unit.

(i) In case of units manufacturing electronics hardware and software, NFE and DTA sale entitlement shall be reckoned separately for hardware and software.

(j) In case of DTA sale of goods manufactured by EOU / EHTP / STP / BTP, where basic duty and CVD is nil, such goods may be considered as non-excisable for payment of duty.

(k) In case of new EOUs, advance DTA sale will be allowed not exceeding 50% of its estimated exports for first year, except pharmaceutical units where this will be based on its estimated exports for first two years.

(l) Units in Textile and Granite sectors shall have an option to sell goods into DTA on payment of an amount equal to aggregate of duties of excise leviable under section 3 of the Central Excise Act, 1944 or under any other law for the time being in force, on like goods produced or manufactured in India other than in an EOU, subject to the condition that they have not used duty paid imported inputs in excess of 3% of the FOB value of exports of the preceding year and they have achieved positive NFE. Once this option is exercised, the unit will not be allowed to import any duty free inputs for any purpose.

(m) Procurement of spares / components, up to 2% of the value of manufactured articles, cleared into DTA, during the preceding year, may be allowed for supply to the same consignee / buyer for the purpose of after-sale-service. The same can be cleared in DTA on payment of applicable duty but such clearances shall be within the overall entitlement of the unit for DTA sale at concessional rate of duty as prescribed in Para 6.08 (a) of FTP.

Other Supplies

Following supplies effected from EOU / EHTP / STP / BTP units will be counted for fulfilment of positive NFE. Such supplies shall not include "marble", except if such supply of marble is an inter unit supply as provided at Sub - para (c) below:

(a) Supplies effected in DTA to holders of Advance Authorisation / Advance Authorisation for annual requirement / DFIA under duty exemption / remission scheme / EPCG scheme. However, printing sector EOUs (or any other sector that may be notified in HBP), can't supply goods, where basic customs duty and CVD is nil or exempted otherwise, to holders of Advance Authorisation / Advance Authorization for annual requirement.

(b) Supplies effected in DTA against foreign exchange remittance received from overseas.

(c) Supplies to other EOU / EHTP / STP / BTP / SEZ units, provided that such goods are permissible for procurement.

(d) Supplies made to bonded warehouses set up under FTP and / or under section 65 of Customs Act and free trade and warehousing zones, where payment is received in foreign exchange.

(e) Supplies of goods and services to such organizations which are entitled for duty free import of such items in terms of general exemption notification issued by MoF, as may be provided in HBP.

(f) Supplies of Information Technology Agreement (ITA-1) items and notified zero duty telecom / electronics items.

(g) Supplies of items like tags, labels, printed bags, stickers, belts, buttons or hangers to DTA unit for export.

(h) Supply of LPG produced in an EOU refinery to Public Sector domestic oil companies for being supplied to household domestic consumers at subsidized prices under the Public Distribution System (PDS) Kerosene and Domestic LPG Subsidy Scheme, 2002, as notified by the Ministry of Petroleum and Natural Gas vide notification No. E-20029/18/2001-PP dated 28.01.2003 (hereinafter referred to as PDS Scheme) subject to the following conditions:-

   (i) Only supply of such quantity of LPG would be eligible for which Ministry of Petroleum and Natural Gas declines permission for export and requires the LPG to be cleared in DTA; and

   (ii) The Ministry of Finance by a notification has permitted duty free imports of LPG for supply under the aforesaid PDS Scheme.

Export through others

An EOU / EHTP / STP / BTP unit may export goods manufactured / software developed by it through another exporter or any other EOU / EHTP / STP / SEZ unit subject to conditions mentioned in Para 6.19 of HBP.

Entitlement for Supplies from the DTA

(a) Supplies from DTA to EOU / EHTP / STP / BTP units will be regarded as "deemed exports" and DTA supplier shall be eligible for relevant entitlements under heading 'deemed exports' of FTP, besides discharge of export obligation, if any, on the supplier. Notwithstanding the above, EOU / EHTP / STP / BTP units shall, on production of a suitable disclaimer from DTA supplier, be eligible for obtaining entitlements specified in same heading of FTP. For claiming deemed export duty drawback, they shall get brand rates fixed by DC wherever All Industry Rates of Drawback are not available.

(b) Suppliers of precious and semi-precious stones, synthetic stones and processed pearls from DTA to EOU shall be eligible for grant of Replenishment Authorisations at rates and for items mentioned in HBP.

(c) In addition, EOU / EHTP / STP / BTP units shall be entitled to following:-

   (i) Reimbursement of Central Sales Tax (CST) on goods manufactured in India. Simple interest @6% per annum will be payable on delay in refund of CST, if the case is not settled within 30 days of receipt of complete application (as in Para 9.10 (b) of HBP).

   (ii) Exemption from payment of Central Excise Duty on goods procured from DTA on goods manufactured in India.

   (iii) Reimbursement of duty paid on fuel procured from Domestic Oil Companies / Depots of Domestic Oil Public Sector Undertakings as per drawback rate notified by DGFT from time to time. Reimbursement of additional duty of excise levied on fuel under the Finance Acts would also be admissible.

   (iv) CENVAT Credit on service tax paid.

Other Entitlements

Other entitlements of EOU / EHTP / STP / BTP units are as under:

(a) Exemption from industrial licensing for manufacture of items reserved for SSI sector.

(b) Export proceeds will be realized within nine months.

(c) Units will be allowed to retain 100% of its export earnings in the EEFC account.

(d) Unit will not be required to furnish bank guarantee at the time of import or going for job work in DTA, where:

  (i) the unit has turnover of ₹ 5 crore or above;

  (ii) the unit is in existence for at least three years; and

  (iii) the unit:

    (1) has achieved positive NFE / export obligation wherever applicable;

    (2) has not been issued a show cause notice or a confirmed demand, during the preceding 3 years, on grounds other than procedural violations, under the penal provision of the Customs Act, the Central Excise Act, the Foreign Trade (Development & Regulation) Act, the Foreign Exchange Management Act, the Finance Act, 1994 covering Service Tax or any allied Acts or the rules made thereunder, on account of fraud / collusion / wilful mis-statement / suppression of facts or contravention of any of the provisions thereof;

(e) 100% FDI investment permitted through automatic route similar to SEZ units.

(f) Units shall pay duty on the goods produced or manufactured and cleared into DTA on monthly basis in the manner prescribed in the Central Excise Rules.

(g) The Units Approval Committee may consider on a case-to-case basis request for sharing of infrastructural facilities among EOUs and it shall forward its recommendation to the Board of Approval for its consideration. While accepting such proposals, the NFE obligations of the Units shall not be altered. Such facilities will be available to Units in EHTP / STP after getting approval from IMSC. However, sharing of facilities between EOUs and SEZ Units shall not be permitted.

Inter Unit Transfer

(a) Transfer of manufactured goods from one EOU / EHTP / STP / BTP unit to another EOU / EHTP / STP / BTP unit is allowed with prior intimation to concerned Development Commissioners of the transferer and transferee units as well as concerned Customs authorities, following procedure of in-bond movement of goods. Transfer of manufactured goods shall also be allowed from EOU / EHTP / STP / BTP unit to a SEZ developer or unit as per procedure prescribed in SEZ Rules, 2006.

(b) Capital goods may be transferred or given on loan to other EOU / EHTP / STP / BTP / SEZ units, with prior intimation to concerned DC and Customs authorities.

  Such transferred goods may also be returned by the second unit to the original unit in case of rejection or for any reason without payment of duty.

(c) Goods supplied by one unit of EOU / EHTP / STP / BTP to another unit shall be treated as imported goods for second unit for payment of duty, on DTA sale by second unit.

(d) In respect of a group of EOUs / EHTPs / STPs / BTP Units which source inputs centrally in order to obtain bulk discount and / or reduce cost of transportation and other logistics cost and / or to maintain effective supply chain, inter unit transfer of goods and services may be permitted on a case-to-case basis by the Unit Approval Committee. In case inputs so sourced are imported and then transferred to another unit, then value of the goods so transferred shall be taken as inflow for the unit transferring these goods and as outflow for the unit receiving these goods, for the purpose of calculation of NFE.

Sub – Contracting

(a) (i) EOU / EHTP / STP / BTP units, including gems and jewellery units, may on the basis of annual permission from Customs authorities, sub - contract production processes to DTA through job work which may also involve change of form or nature of goods, through job work by units in DTA.

(ii) These units may sub - contract upto 50% of overall production of previous year in value terms in DTA with permission of Customs authorities.

(b) (i) EOU may, with annual permission from Customs authorities, undertake job work for export, on behalf of DTA exporter, provided that goods are exported directly from EOU and export document shall jointly be in name of DTA / EOU. For such exports, DTA units will be entitled for refund of duty paid on inputs by way of brand rate of duty drawback.

(ii) Duty free import of goods for execution of export order placed on EOU by foreign supplier on job work basis, would be allowed subject to condition that no DTA clearance shall be allowed.

(iii) Sub - contracting of both production and production processes may also be undertaken without any limit through other EOU / EHTP / STP/ BTP / SEZ units, on the basis of records maintained in unit.

(iv) EOU / EHTP / STP / BTP units may sub - contract part of production process abroad and send intermediate products abroad as mentioned in LoP. No permission would be required when goods are sought to be exported from sub - contractor premises abroad. When goods are sought to be brought back, prior intimation to concerned DC and Customs authorities shall be given.

(c) Scrap / waste / remnants generated through job work may either be cleared from job worker's premises on payment of applicable duty on transaction value or destroyed in presence of Customs / Central Excise authorities or returned to unit. Destruction shall not apply to gold, silver, platinum, diamond, precious and semi-precious stones.

(d) Sub - contracting / exchange by gems and jewellery EOUs through other EOUs or SEZ units or units in DTA, shall be as per procedure indicated in HBP.

Sale of Unutilized Material

(a) In case an EOU / EHTP / STP / BTP unit is unable to utilize goods and services, imported or procured from DTA, it may be:

(i) Transferred to another EOU / EHTP / STP / BTP / SEZ unit; or

(ii) Disposed of in DTA with approval of Customs authorities on payment of applicable duties and submission of import authorization; or

(iii) Exported.

Such transfer from EOU / EHTP / STP / BTP unit to another such unit would be treated as import for receiving unit.

(b) Capital goods and spares that have become obsolete / surplus, may either be exported, transferred to another EOU / EHTP / STP / BTP / SEZ unit or disposed of in DTA on payment of applicable duties. Benefit of depreciation, as applicable, will be available in case of disposal in DTA only when the unit has achieved positive NFE taking into consideration the depreciation allowed. No duty shall be payable in case capital goods, raw material, consumables, spares, goods manufactured, processed or packaged, and scrap / waste / remnants / rejects are destroyed within unit after intimation to Customs authorities or destroyed outside unit with permission of Customs authorities.

Destruction as stated above shall not apply to gold, silver, platinum, diamond, precious and semi-precious stones.

(c) In case of textile sector, disposal of left over material / fabrics upto 2% of CIF value or quantity of import, whichever is lower, on payment of duty on transaction value, may be allowed, subject to certification of Central Excise / Customs officers that these are leftover items.

(d) Disposal of used packing material will be allowed on payment of duty on transaction value.

Reconditioning / Repair and Re - engineering

(a) EOUs shall be set up with approval of UAC to carry out reconditioning, repair, remaking, testing, calibration, quality improvement, upgradation of technology and re-engineering activities for export in foreign currency.

(b) EHTP/STP/BTP units shall be set up with approval of IMSC to carry out reconditioning, repair, remaking, testing, calibration, quality improvement, upgradation of technology and re-engineering activities for export in foreign currency.

Replacement / Repair of Imported / Indigenous Goods

(a) General provisions of FTP relating to export / import of replacement / repair of goods would also apply equally to EOU / EHTP / STP / BTP units. Cases not covered by these provisions shall be considered on merits by DC.

(b) Goods sold in DTA and not accepted for any reasons, may be brought back for repair / replacement, under intimation to concerned jurisdictional Customs / Central Excise authorities.

(c) Goods or parts thereof, on being imported / indigenously procured and found defective or otherwise unfit for use or which have been damaged or become defective subsequently, may be returned and replacement obtained or destroyed. In the event of replacement, goods may be brought back from foreign suppliers or their authorized agents in India or indigenous suppliers. The unit can take free of cost replacement (duty paid) from the authorized agents in India of foreign suppliers, provided the defective part is re - exported or destroyed. However, destruction shall not apply to precious and semi-precious stones and precious metals.

Exit from EOU Scheme

(a) With approval of DC, an EOU may opt out of scheme. Such exit shall be subject to payment of Excise and Customs duties and industrial policy in force.

(b) If unit has not achieved obligations, it shall also be liable to penalty at the time of exit.

(c) In the event of a gems and jewellery unit ceasing its operation, gold and other precious metals, alloys, gems and other materials available for manufacture of jewellery, shall be handed over to an agency nominated by DoC, at price to be determined by that agency.

(d) An EOU / EHTP / STP / BTP unit may also be permitted by DC to exit from the scheme at any time on payment of duty on capital goods under the prevailing EPCG Scheme for DTA Units. This will be subject to fulfilment of positive NFE criteria under EOU scheme, eligibility criteria under EPCG scheme and standard conditions indicated in HBP.

(e) Unit proposing to exit out of EOU scheme shall intimate DC and Customs and Central Excise authorities in writing. Unit shall assess duty liability arising out of de-bonding and submit details of such assessment to Customs and Central Excise authorities. Customs and Central Excise authorities shall confirm duty liabilities on priority basis, subject to the condition that the unit has achieved positive NFE, taking into consideration the depreciation allowed. After payment of duty and clearance of all dues, unit shall obtain "No Dues Certificate" from Customs and Central Excise authorities. On the basis of "No Dues Certificate" so issued by the Customs and Central Excise authorities, unit shall apply to DC for final de-bonding. In case there is no proceeding pending under FT(D&R) Act, as amended, DC shall issue final de-bonding order within a period of 7 working days. Between "No Dues Certificate" issued by Customs and Central Excise authorities and final de-bonding order by DC, unit shall not be entitled to claim any exemption for procurement of capital goods or inputs. However, unit can claim Advance Authorisation / DFIA / Duty Drawback. Since the duty calculations and dues are disputed and take a long time, a BG / Bond / Instalment processes backed by BG shall be provided for expediting the exit process.

(f) In cases where a unit is initially established as DTA unit with machines procured from abroad after payment of applicable import duty, or from domestic market after payment of excise duty, and unit is subsequently converted to EOU, in such cases removal of such capital goods to DTA after de-bonding would be without payment of duty. Similarly, in cases where a DTA unit imported capital goods under EPCG Scheme and after completely fulfilling export obligation gets converted into EOU, unit would not be charged customs duty on capital goods at the time of removal of such capital goods in DTA when de-bonding.

(g) An EOU / EHTP / STP / BTP unit may also be permitted by DC to exit under Advance Authorization as one time option. This will be subject to fulfilment of positive NFE criteria.

(h) A simplified procedure may be provided to fast track the De-bonding/ Exit of the STP / EHTP Unit which has not availed any duty benefit on procurement of raw material, capital goods etc.

Conversion

(a) Existing DTA units may also apply for conversion into an EOU / EHTP / STP / BTP unit.

(b) Existing EHTP / STP units may also apply for conversion / merger to EOU unit and vice-versa. In such cases, units will remain in bond and avail exemptions in duties and taxes as applicable.

Monitoring of NFE

Performance of EOU / EHTP / STP / BTP units shall be monitored by Units Approval Committee as per guidelines in HBP.

Export through Exhibitions / Export Promotion Tours / Showrooms Abroad / Duty Free Shops

EOU / EHTP / STP / BTP are permitted to:

(i) Export goods for holding / participating in Exhibitions abroad with permission of DC.

(ii) Personal carriage of gold / silver / platinum jewellery, precious, semi-precious stones, beads and articles.

(iii) Export goods for display / sale in permitted shops set up abroad.

(iv) Display / sell in permitted shops set up abroad, or in showrooms of their distributors / agents.

(v) Set up showrooms / retail outlets at International Airports.

Personal Carriage of Import / Export Parcels including through Foreign Bound Passengers

Import / export through personal carriage of gems and jewellery items may be undertaken as per Customs procedure. However, export proceeds shall be realized through normal banking channel. Import / export through personal carriage by units, other than gems and jewellery units, shall be allowed provided goods are not in commercial quantity. An authorized person of Gems & Jewellery EOU may also import gold in primary form, upto 10 Kgs in a financial year through personal carriage, as per guidelines prescribed by RBI and DoR.

Export / Import by Post / Courier

Goods including free samples, may be exported / imported by airfreight or through foreign post office or through courier, as per Customs procedure.

Administration of EOUs / Powers of DC

Details of administration of EOUs and power of DC is given in HBP.

6.25 Revival of Sick Units

Subject to a unit being declared sick by appropriate authority, proposals for revival of the unit or its take over may be considered by BOA.

Approval of EHTP / STP

In case of units under EHTP / STP schemes, necessary approval / permission under relevant paras of this Chapter shall be granted by officer designated by Ministry of Communication and Information Technology, Department of Electronics & Information Technology, instead of DC, and by Inter-Ministerial Standing Committee (IMSC) instead of BOA.

Approval of BTP

Bio-Technology Parks (BTP) would be notified by DGFT on recommendations of Department of Biotechnology. In case of units in BTP, necessary approval / permission under relevant provisions of this chapter will be granted by designated officer of Department of Biotechnology.

Warehousing Facilities

An EOU which intends to set up warehousing facilities outside the EOU premises and outside the jurisdiction of DC, at a place near to the port of export, to reduce lead time for delivery of goods overseas and to address unpredictability of supply orders, is permitted to do so subject to the provisions related to export warehousing as per terms and conditions of Notifications issued by the Department of Revenue.

5.7 DEEMED EXPORTS

Objective

To provide a level-playing field to domestic manufacturers in certain specified cases, as may be decided by the Government from time to time.

Deemed Exports

"Deemed Exports" refer to those transactions in which goods supplied do not leave country, and payment for such supplies is received either in Indian rupees or in free foreign exchange. Supply of goods as specified in Paragraph below shall be regarded as "Deemed Exports" provided goods are manufactured in India.

Categories of Supply

Supply of goods under following categories (a) to (d) by a manufacturer and under categories (e) to (h) by main / subcontractors shall be regarded as "Deemed Exports":

A. Supply by manufacturer:

(a) Supply of goods against Advance Authorisation / Advance Authorisation for annual requirement / DFIA;

(b) Supply of goods to EOU / STP / EHTP / BTP;

(c) Supply of capital goods against EPCG Authorisation;

(d) Supply of marine freight containers by 100% EOU (Domestic freight containers-manufacturers) provided said containers are exported out of India within 6 months or such further period as permitted by customs;

B. Supply by main / sub-contractor (s):

(e) (i) Supply of goods to projects financed by multilateral or bilateral Agencies / Funds as notified by Department of Economic Affairs (DEA), MoF, where legal agreements provide for tender evaluation without including customs duty.

(ii) Supply and installation of goods and equipment (single responsibility of turnkey contracts) to projects financed by multilateral or bilateral Agencies/Funds as notified by Department of Economic Affairs (DEA), MoF, for which bids have been invited and evaluated on the basis of Delivered Duty Paid (DDP) prices for goods manufactured abroad.

(iii) Supplies covered in this paragraph shall be under International Competitive Bidding (ICB) in accordance with procedures of those Agencies / Funds.

(iv) A list of agencies, covered under this paragraph, for deemed export benefits, is given in Appendix 7A of AANF.

(f) (i) Supply of goods to any project or for any purpose in respect of which the Ministry of Finance, by Notification No. 12/2012 –Customs dated 17.3.2012, as amended from time to time, permits import of such goods at zero customs duty subject to conditions specified in the above said Notification. Benefits of deemed exports shall be available only if the supply is made under procedure of ICB.

(ii) Supply of goods required for setting up of any mega power project, as specified in the list 32A, at Sl. No. 507 of Department of Revenue Notification No. 12/2012- Customs dated 17.03.2012, as amended from time to time, shall be eligible for deemed export benefits provided such mega power project conforms to the threshold generation capacity specified in the above said Notification.

(iii) For mega power projects, ICB condition would not be mandatory if the requisite quantum of power has been tied up through tariff based competitive bidding or if the project has been awarded through tariff based competitive bidding.

(g) Supply of goods to United Nations or International Organisations for their official use or supplied to the projects financed by the said United Nations or an International organisation approved by Government of India. List of such organisation and conditions applicable to such supplies is given in the Excise Notification No 108/95-CE, dated 28.08.1995, as amended from time to time. A list of Agencies, covered under this paragraph, is given in Appendix-7B of AANF.

(h) Supply of goods to nuclear power projects provided:

(i) Such goods are required for setting up of any Nuclear Power Project as specified in the list 33 at Sl. No. 511 of Notification No. 12/2012 – Customs dated 17.3.2012, as amended from time to time.

(ii) The project should have a capacity of 440 MW or more.

(iii) A certificate to the effect is required to be issued by an officer not below the rank of Joint Secretary to Government of India, in Department of Atomic Energy.

(iv) Tender is invited through National competitive bidding (NCB) or through ICB.

Benefits for Deemed Exports

Deemed exports shall be eligible for any / all of following benefits in respect of manufacture and supply of goods, qualifying as deemed exports, subject to terms and conditions as given in HBP and ANF-7A:

(a) Advance Authorisation / Advance Authorisation for annual requirement / DFIA.

(b) Deemed Export Drawback.

(c) Refund of terminal excise duty, if exemption is not available.

Benefits to the Supplier /Recipient

Categories of supplies	Benefits on supplies, whichever is applicable.		
	Advance Authorisation	Duty Drawback	Terminal Excise Duty
(a)	Yes (for intermediate supplies against an invalidation letter)	Yes (against ARO or Back to Back letter of credit)	(i) Exemption, in case of Invalidation Letter (ii) Refund, in case of ARO or back to back letter of credit (iii) No exemption/refund against supply to DFIA as CVD is not exempted
(b)	Yes	Yes	Exemption
(c)	Yes	Yes	Refund
(d)	No	Yes	Refund
(e)	Yes	Yes	Exemption
(f)	Yes	Yes	Exemption, if supplies under ICB. Refund, if supplies under tariff based competitive bidding.
(g)	Yes	Yes	Exemption
(h)	Yes	Yes	Refund

Conditions for refund of terminal excise duty

(i) Supply of goods will be eligible for refund of terminal excise duty as per point (c) of para, "Benefits for Deemed exports" of FTP, provided recipient of goods does not avail CENVAT credit/rebate on such goods.

(ii) However, supply of goods which are exempted ab-initio from payment of Terminal Excise Duty would be ineligible to get refund of TED. Exemption from TED is available to the following:

  (a) Supplies under ICB;

  (b) Supplies of intermediate goods, against invalidation letter, made by an Advance Authorisation holder to another Advance Authorisation holder;

  (c) Goods Procured by EOU / EHTP / STP / BTP unit from a unit in DTA; and

  (d) Supply of goods to UN/International Organisation or project funded by it.

Conditions for refund of deemed export drawback

Supplies will be eligible for deemed export drawback as per para 7.03 (b) of FTP, as under:

(a) In case CENVAT credit / rebate has not been availed on the inputs / input services, by the supplier of goods, then, benefit as per Column 'A' of All Industry Rate of Duty Drawback Schedule shall be admissible.

(b) If CENVAT credit / rebate has been availed by the supplier of goods, on inputs / input services, then, no Drawback shall be admissible as per Column 'B' of All Industry Rate of Duty Drawback Schedule. However, in such cases, Basic Customs Duty paid can be claimed as Brand Rate of Duty Drawback based upon submission of documents evidencing actual payment of duties.

Common conditions for deemed export benefits

(i) Supplies shall be made directly to entities listed in the Para heading "Categories of Supply". Third party supply shall not be eligible for benefits/exemption.

(ii) In all cases, supplies shall be made directly to the designated Projects/Agencies/Units/ Advance Authorisation/ EPCG Authorisation holder. Subcontractors may, however, make supplies to main contractor instead of supplying directly to designated Projects/ Agencies. Payments in such cases shall be made to sub-contractor by main-contractor and not by project Authority.

(iii) Supply of domestically manufactured goods by an Indian Sub-contractor to any Indian or foreign main contractor, directly at the designated project's/ Agency's site, shall also be eligible for deemed export benefit provided name of sub-contractor is indicated either originally or subsequently (but before the date of supply of such goods) in the main contract. In such cases payment shall be made directly to sub-contractor by the Project Authority.

Benefits on specified supplies

(i) Deemed export benefits shall be available for supplies of 'Cement" only.

(ii) Deemed export benefit shall be available on supply of "Steel":

(a) As an inputs to Advance Authorization/ Annual Advance Authorization/DFIA holder/ an EOU.

(b) To multilateral/ bilateral funded Agencies.

(iii) Deemed export benefit shall be available on supply of "Fuel" provided supplies are made to:

(a) Project listed for petroleum operations in the Customs Notification No. 12/2012–Cus. dated 17.03.2012 under Sr. No. 356, 358 to 360 and covered in Para 7.02 (f) of FTP;

(b) EOUs;

(c) Advance Authorization holder / Annual Advance Authorization holder.

Liability of Interest

Incomplete/deficient application is liable to be rejected. However, simple interest @ 6% per annum will be payable on delay in refund of duty drawback and terminal excise duty under the scheme, provided the claim is not settled within 30 days from the date of issue of final Approval Letter by RA.

Risk Management and Internal Audit mechanism

(a) A Risk Management system shall be in operation, wherein every month, Computer system in DGFT headquarters, on random basis, will select 10% of cases, for each RA, where benefit(s) under this chapter has/have already been granted. Such cases shall be scrutinized by an internal Audit team, headed by a Joint DGFT, in the office of respective Zonal Addl. DGFT. The team will be responsible to audit claims of not only for its own office but also the claims of all RAs falling under the jurisdiction of the Zone.

(b) The respective RA may also, either on the basis of report from Internal Audit/ External Audit Agency(ies) or suo-motu, reassess any case, where any erroneous/in-eligible payment has been made/claimed. RA will take necessary action for recovery of payment along with interest at the rate of 15% per annum on the recoverable amount.

Penal Action

In case, claim is filed by submitting mis-declaration/misrepresentation of facts, then in addition to effecting recovery under Para above, the applicant shall be liable for penal action under the provisions of F.T. (D&R) Act, Rules and orders made thereunder.

5.8 QUALITY COMPLAINTS AND TRADE DISPUTES

Objective

Exporters need to project a good image of the country abroad to promote exports. Maintaining an enduring relationship with foreign buyers is of utmost importance, and complaints or trade disputes, whenever they arise, need to be settled amicably as soon as possible. Importers too may have grievances as well.

In an endeavour to resolve such complaints or trade disputes and to create confidence in the business environment of the country, a mechanism is being laid down to address such complaints and disputes in an amicable way.

Quality Complaints/ Trade disputes

The following type of complaints may be considered:

(a) Complaints received from foreign buyers in respect of poor quality of the products supplied by exporters from India;

(b) Complaints of importers against foreign suppliers in respect of quality of the products supplied; and

(c) Complaints of unethical commercial dealings categorized mainly as non-supply/ partial supply of goods after confirmation of order; supplying goods other than the ones as agreed upon; non-payment; non-adherence to delivery schedules, etc.

Obligation on the part of importer/ exporter

(a) Rule 11 of the Foreign Trade (Regulation) Rules, 1993, requires that on the importation into, or exportation out of, any customs ports of any goods, whether liable to duty or not, the owner of such goods shall in the Bill of Entry or the Shipping Bill or any other documents prescribed under the Customs Act, 1962 (52 of 1962), state the value, quality and description of such goods to the best of his knowledge and belief and in case of exportation of goods, certify that the quality and specification of the goods as stated in those documents, are in accordance with the terms of the export contract entered into with the buyer or consignee in pursuance of which the goods are being exported and shall subscribe a declaration of the truth of such statement at the foot of such Bill of Entry or Shipping Bill or any other documents. Violation of this provision renders the exporter liable for penal action.

(b) Certain export commodities have been notified for Compulsory Quality Control & Pre-shipment Inspection prior to their export. Penal action can be taken under the Export (Quality Control & Inspection) Act, 1963 as amended in 1984, against exporters who do not conform to these standards and/ or provisions of the Act as laid down for such products.

Provisions in FT (D&R) Act & FT (Regulation) Rules for necessary action against erring exporters/ importers

Action against erring exporters can be taken under the Foreign Trade (Development and Regulation) Act, 1992, as amended and under Foreign Trade (Regulation) Rules, 1993, as follows:-

(a) Section 8 of the Act empowers the Director General of Foreign Trade or any other person authorized by him to suspend or cancel the Importer Exporter Code Number for the reasons as given therein.

(b) Section 9 (2) of the Act empowers the Director General of Foreign Trade or an officer authorised by him to refuse to grant or renew a license, certificate, scrip or any other instrument bestowing financial or fiscal benefit granted under the Act.

(c) Section 9(4) empowers the Director General of Foreign Trade or the officer authorized by him to suspend or cancel any License, certificate, scrip or any instrument bestowing financial or fiscal benefit granted under the Act.

(d) Section 11(2) of the Act provides for imposition of fiscal penalty in cases where a person makes or abets or attempts to make any import or export in contravention of any provision of the Act, any Rules or Orders made there under or the Foreign Trade Policy.

Mechanism for handling of Complaints/ Disputes

(a) **Committee on Quality complaints and Trade Disputes (CQCTD)**

To deal effectively with the increasing number of complaints and disputes, a 'Committee on Quality Complaints and Trade Disputes' (CQCTD) will be constituted in the 22 offices of the RA's of DGFT. Names of RAs, where CQCTD has been constituted and jurisdiction of CQCTD is given in Chapter 8 of the Handbook of Procedures.

(b) **Composition of the CQCTD**

The CQCTD would be constituted under the Chairpersonship of the Head of Office. The constitution of CQCTD is given in Chapter 8 of the Hand Book of Procedures.

(c) **Functions of CQCTD**

The Committee (CQCTD) will be responsible for enquiring and investigating into all Quality related complaints and other trade related complaints falling under the jurisdiction of the respective RAs. It will take prompt and effective steps to redress and resolve the grievances of the importers, exporters and overseas buyers, preferably within three months of receipt of the complaint. Wherever required, the Committee (CQCTD) may take the assistance of the Export Promotion Councils/FIEO/Commodity Boards or any other agency as considered appropriate for settlement of these disputes.

Proceedings under CQCTD

CQCTD proceedings are only reconciliatory in nature and the aggrieved party, whether the foreign buyer or the Indian importer, is free to pursue any legal recourse against the other erring party.

Procedures to deal with complaints and trade disputes

The procedure for making an application for such complaints or trade disputes and the procedure to deal with such quality complaints and disputes is given in the Handbook of Procedures.

Corrective Measures

The Committee at RA level can authorize the Export Inspection Agency or any technical authority to assess whether there has been any technical failure of not meeting the standards, manufacturing/ design defects, etc. for which complaints have been received.

Nodal Officer

Director General of Foreign Trade would appoint an officer, not below the rank of Joint Director General, in the Headquarters, to function as the 'Nodal Officer' for coordinating with various Regional Authorities of DGFT.

5.9 DEFINITIONS

1. For purpose of FTP, unless context otherwise requires, the following words and expressions shall have the following meanings attached to them:-

2. "Accessory" or "Attachment" means a part, sub-assembly or assembly that contributes to efficiency or effectiveness of a piece of equipment without changing its basic functions.

3. "Act" means Foreign Trade (Development and Regulation) Act, 1992 (No.22 of 1992) [FT (D&R) Act] as amended from time to time.

4. "Actual User" is a person (either natural or legal) who is authorized to use imported goods in his/its own premise which has a definitive postal address.

   (a) "Actual User (Industrial)" is a person (either natural & legal) who utilizes imported goods for manufacturing in his own industrial unit or manufacturing for his own use in another unit including a jobbing unit which has a definitive postal address.

   (b) "Actual User (Non-Industrial)" is a person (either natural & legal) who utilizes the imported goods for his own use in:

      (i) any commercial establishment, carrying on any business, trade or profession, which has a definitive postal address; or

      (ii) any laboratory, Scientific or Research and Development (R&D) institution, university or other educational institution or hospital which has a definitive postal address; or

      (iii) any service industry which has a definitive postal address.

5. "AEZ" means Agricultural Export Zones notified by DGFT in Appendix 2V of Appendices and Aayat Niryat Forms.

6. "Appeal" is an application filed under section 15 of the Act and includes such applications preferred by DGFT officials in government interest against decision by designated adjudicating/appellate authorities.

7. "Applicant" means person on whose behalf an application is made and shall, wherever context so requires, includes person signing the application.

8. "Authorization" means permission as included in Section 2 (g) of the Act to import or export as per provisions of FTP.

9. "Capital Goods" means any plant, machinery, equipment or accessories required for manufacture or production, either directly or indirectly, of goods or for rendering services, including those required for replacement, modernisation, technological up-gradation or expansion. It includes packaging machinery and equipment, refrigeration equipment, power generating sets, machine tools, equipment and instruments for testing, research and development, quality and pollution control.

   Capital goods may be for use in manufacturing, mining, agriculture, aquaculture, animal husbandry, floriculture, horticulture, pisciculture, poultry, sericulture and viticulture as well as for use in services sector.

10. "Competent Authority" means an authority competent to exercise any power or to discharge any duty or function under the Act or the Rules and Orders made there under or under FTP.

11. "Component" means one of the parts of a sub-assembly or assembly of which a manufactured product is made up and into which it may be resolved. A component includes an accessory or attachment to another component.

12. "Consumables" means any item, which participates in or is required for a manufacturing process, but does not necessarily form part of end-product. Items, which are substantially or totally consumed during a manufacturing process, will be deemed to be consumables.

13. "Consumer Goods" means any consumption goods, which can directly satisfy human needs without further processing and includes consumer durables and accessories thereof.

14. "Counter Trade" means any arrangement under which exports/imports from /to India are balanced either by direct imports/exports from importing/exporting country or through a third country under a Trade Agreement or otherwise.

    Exports/ Imports under Counter Trade may be carried out through Escrow Account, Buy Back arrangements, Barter trade or any similar arrangement. Balancing of exports and imports could wholly or partly be in cash, goods and/or services.

15. "Developer" means a person or body of persons, company, firm and such other private or government undertaking, who develops, builds, designs, organises, promotes, finances, operates, maintains or manages a part or whole of infrastructure and other facilities in SEZ as approved by Central Government and also includes a co- developer.

16. "Development Commissioner" means Development Commissioner of SEZ

17. "Domestic Tariff Area (DTA)" means area within India which is outside SEZs and EOU/ EHTP/ STP/ BTP.

18. "Drawback on deemed export" in relation to any goods manufactured in India and supplied as deemed exports, means the rebate of duty or tax, as the case may be, chargeable on any imported materials or excisable materials used or taxable services used as input services in the manufacture of such goods.

19. "EOU" means Export Oriented Unit for which a letter of permit has been issued by Development Commissioner.

20. "Excisable goods" means any goods produced or manufactured in India and subject to duty of excise under Central Excise and Salt Act 1944 (1 of 1944).

21. "Export" is as defined in FT (D&R) Act, 1992, as amended from time to time.

22. "Exporter" means a person who exports or intends to export and holds an IEC number, unless otherwise specifically exempted.

23. "Export Obligation" means obligation to export product or products covered by Authorisation or permission in terms of quantity, value or both, as may be prescribed or specified by Regional or competent authority.

24. "Free" as appearing in context of import/export policy for items means goods which do not need any 'Authorisation'/ License or permission for being imported into the country or exported out.

25. "FTP" means the Foreign Trade Policy which specifies policy for exports and imports under Section 5 of the Act.

26. "Import" is as defined in FT (D&R) Act, 1992 as amended from time to time.

27. "Importer" means a person who imports or intends to import and holds an IEC number, unless otherwise specifically exempted.

28. ITC (HS) refers to Indian Trade Classification (Harmonized System) at 8 digits.

29. "Jobbing" means processing or working upon of raw materials or semi-finished goods supplied to job worker, so as to complete a part of process resulting in manufacture or finishing of an article or any operation which is essential for aforesaid process.

30. “Licensing Year” means period beginning on the st st 1 April of a year and ending on the 31 March of the following year.

31. “Managed Hotel” means hotels managed by a three star or above hotel/ hotel chain under an operating management contract for a duration of at least three years between operating hotel/ hotel chain and hotel being managed. Management contract must necessarily cover the entire gamut of operations/ management of managed hotel.

32. “Manufacture” means to make, produce, fabricate, assemble, process or bring into existence, by hand or by machine, a new product having a distinctive name, character or use and shall include processes such as refrigeration, re-packing, polishing, labeling, Re-conditioning repair, remaking, refurbishing, testing, calibration, re-engineering.

    Manufacture, for the purpose of FTP, shall also include agriculture, aquaculture, animal husbandry, floriculture, horticulture, pisciculture, poultry, sericulture, viticulture and mining.

33. “Manufacturer Exporter” means a person who exports goods manufactured by him or intends to export such goods.

34. “Merchant Exporter” means a person engaged in trading activity and exporting or intending to export goods.

35. “NC” means the Norms Committee in the Directorate General of Foreign Trade for approval of adhoc input –output norms in cases where SION does not exist and recommend SION to be notified in DGFT.

36. “Notification” means a notification published in Official Gazette.

37. “Order” means an Order made by Central Government under the Act.

38. “Part” means an element of a sub-assembly or assembly not normally useful by itself, and not amenable to further disassembly for maintenance purposes. A part may be a component, spare or an accessory.

39. “Person” means both natural and legal and includes an individual, firm, society, company, corporation or any other legal person including the DGFT officials.

40. “Policy” means Foreign Trade Policy (2015-2020) as amended from time to time.

41. “Prescribed” means prescribed under the Act or the Rules or Orders made there under or under FTP.

42. “Prohibited” indicates the import/export policy of an item, as appearing in ITC (HS) or elsewhere, whose import or export is not permitted.

43. “Public Notice” means a notice published under provisions of paragraph 2.04 of FTP.

44. “Quota” means the quantity of goods of a specific kind that is permitted to be imported without restriction or imposition of additional Duties.

45. “Raw material” means input(s) needed for manufacturing of goods. These inputs may either be in a raw/natural/ unrefined/ unmanufactured or manufactured state.

46. “Regional Authority” means authority competent to grant an Authorisation under the Act / Order.

47. “Registration-Cum-Membership Certificate” (RCMC) means certificate of registration and membership granted by an Export Promotion Council / Commodity Board / Development Authority or other competent authority as prescribed in FTP or Handbook of Procedures.

48. "Restricted" is a term indicating the import or export policy of an item, which can be imported into the country or exported outside, only after obtaining an authorization from the offices of DGFT.

49. "Rules" means Rules made by Central Government under Section 19 of the FT (D&R)Act.

50. "SCOMET" is the nomenclature for dual use items of Special Chemicals, Organisms, Materials, Equipment and Technologies (SCOMET). Export of dual-use items and technologies under India's Foreign Trade Policy is regulated. It is either prohibited or is permitted under an authorization.

51. "Services" include all tradable services covered under General Agreement on Trade in Services (GATS) and earning free foreign exchange.

52. "Service Provider" means a person providing:

    (i) Supply of a 'service' from India to any other country; (Mode1- Cross border trade)

    (ii) Supply of a 'service' from India to service consumer(s) of any other country; (Mode 2- Consumption abroad)

    (iii) Supply of a 'service' from India through commercial presence in any other country. (Mode 3 – Commercial Presence.)

    (iv) Supply of a 'service' from India through the presence of natural persons in any other country (Mode 4- Presence of natural persons.)

53. "Ships" mean all types of vessels used for sea borne trade or coastal trade, and shall include second hand vessels.

54. "SION" means Standard Input Output Norms notified by DGFT.

55. "Spares" means a part or a sub-assembly or assembly for substitution that is ready to replace an identical or similar part or sub- assembly or assembly. Spares include a component or an accessory.

56. "Specified" means specified by or under the provisions of this Policy through Notification / Public Notice.

57. "Status holder" means an exporter recognized as One Star Export House/ Two Star Export House / Three Star Export House / Four Star Export House/ Five Star Export House by DGFT/ Development Commissioner.

58. "Stores" means goods for use in a vessel or aircraft and includes fuel and spares and other articles of equipment, whether or not for immediate fitting.

59. (a) "Supporting Manufacturer" is one who manufactures goods/products or any part/ accessories/components of a good/product for a merchant exporter or a manufacturer exporter under a specific authorization.

    (b) "Supporting Manufacturer" for the EPCG Scheme shall be one in whose premises/factory Capital Goods imported/ procured under EPCG authorization is installed.

60. State Trading Enterprises (STEs), for the purpose of this FTP, are those entities which are granted exclusive right / privileges export and / or import as per para 2.20 (a) of FTP.

61. "Third-party exports" means exports made by an exporter or manufacturer on behalf of another exporter(s).

    In such cases, export documents such as shipping bills shall indicate name of both manufacturing exporter /manufacturer and third party exporter(s). Bank Realisation Certificate, Self Declaration Form (SDF), export order and invoice should be in the name of third party exporter.

62. "Transaction Value" is as defined in Customs Valuation Rules of Department of Revenue.

63. "Wild Animal" means any wild animal as defined in Section 2(36) of Wildlife (Protection) Act, 1972.

The following annexures and appendices are required to be certified by the Cost Accountants:

Appendix -5B	Certificate of Chartered Accountant/ Cost Accountant/ Company Secretary (For Issue of EPCG Authorisation)
Appendix- 5C	Certificate of Chartered Accountant/ Cost Accountant/ Company Secretary (For Redemption of EPCG Authorization / Issuance of Post Export EPCG Duty Credit Scrip)
Annexure to Appendix 2 L	Certificate for Offsetting of Export Proceeds
Appendix -4H	Register for Accounting the Consumption and Stocks of Duty Free Imported or Domestically Procured Raw Materials, Components etc. Allowed Under Advance Authorisation / DFIA
Appendix -3B	List of products and list of markets eligible under Merchandise Exports from India Scheme (MEIS)
Appendix- 3C	List of eligible category under MEIS if exported through using E-commerce platform
Appendix- 3D	List of Services eligible under Service Exports from India Scheme (SEIS)
Appendix -3E	List of services where payment has been received in Indian rupees which can be treated as receipt in Deemed Foreign Exchange as per guidelines of Reserve Bank of India

GLOSSARY (ACRONYMS)

Acronym	Explanation
AA	Advance Authorisation
AANF	Appendices and Aayaat Niryaat Form
ACU	Asian Clearing Union
AEZ	Agri Export Zone
ANF	Aayat Niryaat Form
ARE-1	Application for Removal of Excisable Goods for Export (By Air/Sea/Post/Land)
ARE-3	Application for Removal of Excisable Goods from a factory or a warehouse to another warehouse
ACP	Accredited Clients Programme
AEO	Authorised Economic Operator
AES	Approved Exporter's Scheme
APEDA	Agricultural & Processed Food Products Export Development Authority
ARO	Advance Release Order
ASEAN	Association of South- East Asian Nations
ASIDE	Assistance to States for Infrastructure Development of Exports
AU	Actual User
BCD	Basic Customs Duty
BG	Bank Guarantee
BIFR	Board of Industrial and Financial Reconstruction
BOA	Board of Approval
BOT	Board of Trade
BRC	Bank Realisation Certificate
BTP	Biotechnology Park
BIS	Bureau of Indian Standards
CBEC	Central Board of Excise and Customs
CCP	Customs Clearance Permit
CEA	Central Excise Authority
CEC	Chartered Engineer Certificate
CED	Central Excise Duty
CENVAT	Central Value Added Tax
CETF	Common Effluent Treatment Facility
CFCs	Common Facility Centres
CG	Capital Goods
CIF	Cost, Insurance & Freight
CIN	Corporate Identification Number
CIS	Commonwealth of Independent States
CKD	Completely Knocked Down
CoD	Cash on Delivery
CoO	Certificate of Origin
CQCTD	Committee on Quality Complaints and Trade Disputes
CRES	Certificate of Registration as Exporter of Spices

CST	Central Sales Tax
CIN	Company Identification Number
CRES	Certification of Registration as Exporter of Spices
CEPA	Comprehensive Economic Partnership Agreement
CBEC	Central Board of Excise and Customs
CSP	Common Service Provider
CECA	Comprehensive Economic Cooperation Agreement
CVD	Countervailing Duty
DA	Document against Acceptance
DBK	Drawback
DC	Development Commissioner
DDA	Diamond Dollar Accounts
DEA	Department of Economic Affairs
DEL	Denied Entity List
DES	Duty Exemption Schemes
DFIA	Duty Free Import Authorisation
DGCI&S	Director General, Commercial Intelligence & Statistics.
DIN	Director Identification Number
DPIN	Designated Partner Identification Number
DGFT	Director General of Foreign Trade
DIPP	Department of Industrial Policy & Promotion
DoBT	Department of Bio-Technology
DoC	Department of Commerce
DeitY	Department of Electronics and Information Technology
DoR	Department of Revenue
DoT	Department of Telecommunications
DRS	Duty Remission Schemes
DTA	Domestic Tariff Area
e-BRC	Electronic Bank Realisation Certificate
e-IEC	Electronic Importer-Exporter Code
ECA	Enforcement- cum-Adjudication
EDI	Electronic Data Interchange
ECGC	Export Credit Guarantee Corporation
EEFC	Exchange Earners' Foreign Currency
EFC	Exim Facilitation Committee
EFT	Electronic Fund Transfer
EGM	Export General Manifest
EHTP	Electronic Hardware Technology Park
EIC	Export Inspection Council
EO	Export Obligation
EODC	Export Obligation Discharge Certificate
EOP	Export Obligation Period
EOU	Export Oriented Unit
EPC	Export Promotion Council
EPCG	Export Promotion Capital Goods
EPO	Engineering Process Outsourcing
EXIM	Export Import

FDI	Foreign Direct Investment
FE	Foreign Exchange
FEMA	Foreign Exchange Management Act
FIEO	Federation of Indian Export Organisation
FIRC	Foreign Exchange Inward Remittance Certificate
FOB	Free On Board
FOR	Freight on Road and Rails
FT (D&R)Act	Foreign Trade (Development & Regulation) Act, 1992 (22 of 1992)
FTDO	Foreign Trade Development Officer
FTP	Foreign Trade Policy
FT(R) Rules	Foreign Trade (Regulation) Rules
FTWZ	Free Trade and Warehousing Zone
FTA	Free Trade Agreement
G&J EPC	Gems & Jewellery Export Promotion Council
GOI	Government of India
GATS	General Agreement on Trade in Services
GR	Guarantee of Realisation
HACCP	Hazard Analysis and Critical Control Process
HBP	Handbook of Procedures
HHEC	Handicraft & Handlooms Exports Corporation
ICB	International Competitive Bidding
ICD	Inland Container Depot
ICM	Indian Commercial Mission
IEC	Importer Exporter Code
ISO	International Organisation for Standardisation
IAEA	International Atomic Energy Agency
INFCIRC	International Atomic Energy Agency Information Circular
IEM	Industrial Entrepreneurial Memorandum
IMSC	Inter-Ministerial Standing Committee
IL	Industrial Licensing
ISO	International Standards Organisation
ITC (HS)	Indian Trade Classification (Harmonised System) for Export & Import Items
KVIC	Khadi and Village Industries Commission
LC	Letter of Credit
LCS	Land Customs Station
LLPIN	Limited Liability Partnership Number
LPG	Liquefied Petroleum Gas
LoC	Line of Credit
LoI	Letter of Intent
LoP	Letter of Permit
LUT	Legal Undertaking
MAI	Market Access Initiative
MDA	Market Development Assistance
MEA	Ministry of External Affairs
MEIS	Merchandise Exports from India Scheme
MRA	Mutual Recognition Agreements
MoD	Ministry of Defence

MoF	Ministry of Finance
MSME	Ministry of Micro Small and Medium Enterprises
MSMED	Micro Small and Medium Enterprises Development
MSTC	Metal Scrap Trade Corporation
NBFC	Non- Banking Financial Company
NC	Norms Committee
NFE	Net Foreign Exchange
NI	Non-Infringing
NCB	National Competitive Bidding
NOC	No Objection Certificate
PDS	Public Distribution System
PEC	Project and Equipment Corporation of India Ltd.
PIC	Policy Interpretation Committee
PRC	Policy Relaxation Committee
PAN	Permanent Account Number
PH	Personal Hearing
PTA	Preferential Trade Agreement
PSU	Public Sector Undertaking
R&D	Research and Development
RA	Regional Authority
RBI	Reserve Bank of India
RCMC	Registration-cum-Membership Certificate
REP	Replenishment
RPA	Rupee Payment Area
S/B	Shipping Bill
SAD	Special Additional Duty
SCOMET	Special Chemicals, Organisms, Materials, Equipment and Technology
SEI CMM	Software Engineers Institute's Capability Maturity Model
SEZ	Special Economic Zone
SEIS	Service Exports from India Scheme
SIA	Secretariat for Industrial Assistance
SIIC	State Industrial Infrastructure Corporation
SION	Standard Input Output Norms
SKD	Semi- Knocked Down
SLEPC	State Level Export Promotion Committee
STC	State Trading Corporation
STCL	Spices Trading Corporation Limited
STE	State Trading Enterprise
STH	Star Trading House
STPI	Software Technology Park of India
STR	State Trading Regime
SUVs	Sports Utility Vehicles

TED	Terminal Excise Duty
TEE	Towns of Export Excellence
TH	Trading House
TPO	Trade Promotion Organization
TRA	Telegraphic Release Advice
TRQ	Tariff Rate Quota
TUFS	Technology Upgradation Fund Scheme
UAC	Units Approval Committee
UN	United Nations
VA	Value Addition
WCO	World Customs Organisation
WHOGMP	World Health Organisation Good Manufacturing Practices

Study Note - 6

SERVICE TAX

This Study Note includes

6.1 INTRODUCTION

There is no separate Act for Service Tax. The provisions of service tax are contained in Chapter V of the Finance Act, 1994 and administered by the Central Board of Excise & Customs (CBEC).

Service tax is being imposed by amending Finance Act, 1994 and the scope has been amended time to time.

The power to change service tax vests with the Central Government. This authority is granted to the Central Government by Entry 92C (yet to be made effective) of the union list. However, currently, the service tax is collected under the power of the Residuary Entry 97 of the Union List.

Service tax was introduced in the year 1994. No separate Act on Service Tax is in force as yet but it finds its enactment in the Finance Act, 1994. Till date, the service tax amendments are being introduced by amending the Finance Act, 1994 from time to time. The taxable services are defined in section 65 of the Finance Act, 1994. Section 66 is the charging section of the said Act.

6.1.1 Statutes Governing the Levy of Service Tax

i. The Finance Act, 1994 Chapter V — Sections 64 to 96-I. This chapter extends to the whole of India except the State of Jammu and Kashmir.

ii. The Service Tax Rules, 1994. (Also referred to as 'Rules' or 'STR, 1994').

iii. The CENVAT Credit Rules, 2004.
iv. The Place of Provision of Services Rules, 2012
v. The Service Tax (Registration of Special categories of persons) Rules, 2005.
vi. The Service Tax (Determination of Value) Rules, 2006 (with effect from 19th April, 2006)
vii. The Point of Taxation Rules, 2011

6.1.2 Sources of Service Tax Law

As you are aware there is no separate Act for the service tax. However, the sources of service tax law are:

i. Finance Act, 1994
ii. Various Rules on service tax
iii. Notifications on service tax
iv. Circulars/Instructions on service tax issued by CBEC time to time
v. Orders on service tax published by the CBEC (Rule 3) and the Central Government (Section 95) and
vi. Trade notices on service tax issued by Central Excise and Service tax commissionerates

6.1.3 Extent and scope of service tax [section 64 of the Finance Act, 1994]

Chapter V of the Finance Act, 1994 (i.e. the service tax law), which came into force from 1-7-1994, extends to the whole of India except the state of Jammu and Kashmir. The various aspects relating to the extent of applicability of the service tax law are as follows:

(1) India [Section 65B(27)]: India means,-

(a) the territory of the Union as referred to in clauses (2) and (3) of Article 1 of the Constitution i.e. the States and Union Territories;

(b) its territorial waters, continental shelf, exclusive economic zone or any other maritime zone as defined in the Territorial Waters, Continental Shelf, Exclusive Economic Zone and other Maritime Zones Act, 1976;

(c) the seabed and the subsoil underlying the territorial waters;

(d) the air space above its territory and territorial waters; and

(e) the installations, structures and vessels located in the continental shelf of India and the exclusive economic zone of India, for the purposes of prospecting or extraction or production of mineral oil and natural gas and supply thereof.

(2) Service Tax extends to the Continental Shelf & Exclusive Economic Zone (CS & EEZ) of India [Notification No. 14/2010-S.T., dated 27-2-2010]: The Central Government has extended provisions of Chapter V of the Finance Act, 1994, to the following areas in the continental shelf and exclusive economic zone of India for the following purposes mentioned correspondingly –

Area	Purpose for which service tax law extended
(1) Whole of continental shelf economic zone of India and exclusive	Any service provided for all activities pertaining to construction of installations, structures and vessels for the purposes of prospecting or extraction or production of mineral oil and natural gas and supply thereof.
(2) Installations, structures and the continental shelf and vessels within the exclusive economic zone of India, constructed for the purposes of prospecting or extraction or production of mineral oil and natural gas.	Any service provided or to be provided by or to such installations, structures and vessels and for supply of any goods connected with the said activity.

(3) **Service tax doesn't extend to the State of Jammu and Kashmir:** This means that the services provided (as per the Place of provision of service rules, 2012) in the territorial jurisdiction of the State of Jammu and Kashmir are not liable to service tax. The location of the service provider or the service recipient doesn't matter.

6.1.4 Salient features of levy of service tax

The salient features of levy of service tax are as under -

(i) **Service defined:** The word service has been defined under section 65B(44) of the Chapter V of Finance Act, 1994. It is an exhaustive definition and covers all the activities except those specifically excluded from the ambit of service tax.

(ii) **Scope:** Section 66B is the charging section which provides that service tax shall be levied on all the services provided or agreed to be provided in a taxable territory other than services specified in Negative list.

(iii) **Negative list:** Section 66D specifies services which are covered in negative list. The *services so* specified go out of ambit of chargeability of service tax. In all, there are seventeen heads of services that have been specified in the negative list.

(iv) **Exempted Services:** In addition to services specified in negative list, a mega exemption Notification No. 25/2012-S.T., dated 20-06-2012 has been issued exempting many services from payment of service tax.

(v) While the services in the negative list are not taxable at all, the exempted services are those that are otherwise taxable but exempt *vide* notification issued by the Central Government.

(vi) **Declared services:** To avoid disputes between sale of goods and services, Section 66E provides certain activities to be specifically treated as declared services. Nine activities have been specified in the said section which are deemed to be declared service.

(vii) **Taxable Territory:** Since provision of service in taxable territory is an important ingredient of taxability, Section 66C empowers the Central Government to make rules for determination of place of provision of service. The Central Government has notified Place of Provision of Service Rules, 2012 in this regard.

(viii) **Principles of Interpretation:** Principles of Interpretation have been laid down in Section 66F of the Act for interpretation whenever services have to be treated differentially for any reason and also for determining the taxability of bundled services.

(ix) **Date of determination of rate of tax, value of taxable service & exchange rate:** Section 67A has been inserted w.e.f. 01-07-2012 which states that the rate of service tax, value of taxable service & exchange rate shall be the rate in force or as applicable at the time when taxable service has been provided or agreed to be provided. Point of taxation Rules, 2011 has been framed for this purpose.

As per newly inserted rule 11 of Service Tax Rules, 1994 dated 25.8.2014 vide Notification No. 19/2014-Service Tax provides that the rate of exchange for determination of value of taxable service shall be the applicable rate of exchange as per the generally accepted accounting principles on the date when point of taxation arises in terms of the Point of Taxation Rules, 2011.

(x) **Rate of service tax:** The rate of service tax specified under section 66B is 14% of value of taxable services. Swachh Bharat Cess has been levied u/s 119 of Finance Act, 2015 @ 0.5% w.e.f. 15-11-2015 on value of taxable services. Hence, effective rate of charge of service tax is 14.5% of value of taxable service.

(xi) **Valuation of services:** For the purpose of levy of service tax, the value of taxable service is to be determined in accordance with Section 67 read with Service Tax (Determination of Value) Rules, 2006.

(xii) **Payment of service tax:** The liability for payment of service tax is affixed either on service provider or on recipient of service (in case of reverse charge). With effect from 01-07-2012, a new scheme of taxation is brought into effect where the liability of payment of service tax will be shared by service provider as well as service recipient in specified services. This is called as partial reverse charge.

(xiii) Cenvat credit: The credit of service tax and excise duty across goods and services are available in accordance with Cenvat Credit Rules, 2004.

(xiv) Procedural compliances: Provisions have been made for registration, assessment including self assessment, rectification, special audit, appeals and penalties for non compliance of the provisions of the Act and Rules.

6.1.5 Concept of charge of service tax

Charge of service tax on and after Finance Act, 2012 [Section 66B]: There shall be levied service tax at the rate of 14.5% on the value of all services, other than those services specified in the negative list, provided or agreed to be provided in the taxable territory by one person to another and collected in such manner as may be prescribed.

Essentials for charge of service tax: Thus, important ingredients for charge of service tax are -

(i) The service should have been provided or agreed to be provided.

(ii) The service should be provided for a consideration.

(iii) The service should be provided by one person to another person.

(iv) The service should be provided in taxable territory *(i.e.* India excluding State of Jammu & Kashmir) as per Place of Provision of Service Rules, 2012.

(v) Services must not be specified in the negative list.

(vi) Service tax is levied @ 14% (increased by Swachh Bharat Cess @0.5%) of value of taxable service. Hence, effective rate is 14.5% of value of taxable service.

(vii) Service tax is collected in such manner as may be prescribed (i.e. in accordance with Service Tax Rules, 1994).

6.1.6 Nature of Service Tax

Service tax can be levied on the following:

(a) Taxable Service, and

(b) Value of Taxable Service.

Taxable Services

Service tax is levied on all services except negative list of services in the Finance Act, 1994. There are several services which are taxable if service is provided by a service provider; any person to any person.

However, all taxable services are NOT subject to service tax.

This is because taxability is not only dependent on the nature of service but also on—

(i) Who is the service provider,

(ii) Who is the service receiver.

Example 1:

X Ltd, an advertising company is not liable to collect and pay service tax on advertisement service rendered to the Approved International Organisation in India, even though for the same service to another entity X Ltd will have to collect and pay tax. ("Who is the Service receiver" principle)

Example 2:

Mr. A, a professional dealing in indirect tax gives consulting advice to the government of India, he is required to collect service tax from the Government of India and remit the same to the Service Tax department. However, if the Reserve Bank of India were to render the same service to the Government of India it is not required to collect and pay service tax. ("Who is the Service provider" principle) such services are taxable services; RBI is not liable to pay the service tax. Likewise any services provided by the service provider which are in the nature of statutory services, then service tax cannot be levied.

6.1.7 Service [Section 65B(44)]: "Service" means -

- any activity carried out by a person for another for consideration, and
- includes a declared service,
- but shall not include, -

  (a) An activity which constitutes merely, -

  (i) A transfer of title in goods or immovable property, by way of sale, gift or in any other manner; or

  (ii) Such transfer, delivery or supply of any goods which is deemed to be a sale within the meaning of Article 366(29A) of the Constitution; or

  (iii) A transaction in money or actionable claim;

  (b) A provision of service by an employee to the employer in the course of or in relation to his employment;

  (c) Fees taken in any Court or tribunal established under any law for the time being in force.

Explanation 1: For the removal of doubts, it is hereby declared that nothing contained in this clause shall apply to, -

(A) The functions performed by the Members of Parliament, Members of State Legislative, Members of Panchayats, Members of Municipalities and Members of other local authorities who receive any consideration in performing the functions of that office as such member; or

(B) The duties performed by any person who holds any post in pursuance of the provisions of the Constitution in that capacity; or

(C) The duties performed by any person as a Chairperson or a Member or a Director in a body established by the Central Government or State Governments or local authority and who is not deemed as an employee before the commencement of this section.

Explanation 2:

(i) For the purposes of this clause, transaction in money shall not include any activity relating to the use of money or its conversion by cash or by any other mode, from one form, currency or denomination, to another form, currency or denomination for which a separate consideration is charged.

(ii) any activity carried out, for a consideration, in relation to, or for facilitation of, a transaction in money or actionable claim, including the activity carried out —

  (a) by a lottery distributor or selling agent in relation to promotion, marketing, organising, selling of lottery or facilitating in organising lottery of any kind, in any other manner;

  (b) by a foreman of chit fund for conducting or organising a chit in any manner.

Explanation 3: For the purposes of this Chapter,-

(a) An unincorporated association or a body of persons, as the case may be, and a member thereof shall be treated as distinct persons;

(b) An establishment of a person in the taxable territory and any of his other establishment in a non-taxable territory shall be treated as establishments of distinct persons.

Explanation 4: A person carrying on a business through a branch or agency or representational office in any territory shall be treated as having an establishment in that territory.

The following are the ingredients of service, -

(1) Service means any activity carried out by a person:

(a) The term 'Activity' would include an act done, a work done, a deed done, an operation carried out, execution of an act, provision of a facility etc. It is a term with very wide connotation.

(b) Activity could be active or passive and would also include forbearance to act. Agreeing to an obligation, to refrain from an act or to tolerate an act or a situation has been specifically listed as a declared service under section 66E of the Act.

(2) The activity shall be carried out by one person for another person:

(a) Person [Section 65B(37)]: Person includes, -

- an individual,
- a Hindu undivided family,
- a company,
- a society,
- a limited liability partnership,
- a firm,
- an association of persons or body of individuals, whether incorporated or not,
- Government,

  Government [Section 65B (26A), inserted by the Finance Act, 2015, w.e.f. 14.05.2015]:

  "Government" means —

  (i) the Departments of the Central Government,

  (ii) a State Government and its Departments and

  (iii) a Union territory and its Departments,

  but shall not include any entity, —

  (A) whether created by a statute or otherwise,

  (B) the accounts of which are not required to be kept in accordance with article 150 of the Constitution or the rules made thereunder.

- a local authority, or
- every artificial juridical person, not falling within any of the preceding sub-clauses.

(b) Two separate persons are required for taxability: Service must be provided by one person to another i.e. service provider and service receiver. Thus, self service is outside the purview of service tax. However the following are its exceptions, -

- **Deemed Separate person:** As per Explanation 3 of Section 65B(44) which are as under,-

  (a) an establishment of a person located in taxable territory and another establishment of such person located in non-taxable territory are treated as establishments of distinct persons.

  (b) an unincorporated association or body of persons and members thereof are also treated as distinct persons.

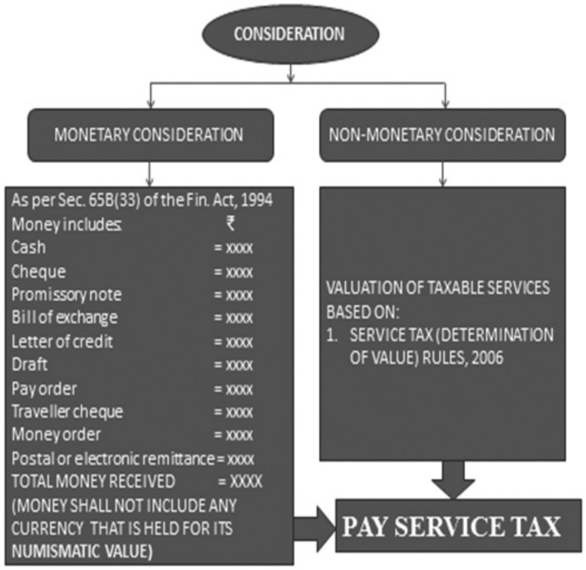
- **Implications of these deeming provisions:** Thus, inter-se provision of services between such persons, deemed to be separate persons, would be taxable. This provision is an exception to the 'principle of mutuality'.

Example 3:

(a) Services provided to the branch office in India of a multi-national company by the headquarters of the multi-national company located outside India;

(b) Services provided by a club to its members, would be taxable provided other conditions relating to taxability of service are satisfied.

(3) Activity must be carried out for a consideration:



(a) **Consideration:** "Consideration" means everything received or recoverable in return for a provision of service which includes monetary consideration as well as non-monetary consideration.

Monetary consideration: "Monetary consideration" means any consideration received in the form of money.

Non monetary consideration: Non-monetary consideration essentially means compensation in kind such as the following:

- Supply of goods and services in return for provision of service ;
- Refraining or forbearing to do an act in return for provision of service ;
- Tolerating an act or a situation in return for provision of a service;
- Doing or agreeing to do an act in return for provision of service.

In case of non-monetary consideration, the money value of such consideration is to be determined in accordance with Service Tax (Determination of Value) Rules, 2006.

(b) **Activities carried out without consideration are outside the scope of service:** Activity carried out without any consideration like donations, gifts or free charities are, therefore, outside the ambit of service.

Example 4:

(i) Grants given for a research where the researcher is under no obligation to carry out a particular research would not be a consideration for such research. Conditions in a grant stipulating merely proper usage of funds and furnishing of account also will not result in making it a provision of service.

(ii) Donations to a charitable organization is not consideration unless charity is obligated to provide something in return e.g. display or advertise the name of the donor in a specified manner or such that it gives a desired advantage to the donor. *(Circular No.* 127/09/2010-ST, *dated* 16-8-2010]

(c) **Consideration need not only be paid by service receiver:** Consideration may be paid by any person and not necessarily receiver of service.

(d) **Consideration must arise out of contractual reciprocity:** An activity done without express or implied contractual reciprocity of consideration would not be an activity for a consideration even if such activity may lead to accrual of gains to the person carrying out such activity.

Example 5:

(i) Life time achievement award will not comprise an activity for a consideration.

(ii) Artist performing at street where viewers are under no obligation to pay any amount.

(iii) Provision for free tourism, access to free TV channels or governmental activities without charges will not comprise an activity for a consideration.

(iv) Grant of pocket money, a gift or reward (which has not been given in terms of reciprocity), amount paid as alimony for divorce would be examples in this category.

However a reward given for an activity performed explicitly on the understanding that the winner will receive the specified amount in reciprocity for a service to be rendered by the winner would be a consideration for such service.

Thus amount paid in cases where people at large are invited to contribute to open software development (e.g. Linux) and getting an amount if their contribution is finally accepted will be examples of activities for consideration.

(e) Fines and penalties which are legal consequences of persons actions are not in nature of activity for a consideration.

(4) **Certain instances:**

Sl. No.	A Nature of payment	B Whether consideration for service?
1.	Amount received in settlement of dispute.	It shall not be regarded as consideration unless it represents a portion of the consideration for an activity that has been carried out. If the dispute itself pertains to consideration relating to service then it would be a part of consideration.
2.	Amount received advances for performance of service.	Such advances are consideration for the agreement to perform a service.
3.	Deposits returned on cancellation of an agreement to provide a service.	Returned deposits are in the nature of a returned consideration. If tax has already been paid the tax payer would be entitled to refund to the extent specified and subject to provisions of law in this regard.
4.	Advances forfeited for cancellation of an agreement to provide a service.	Since service becomes taxable on an agreement to provide a service such forfeited deposits would represent consideration for the agreement that was entered into for provision of service.
5.	Security deposit that is returnable on completion of provision of service.	Returnable deposit is in the nature of security and hence do not represent consideration for service. However if the deposit is in the nature of a colorable device wherein the interest on the deposit substitutes for the consideration for service provided or the interest earned has a perceptible impact on the consideration charged for service then such interest would form part of gross amount received for the service. Also security deposit should not be in lieu of advance payment for the service.

6.	Security deposits forfeited for damages done by service receiver in the course of receiving a service.	If the forfeited deposits relate to accidental damages due to unforeseen actions not relatable to provision of service then such forfeited deposits shall not be regarded as consideration and the same is specifically excluded in the Valuation Rule, 2006.
7.	Excess payment made as a result of a mistake.	If returned it is not consideration. If not returned and retained by the service provider it becomes a part of the taxable value.

(5) Declared Services:

The definition of service includes declared service. Declared services are activities that have been specified in Section 66E of the Act. When such activities are carried out by one person for another in the taxable territory for a consideration, then such activities are taxable services. In fact, most of the declared services have been specified with the intent of clarifying the distinction between the deemed sales and activities related thereto which are outside the realm of deemed sales but qualify as a service.

Exclusions from the definition of Service / Activities not covered under Service -

(1) Sale/Deemed sale/Transaction only in money do not constitute service:

(a) **Sale - Mere transfer in title of goods or immovable property:** Mere transfer in title of goods or immovable property by way of sale, gift or in any other manner for a consideration, does not constitute service.

(i) **Goods [Section 65B(25)]:** Goods means every kind of movable property other than actionable claim and money; and includes securities, growing crops, grass, and things attached *to or* forming part of the land which are agreed to be severed before sale or under the contract of sale.

(ii) **Immovable property [Clause (26) of the General Clauses Act, 1897]:** Immovable property to include land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth.

(iii) **Transfer of title:** "Transfer of title" means change in ownership. Mere transfer of custody or possession over goods or immovable property *where* ownership is not transferred does not amount to transfer of title. For example giving the property on rent or goods for use on lure would not involve a transfer of fide, and will therefore, be charged to service tax.

(iv) **Composite transactions:** A transaction which, in addition to a transfer of title in goods or immovable property, involves an element of another activity carried out or to be carried out by the person transferring the tide would not be out rightly excluded from the definition of service.

(b) **Deemed sales:** "Service" shall not include an activity which constitutes merely transfer, delivery or supply of *any* goods which is deemed to be sales within the meaning of Article 366(29A) of the Constitution. 'Deemed sales' refer to those transactions which will be deemed as sales even if, as per the normal definition, these cannot be held as sales.

Though deemed sales are outside the purview of 'Service' but activities related to deemed sales which qualify as a service, has been declared as a service as per the provisions of Section 66E of the Finance Act, 1994.

(c) **A mere transaction in money or actionable claims:** Any activity which constitutes merely a transaction in money or actionable claim will not constitute service.

(i) Money [Section 65B(33)]: "Money" means legal tender, cheque, promissory note, bill of exchange, letter of credit, draft, pay order, traveller cheque, money order, postal or electronic remittance or any such similar instrument but shall not include any currency that is held for its numismatic value.

(ii) Actionable Claim [Section 65B(1)]: Actionable claim shall have the meaning assigned to it in Section 3 of the Transfer of Property Act, 1882. As per Section 3 of the Transfer of Property Act, 1882 'Actionable claim' means a claim to,-

(a) any debt, other than a debt secured by mortgage of immovable property or by hypothecation or pledge of movable property; or

(b) any beneficial interest in movable property not in the possession, either actual or constructive, of the claimant, which the Civil Courts recognize as affording grounds for relief,

whether such debt or beneficial interest be existent, accruing, conditional or contingent.

Examples of actionable claims are -

- Unsecured debts;
- Right to participate in the draw to be held in a lottery.

[**Note:** Only those debts which can be enforced through Court of Law can be said to be actionable claims.]

(iii) Activities regarded as transaction only in money: The following are some of the activities which fall under this category -

(a) principal amount of deposits in, or withdrawals from a bank;

(b) advancing or repayment of principal sum on loan to some one;

(c) conversion of, say Z 1,000 currency notes into one rupee coins (to the extent amount is received in money form);

(d) actionable claims like transfer of unsecured debts.

Thus, transaction in money per-se would be outside the ambit of service.

Related activities covered: Any related activity for which separate consideration is charged would not be treated as transaction in money and would be chargeable to service tax if other elements of taxability are present.

For example: Making of a bank draft, where the bank charges a commission for the preparation of the same is not transaction only in money and the commission charged shall be the value of service provided.

(iv) Activities relating to use of money or its conversion into another form/currency/denomination for consideration included in definition of service [Explanation 2]:

(A) Activities relating -

- to use of money; or
- its conversion from one form, currency or denomination to another form, currency or denomination;

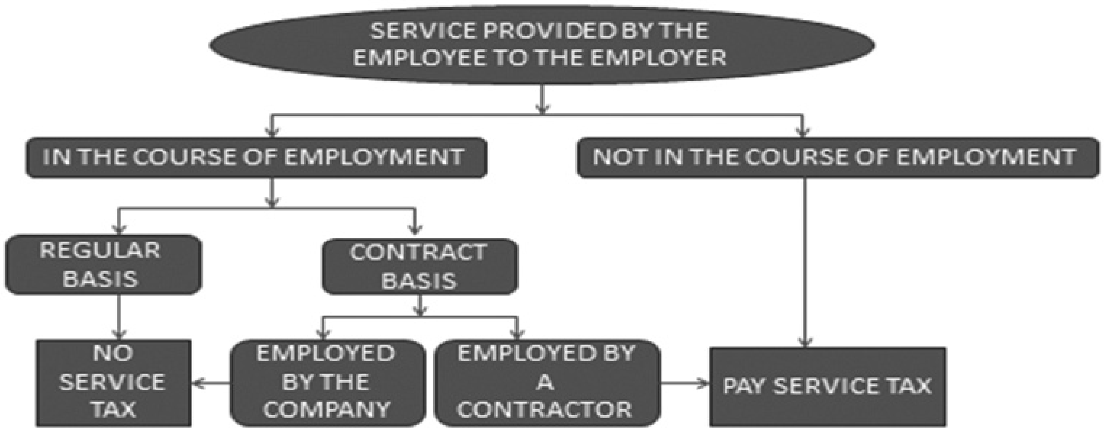
for which a separate consideration is charged; shall be included as 'service'.

(B) any activity carried out, for a consideration, in relation to, or for facilitation of, a transaction in money or actionable claim, including the activity carried out —

(a) by a lottery distributor or selling agent in relation to promotion, marketing, organising, selling of lottery or facilitating in organising lottery of any kind, in any other manner;

(b) by a foreman of chit fund for conducting or organising a chit in any manner.

(2) Service by an employee to employer in course of employment do not constitute service:



Any service provided by an employee to his employer during the course of his employment is outside the ambit of service. Therefore,-

Functions performed by MPs, MLAs, persons holding constitutional posts are not included in 'service' [Explanation 1]: As per explanation 1, the following functions/ duties will not be covered in service,-

(a) The functions performed by the Members of Parliament, Members of State Legislative, Members of Panchayats, Members of Municipalities and Members of other local authorities who receive any consideration in performing the functions of that office as such member; or

(b) The duties performed by any person who holds any post in pursuance of the provisions of the Constitution in that capacity; or

(c) The duties performed by any person as a Chairperson or a Member or a Director in a body established by the Central Government or State Governments or local authority and who is not deemed as an employee before the commencement of this section.

However, the following will be covered in scope of service -

(i) **Services provided outside employment for a consideration -Taxable:** Services provided outside employment for a consideration would be covered under the definition of 'service'.

Example: If an employee provides his service on contract basis to an associate of the employer, it would be covered under 'service'.

(ii) **Services provided on contract basis - Taxable:** Services provided on contract basis i.e. principal to principal basis are not services in course of employment and therefore come within the ambit of taxable service.

(iii) **Amounts received by an employee from the employer on premature termination of contract of employment - Not regarded as service:** Such amounts paid by the employer to the employee for premature termination of a contract of employment are treatable as amounts paid in relation to services provided by the employee to the employer in the course of employment. Hence, amounts so paid would not be chargeable to service tax.

(iv) **Non competing fees - Taxable:** Any amount paid for not joining a competing business would be liable to be taxed being paid for providing the service of forbearance to act.

(d) Status of services provided by casual workers or contract labour:

If	Then
Services provided by casual worker to employer who gives wages on daily basis to the worker	These are services provided by the worker in the course of employment
Casual worker are employed by a contractor, like a building contractor or a security service agency, who deploys them for execution of a contract or for provision of security services to a client.	Service provided by the workers to the contractor are services in the course of employment and hence not taxable. However, services provided by the contractor to his client by deploying such workers would not be a service provided by the workers to the client in the course of employment. The consideration received by the contractor would therefore be taxable if other conditions of taxability are present.

(3) Service of Court/Tribunal - Not covered:

Fees taken in any Court or tribunal established under any law for the time being in force is outside the coverage of 'service'

6.1.8 Extent and scope of levy of service tax on 'Composite contracts of sale and service'

The power to levy tax on sale of goods is within the legislative competence of the states. A transaction which in addition to a transfer of title in goods or immovable property involves an element of another activity carried out or to be carried out by the person transferring the title would not be outrightly excluded from the definition of service.

(1) If two transactions can be separable then service portion will be leviable to service tax: If two transactions, although associated, are two discernibly separate transactions then each of the separate transactions would be assessed independently. The service portion will only be liable for service tax.

Example 6: A builder carrying out an activity for a client wherein a flat is constructed by the builder for the client for which payments are received in instalments and on completion of the construction the title in the flat is transferred to the client involves two elements namely provision of construction service and transfer of title in immovable property. The two activities are discernibly separate. The activity of construction carried out by *the* builder would, therefore, be a service and the activity of transfer of title in the flat would be outside the ambit of service.

(2) Composite contract for sale of goods & **provision of services - Inseparable - 'Dominant Nature Test' applicable:** Service is different from sale. The fact that some goods have been used in the course of providing 'service' doesn't make that transaction a 'sale'.

The nature of the transaction depends on the intention of the parties. If the parties intended to enter into a transaction of purchase and sale of 'goods', the transaction will be 'sale' even though some services might have been provided, which will be taxed separately. However, in case where goods have been used in providing services or in case where the sale of goods is incidental to the provision of services, the transaction would primarily be that of service.

Therefore, if the predominant factor in a transaction is 'sale', the transaction would be classified as 'sale', however, if the predominant factor in a transaction is 'service', the transaction would be classified as 'service' only. This is commonly known as "Dominant Nature Test". - *Bharat Sanchar Nigain Ltd. v.* i.IOI [2006] 2 STR 161 (SC)

(3) Exceptions to Dominant Nature Test - Transactions of 'deemed sales' under Constitution [Article 366(29A)]: As per Article 366(29A) of Constitution of India, sale includes some transactions which are regarded as deemed sale. The dominant nature test doesn't apply to the aforesaid transactions of deemed sales, which are deemed to divisible. The 'sale' element, which is deemed to be divisible, cannot be subjected to service tax.

Further, the States can impose tax only on the 'sale' element of these transactions; the States cannot impose any tax on 'service element' in these transactions, as the 'service element' can be taxed only by Parliament/ Centre.

The present status as regards taxation of deemed sales is as under -

		'Sale Element'	'Service Element'
(1)	**Transfer, otherwise than in pursuance of a contract**	Transfer, otherwise than in pursuance of a contract, of property in any goods for cash, deferred payment or other valuable consideration;	There is no service element
(2)	**Works Contract**	Transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;	Service portion in the execution of a works contract is a declared service under section 66E(h);
(3)	**Hire-purchase contract**	Delivery of goods on hire-purchase or any system of payment by installments;	Activities in relation to delivery of goods on hire purchase or any system of payment by instalments is a declared service under section 66E(g);
(4)	**Lease contract**	Transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration;	Transfer of goods by way of hiring, leasing, licensing or in any such manner without transfer of right to use such goods is a declared service under section 66E(f);
(5)	**Supply of goods by association to its members**	Supply of goods by any unincorporated association or body of persons to a member thereof for cash, deferred payment or other valuable consideration;	According to section 65B(44) explanation 3(b), An unincorporated association or a body of persons, as the case may be, and a member thereof shall be treated as distinct persons and provision of service between them is chargeable to tax.
(6)	**Catering Contract**	Supply, by way of or as part of any service or in any other manner whatsoever, of goods, being food or any other article for human consumption or any drink (whether or not intoxicating), where such supply or service, is for cash, deferred payment or other valuable consideration.	Service portion in an activity wherein goods, being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as a part of the activity is a declared service under section 66E(i).

6.2 REGISTRATION UNDER SERVICE TAX

Any person liable to pay service tax has to register with the Superintendent of Central Excise (Section 69) within 30 days from the date of commencement of the business of providing taxable service (Rule 4 of Service Tax Rules, 1994).

Service Tax Registration is required if —

i. the taxable turnover of the service provider during the previous year exceeds ₹ 9 lakhs, or

ii. the service provider is acting as an input service distributor irrespective of his turnover.

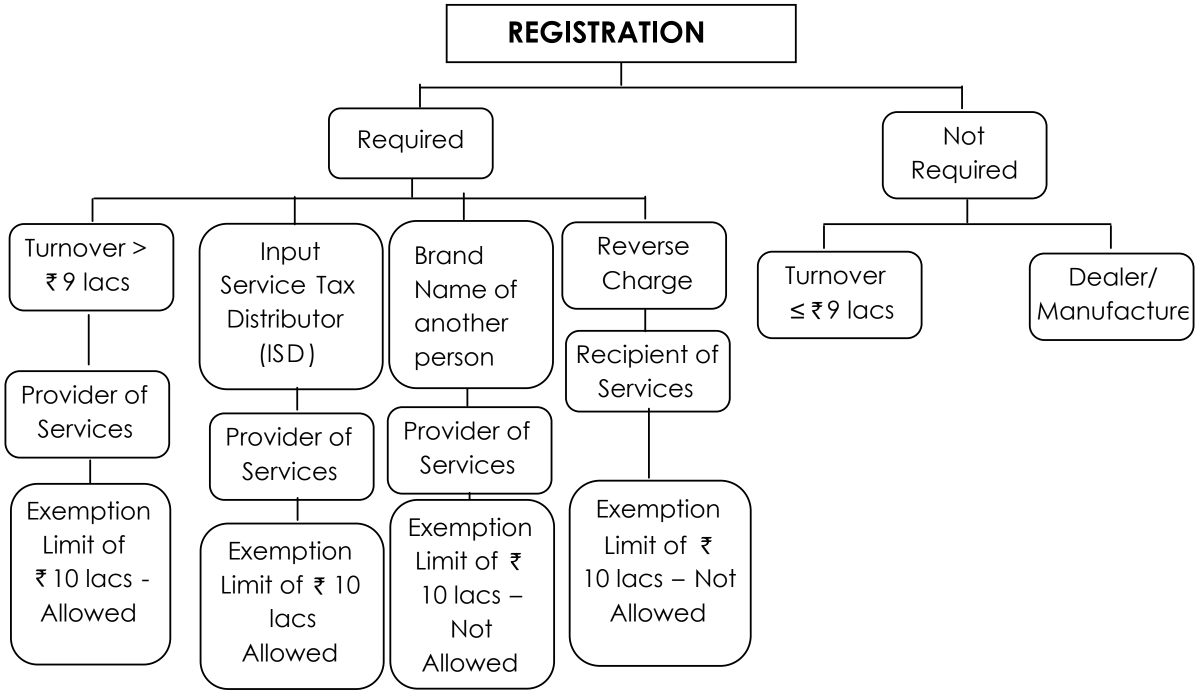
iii. Service provider provided services under the brand name of another person.

iv. the service receiver is liable to pay service tax being recipient of any services under Reverse Charge.

A service provider whose value of service exceeds ₹ 9 lakhs, in the year of providing the service or in any subsequent year, when the value of service cross ₹ 9 lakh for the first time, would require registration, however such service provider can avail exemption if the value of service does not exceed ₹ 10 Lakhs per annum.

Small Service Provider Exemption

Service tax provides for an exemption to small service providers who provide taxable services of a value not exceeding the specified limit. The specified limit is now ₹ 10 lakhs. In other words where the value of taxable services provided do not exceed ₹ 10 lakhs in the previous financial year, the concerned service provider would not be required to pay service tax upto receipts of ₹ 10 lakhs in the current financial year. The exemption is through notification 6/2005 ST dated 01.03.05 as amended from time to time.



6.2.1 Registration procedure under Service Tax

Step 1: Apply for registration in Form ST-1 to the Superintendent of Central Excise

Step 2: Submit along with Form ST-1 the following documents

- Permanent Account Number (PAN)
- Affidavit declaring the commencement of the services (prescribed Format)
- Copy of passport or ration card or any other document as residential proof
- Passport size photograph of the assessee in case of individual and of partners in the case of partnership firm and of directors in the case of a company.
- Partnership deed in case of firm
- Memorandum and Articles of Association in case of company

Step 3: The Superintendent of Central Excise will grant a certificate of registration in Form ST-2 within 7 days of the date of receipt of the application. If the registration is not granted within 7 days registration is deemed to be granted. It means deeming provision in rule 4(5) is applicable to registration granted by the Superintendent of Central Excise. However, no time stipulated on the Commissioner of Central Excise to grant centralized centralised registration under rule 4(2), the provision of deemed registration is not attracted in case of grant of centralised registration by the Commissioner *[Karamchand Thapar & Bros. (Coal Sales) Ltd. v UOI 2010 (20) STR 3 (Cal)]*.

Step 4: Certificate of Registration can be surrendered if the assessee ceases to provide the taxable services for which he had been registered.

Where a service is rendered from different locations falling under different Commissionerates, multiple registrations are required. However, even in this case a single registration is possible, with the permission from the Department, if the assessee maintains centralized billing or centralized accounting for multiple services provided from more than one premises.

> Dealer's registration not available under service tax unlike First Stage Dealer and Second Stage Dealer under Central Excise

Such permission can be granted by the Chief Commissioner of Central Excise or Commissioner of Central Excise if all the premises are falling under the jurisdiction of one Chief Commissioner or Commissioner.

If the premises of the assessee are falling under the jurisdiction of more than one Chief Commissioner then the permission has to be got from the Director General of Service Tax (DGST).

Registration under service tax can also be done through online system namely ACES mode (i.e. Automation of Central Excise and Service Tax).

6.2.2 Registration in case of Multiple Services

One application for registration is enough even though the service provider is providing or provides multiple services. Registration is not granted service wise but assessee wise. All services can be mentioned in one ST-1 form and the same can be submitted in the office of the Superintendent of Central Excise.

Example 7:

Mr. B is providing erection, commissioning and installation and mining services in addition to Mandap keeping services. How many applications for registration under service tax provisions Mr. B need to apply?

Answer:

Single ST-1 Form is enough for all multiple services rendered by Mr. B.

6.2.3 Transfer of Business

If the assessee transferred his business to another person, the transferee shall obtain a fresh certificate of registration. Certificate of registration is non-transferable.

Example 8:

Mr. Ram provider of interior decorating services since 2009, hold's service tax registration under service tax provisions. Mr. Ram subsequently sold the entire business to Mr. Y for ₹ 10 lacs. You are required to answer wether the registration number of Mr. Ram will be the registration number of Mr. Y?

Answer:

No, the registration certificate under the service tax is non-transferable.

6.2.4 Amendments in Registration Certificate

Certain changes may require amendments in registration certificate. Whereas any change in constitution of the business, new registration number is required to be obtained.

Changes in registration certificate:

In Case of

i. Service provider providing new taxable service other than that provided in the registration certificate.

ii. Change in the information supplied in form ST-1 e.g. change in name or address of the applicant, various premises exam which service is provided etc.

Service provider should furnish such additional information or details, in writing to the jurisdictional Assistant Commissioner or Deputy Commissioner of Central Excise within 30 days of such change.

Hence, the revised registration certificate will be issued after cancelling the registration certificate issued earlier. However, no new registration number will be allotted.

Change of business constitution:

Where there in change in the constitution of business such as, a new registration certificate for the changed form of business need to be obtained, like partnership firm converting into a private limited or public limited company, a private limited company converted into public limited company and so on. In the case of change, the transferee needs to obtain a fresh new registration certificate with a new number.

6.2.5 Salient Features of STC

Service Tax Registration number also known as Service Tax Code (STC) contains 15 digits PAN based number.

i. The first 10 digits of this number (i.e. STC) are the same as the PAN of such person.

ii. Next 2 digits are ST

iii. Next 3 digits are serial numbers indicating the number of registrations taken by the service taxpayer against a common PAN. (for example 001 for one registration number, 002 for two registration numbers of such a person having common PAN for such premises)

6.2.6 Premises Code

In addition to PAN based STC number, another number, namely, 'premises code' is also given in the registration certificate (i.e. ST-2). This number indicates the code of the jurisdictional Commissionerate, division, range and serial number within the range. This number is issued for easy identification of location of registration of the service tax payer.

6.2.7 Multiple Centralized Registration

A bank has its head office at Mumbai and regional offices at Chennai, Hyderabad and Cochin and the bank has centralized billing or centralized accounting facilities available at each of these regional offices, in addition to the Head office. Such bank at its option can obtain multiple centralized registration for each regional offices for the purpose of discharging the service tax liability.

6.2.8 Cancellation or Surrender of Registration Certificate

Once registration is granted it will be valid till such time it is surrendered. However, registration can be cancelled in the following cases:

i. Service provider ceases to provide the taxable service

ii. Service provider deceased (in case of a sole proprietor)

iii. Service provider transferred his business in favour of others

Before cancellation of registration the Superintendent of Central Excise shall ensure that the assessee has paid all monies due to the Central Government and then cancel the registration certificate.

6.2.9 Input Service Distributor (ISD)

In case of input service distributor registration under Service Tax provisions is compulsory irrespective of the turnover limit.

Input service distributor means an office managing the business of manufacturer or producer of final products or provider of output services, which receives invoices issued under Rule 4A of the Service Tax Rules, 1994 towards purchase of input services and issues invoice, bill or, as the case may be, challan for the purpose of distributing the credit of service tax paid under said services to such manufacturer or producer or provider, as the case may be. [Rule 2(m) of the CENVAT CREDIT RULES, 2004]

Manner of distribution of credit by input service distributor (Rule 7 of the CENVAT CREDIT RULES, 2004) (w.e.f. 1-4-2012):

The input service distributor may distribute the CENVAT CREDIT in respect of the service tax paid on the input service to its manufacturing units or units providing output service, subject to the following conditions, namely:-

(a) The Input service distributor must ensure that such a distribution should not exceed the service tax paid.

(b) In case an input service is attributable to service use in a unit exclusively engaged in manufacture of exempted goods or exempted services, then such credit of service tax shall not be distributed.

(c) Credit of service tax attributable to service used wholly in a unit shall be distributed only to that unit; and

(d) Credit of service tax attributable to service used in more than one unit shall be distributed pro-rata on the basis of the turnover of the concerned unit to the sum total of the turnover of all the units to which the service relates.

Example 9:

X Ltd. has three units namely:

Place	Nature	Turnover for the April 2015 (₹)	Output
Chennai	Factory	2,50,000	Dutiable goods
Bangalore	Factory	1,50,000	Dutiable goods
Hyderabad	Service unit	1,10,000	Taxable service
Total		**5,10,000**	

M/s Mudra Pvt. Ltd an advertising agency provided services for ₹ 3,00,000 in the month April 2015 by charging Service Tax @14.5% to X Ltd. to promote products of Chennai and Bangalore factories. However, Hyderabad unit not received input services from M/s Mudra Pvt. Ltd.

In the given case X Ltd can distribute the CENVAT CREDIT on input service to Chennai and Bangalore factory, in respect of their turnover ratio. It means input service distributor should not distribute the CENVAT CREDIT on input service to the Hyderabad unit. Since, this unit were not received any input service.

6.2.10 Penalty for late Registration

If there is delay, interest for delayed payment will have to be paid, which cannot be waived. Though there is no mandatory penalty for delay in registration, penalty upto ₹ 10,000 can be imposed under section 77(1) of Finance Act, 1994 as amended w.e.f. 10th May, 2013.

If an assessee proves that there was reasonable cause for delay in registration or payment of service tax, the penalty can be waived. However, interest under section 75 for late payment of service tax is automatic and it cannot be waived.

6.3 REVERSE CHARGE

Every person providing a taxable service is required to pay service tax at the prescribed rate. However in certain cases the service recipient is made liable to pay service tax on the services received. Since the person receiving services is made liable to pay service tax, the mechanism of collection of such tax is called as reverse charge (RCM).

This concept is set out in service tax law by virtue of section 68(2) by empowering the Central Government to notify services positively on which the said RCM would apply. To support this the person liable to pay service tax as defined in rule 2(1)(d) of the Service Tax Rules, 1994 also includes service recipients.

The SSI exemption is not available for the service tax payable under reverse charge in Service tax, person receiving the service covered under RC is liable to pay irrespective of quantum.

However, in addition to the concept of reverse charge a new concept of joint charge (recipient and provider of services liable to pay tax) is also introduced.

Joint Charge Mechanism

Under the concept of joint charge, for one service the service provider as well as service receiver is made liable for payment of service tax to the extent notified. This liability is independent of the other person's liability. In other words the failure to comply with the provisions by one person on his part would not impact the compliance requirement of other person and vice versa.

The notified taxable services are as follows:

(i) **Insurance Services:** General Insurance Services or Life Insurance Services provided by the insurance agents to the insurance company. Hence, the insurance company being recipient of service is liable to pay service tax. However, an option to pay service tax at a rate other than standard rate (i.e. 14.5%) is given an insurer carrying on life insurance business. Life insurance company collects premium which covers risk plus savings has option to pay service tax @ 3% 1ST YEAR AND SUBSEQUENTLY @1.5% on PREMIUM (w.e.f. 1-4-2012). Cenvat Credit Fully Allowed on Inputs, Capital Goods and Input Services.

   (i) However, such option shall not be available in cases where

   (ii) the entire premium paid by the policy holder is only towards risk cover in life insurance; or

   (iii) the part of the premium payable towards risk cover in life insurance is shown separately in any of the documents issued by the insurer to the policy holder.

(ia) provided or agreed to be provided by a recovery agent to a banking company or a financial institution or a non-banking financial company.

(ii) **Import of Services:** Services imported from a country outside India, into India for business or commerce. Hence, the importer being recipient of service is liable to pay service tax.

Example 10: X Ltd an Indian company, imported services from A Ltd of USA for the personal purposes. X Ltd liable to pay service tax in India, since there is no personal service in the case of a body corporate.

(iii) **GTA Services:** As per the new rule, if the person liable for making payment of freight in a specified person then he is liable to pay taxes otherwise GTA is liable to pay taxes.

Goods Transport Agency means any person who provides service in relation to transport of goods by road and issues consignment note.

RULE 4B: Issue of consignment note - Any goods transport agency which provides service in relation to transport of goods by road in a goods carriage shall issue a consignment note to the recipient of Service:

Provided that where any taxable service in relation to transport of goods by road in a goods carriage is wholly exempted under section 93 of the Act, the goods transport agency shall not be required to issue the consignment note.

Explanation - For the purposes of this rule and the second proviso to rule 4A, "consignment note" means a document, issued by a goods transport agency against the receipt of goods for the purpose of transport of goods by road in a goods carriage, which is serially numbered, and contains the names of the consignor and consignee, registration number of the goods carriage in which the goods are transported, details of the goods transported, details of the place of origin and destination, person liable for paying service tax whether consignor, consignees or the goods transport agency.

Contents of Consignment Note:

(i) Name of the consignor or consignee

(ii) Registration number of the goods carriage (i.e. vehicle registration number)

(iii) Details of goods transported

(iv) Details of the place of origin and destination

(v) Person liable for paying service tax whether consignor, consignee or the goods transport agency.

Exemption based on amount charged:

The gross amount charged on an individual consignment transported in a goods carriage does not exceed ₹ 750 (i.e. Freight collected for transporting small consignment for persons, who paid less than or equal to ₹ 750 for each consignment) or

The gross amount charged on consignments transported in a goods carriage does not exceed ₹ 1,500 (i.e. Freight collected for transporting goods in small vehicles for persons, who paid less than or equal to ₹ 1,500 per trip)

Note: (i) An individual consignment means all goods transported by a goods transport agency by road in a goods carriage for a consignee.

(ii) S.T. is Payable afer Claiming an Abatement @ 75%

(iv) Sponsorship services to any body corporate or firm located in Taxable Territory: In case of sponsorship service provided to a body corporate or firm located in India, the body corporate or firm receiving such services will be liable to pay service tax. However, if the recipient of sponsorship service is located outside India, service tax is required to be paid by the service provider and not by the recipient of such sponsorship services.

Example 11:

Ferrari conducting the Formula 1 races by displaying logo or brand name of various companies. Hence, companies receiving sponsorship services from Ferrari are liable to pay service tax.

Example 12:

Sponsorship services provided for events like Indian Premier League (IPL) cricket matches, golf and tennis etc., are covered under reverse charge.

(iva) provided or agreed to be provided by a director of a company or a body corporate to the said company or the body corporate.

(v) Services Provided by an Arbitral Tribunal to any business entity located in taxable territory then recipient of service is liable to pay service tax (w.e.f. 1-7-2012)

(vi) Legal Consultancy Service: In case of Services provided by an individual advocate or a firm of advocates by way of legal services to any business entity located in the taxable territory, the recipient of such services is liable to pay service tax.

(vii) Support Services by Govt. or Local Authority: Support services provided by Govt. or local authority to a business entity then the liability to pay S.T. is on the business entity.

Support services includes :

i. Infrastructural

ii. Operational

iii. Administrative

iv. Logistic,

v. marketing

(viii) Directors Remuneration (VIDE NT 45/2012 W.E.F. 7-8-2012): Services provided or agreed to be provided by a director of a company to the company, such company would be liable to pay service tax on remuneration paid to such directors.

Note: No service tax is payable if the director is employee of the company.

List 1 - Service under Full Reverse Charge Mechanism:

Sl. No.	Nature of Service	Description of services	Percentage of Service tax payable by the person providing service	Percentage of Service tax payable by the person receiving the service
i.	Goods transport Service	Transport of goods by road (If the person is specified person)	Nil	100%
ii.	Sponsorship Service	Sponsorship service	Nil	100%
iii.	Legal Services	Legal Serivces by Individual advocate or a firm of advocate including arbitral services.	Nil	100%
iv.	Government Services	Support services by Government or local authority (excluding renting of immovable property and certain other specified services)	Nil	100%
v.	Directors Fees	Services provided or agreed to be provided by a Director of a company or a body corporate to the said company or the body corporate.	Nil	100%
vi.	Import of Service	Any taxable service where the Service provider is located in a non taxable territory and service recipient located in a taxable territory	Nil	100%

vii.	Recovery Agents Service	Services provided by Recovery Agents to Banks Financial Institutions and NBFC.	Nil	100%
viii.	Insurance Business	Service provided or agreed to be provided by an insurance agent to any person carrying on insurance business.	Nil	100%
ix.	Any taxable service	Any taxable services provided or agreed to be provided by any person who is located in a non-taxable territory and received by any person located in the taxable territory.	Nil	100%
x.	Lottery agents	Selling or marketing agent of lottery tickets	Nil	100%
xi.	Manpower/ Security	Any individual/ HUF/ Firm/ LLP/ AOP located in taxable territory by way of — • supply of manpower for any purpose or, • security services	Nil [25% upto 31.03.2015]	100% [75% upto 31.03.2015]
xii.	Mutual Fund agent	Mutual Fund agent or distributor	Nil	100%

(ix) Partial Reverse Charge (w.e.f. 1-7-2012)

By the virtue of powers conferred under Sub-section (2) of Section 68 of the Act, the Central Govt. has issued notification dated 1.7.2012 notification dated 1.7.2012 notifying the following below services which shall be covered under the partical reverse charge mechanism.

Partial reverse charge is applicable in relation to service provided or agreed to be provided by way of renting of a motor vehicle designed to carry passengers to any person who is not in the similar line of business or supply of manpower for any purpose of service portion in execution of works contract by any individual, hindu undivided family or partnership firm whether registered or not, including association of person, located in the taxable territory to a business entity registered as body corporate, located in the taxable territory, both the service provider and the service recipient to the extent notified under sub-section (2) of section 68 of the act, for each respectively.

"Body Corporate" or "corporation" includes a company incorporated outside India but does not include –

(a) a corporation sole;

(b) a co-operative society registered under any law relating to co-operative societies; and

(c) any other corporate (not being a company as defined in this act) which the central Government may, by notification in the Official Gazette, specify in this behalf.

The service provider and service recipient will pay the service tax in the following proportion as notified by the Government:

List 2 - Service under Partial Reverse Charge Mechanism:

S. No.	Nature of Service	Description of services	Percentage of Service tax payable by the person providing service	Percentage of Service tax payable by the person receiving the service
i.	Rent-a-cab Service	Hiring of a motor vehicle designed to carry passengers		
		(a) With abatement (i.e. 60%)	Nil	100%
		(b) Without abatement	50%	50%
ii.	Works contract service	Works contract service	50%	50%

Partial Reverse Charge is not Applicable in the following cases:

Service Provider	Recipient of Service
Company or body corporate	Individual or partnership firm or body corporate or any other person
Renting of motor vehicle designed to carry passengers by individual / firm / HUF/AOP	Any person who is in the same business of carry in passengers (i.e. sub-contract)

6.4 BRAND NAME OF ANOTHER PERSON

Service provider who is providing taxable services under the brand name of another person is not eligible for claiming exemption limit of ₹ 10 lakhs and hence, is liable to pay service tax irrespective of the turnover.

Notification No. 8/2005-ST clearly provides that small scale service provider exemption will not be applicable to taxable services provided by a person under a brand name or trade name, whether registered or not, of another person.

Example 13: Mr. Ram who markets his goods under the brand name of TATA Company. Therefore, it is very clear that Mr. Ram is a provider of services under the brand name of the company and his services are taxable under Business Auxiliary Services. Hence, he can not avail the benefit of ₹ 10,00,000 exemption.

6.5 PAYMENT OF SERVICE TAX [RULE 6]

Service Tax on value of taxable services provided or received during the calendar month whichever is earlier should be paid by the 6th of the following month. In case the assessee is an individual or proprietary firm or partnership firm (other than HUF) or Limited Liability Partnership firm, the tax is payable on quarterly basis within 6 days from the end of the quarter.

If the payment is made through any other mode, such payment can be made by the 5th of the following month or following quarter as the case may be.

If the last day of payment and filing return is a public holiday, tax can be paid and return can be filed on the next working day.

In case of individual and partnership firms whose aggregate value of taxable services provided from one or more premises is fifty lakh rupees or less in the previous financial year, the service provider shall have the option to pay tax on taxable services provided or agreed to be provided by him up to a total of rupee fifty lakhs in the current financial year, by the dates specified in sub-rule (1) with respect to the month or quarter, as the case may be, in which payment is received.

Every assessee shall electronically pay the service tax payable by him, through internet banking. Provided that the Assistant Commissioner or the Deputy Commissioner of Central Excise, as the case may be, having jurisdiction, may for reasons to be recorded in writing, allow the assessee to deposit the service tax by any mode other than internet banking.

Manual Payment of service tax may be either by cheque or cash depositing it through GAR-7 Challan with the bank designated by the CBEC.

Delay in payment of service tax attracts the simple interest (as per Section 75 of the Finance Act, 1994) at the rate as prescribed below and penalty. Notification No. 26/2004, dated 10-9-2004 has specified the rate. The table below shows the rate of interest applicable at relevant period of time:

Interest on delayed payment of service tax - Section 75 of the Finance Act, 1994

Sr. No.	Period	Rate of Interest	
i.	Till 11-5-2001	1.5% per month	
ii.	11-5-2001 to 11-5-2002	24% per annum	
iii.	11-5-2002 to 10-9-2004	15% per annum	
iv.	From 10-9-2004 to 31-3-2011	13% per annum	
v.	From 1-4-2011	15% per annum (whose annual turnover of taxable services during the previous year is ₹ 60 lakh).	
vi.	From 1-10-2014	<u>Extent of delay</u>	
		up to 6 months	18%
		From 6 months and upto 1 year	24%
		More than one year	30%
		<u>Extent of delay for small assessees having annual turnover upto ₹60 lacks in the previous year</u>	
		up to 6 months	15% p.a.
		From 6 months and upto 1 year	21% p.a.
		More than one year	27% p.a.

6.6 RATE OF SERVICE TAX

The table below shows the rate of service tax applicable at the relevant period of time:

Sr. No.	Period	Rate of Service Tax	Rate of Education Cess
i.	Till 13-5-2003	5%	Nil
ii.	14-5-2003 to 9-9-2004	8%	Nil
iii.	10-9-2004	10%	2% of the S.T.
iv.	18-4-2006 onwards	12%	2% of the S.T. and 1% SAH w.e.f. 11th May 2007
v.	w.e.f. 24-2-2009	10%	2% plus 1% cess
vi.	w.e.f. 01 -04-2012	12%	2% plus 1% cess
vii.	w.e.f. 15 -11-2015	14.5% (including Swachh Bharat Cess	

Note: SAH means Secondary and Higher Education Cess.

6.7 INVOICES UNDER SERVICE TAX

RULE 4A: Taxable service to be provided or credit to be distributed on invoice, bill or challan –

(1) Every person providing taxable service shall, not later than thirty days from the date of completion of such taxable service or receipt of any payment towards the value of such taxable service, whichever is earlier, issue an invoice, a bill or, as the case may be, a challan signed by such person or a person authorized by him in respect of such taxable service provided or agreed to be provided and such invoice, bill or, as the case may be, challan shall be serially numbered and shall contain the following, namely :-

(i) the name, address and the registration number of such person;

(ii) the name and address of the person receiving taxable service;

(iii) description and value of taxable service provided or agreed to be provided; and

(iv) the service tax payable thereon.

Provided that in case the provider of taxable service is a banking company or a financial institution including a non-banking financial company providing service to any person, an invoice, a bill or, as the case may be, challan shall include any document, by whatever name called, whether or not serially numbered, and whether or not containing address of the person receiving taxable service but containing other information in such documents as required under this sub-rule:

Provided further that in case the provider of taxable service is a goods transport agency (GTA), providing service to any person, in relation to transport of goods by road in a goods carriage, an invoice, a bill or, as the case may be, a challan shall include any document, by whatever name called, which shall contain the details of the consignment note number and date, gross weight of the consignment and also contain other information as required under this sub-rule.

Provided also that in case of continuous supply of service, every person providing such taxable service shall issue an invoice, bill or challan, as the case may be, within thirty days of the date when each event specified in the contract, which requires the service receiver to make any payment to service provider, is completed.

Provided also that in case the provider of taxable service is a banking company or a financial institution including a non-banking financial company providing service to any person, the period within which the invoice, bill or challan, as the case may be, is to be issued, shall be forty-five days:

Provided also that in case the provider of taxable service is providing the service of transport of passenger, an invoice, a bill or as the case may be, challan shall include ticket in any form by whatever name called and whether or not containing registration number of the provider of service and address of the recipient of service but containing other information in such documents as required under this sub-rule.

Provided also that wherever the provider of taxable service receives an amount upto rupees one thousand in excess of the amount indicated in the invoice and the provider of taxable service has opted to determine the point of taxation based on the option as given in Point of Taxation Rules, 2011, no invoice is required to be issued to such extent.

(2) Every input service distributor distributing credit of taxable services shall, in respect of credit distributed, issue an invoice, a bill or, as the case may be, a challan signed by such person or a person authorized by him, for each of the recipient of the credit distributed, and such invoice, bill or, as the case may be, challan shall be serially numbered and shall contain the following, namely:-

(i) the name, address and registration number of the person providing input services and the serial number and date of invoice, bill, or as the case may be, challan issued under sub-rule (1);

(ii) the name, and address of the said input services distributor;

(ill) the name and address of the recipient of the credit distributed;

(iv) the amount of the credit distributed.

Provided that in case the input service distributor is an office of a banking company or a financial institution including a non-banking financial company providing service to any person an invoice, a bill or, as the case may be, challan shall include any document, by whatever name called, whether or not serially numbered but containing other information in such documents as required under sub-rule.

6.8 RECORDS TO BE MAINTAINED

Rule 5: Records

(1) The records including computerized data as maintained by an assessee in accordance withnthe various laws in force from time to time shall be acceptable.

(2) Every assessee shall furnish to the superintendent of Central Excise at the time of filing of return for the first time or the 31st day of January, 2008, whichever is later, a list in duplicate, of –

(i) all the record prepared or maintained by the assessee for accounting of transactions in regard to,-

(a) Providing of any service;

(b) receipt pr procurement of input services and payment for such input services;

(c) receipt, purchase, manufacture, storage, sale, or delivery, as the case may be, in regard of inputs and capital goods;

(d) other activities, such as manufacture and sale of goods, if any.

(ii) all other financial records maintained by him in the normal course of business.;

(3) All such records shall be preserved at least for a period of five years immediately after the financial year to which such records pertain.

Explanation – For the purpose of this rule, "registered premises" includes all premises or offices from where an assessee is providing taxable services.

6.9 AUTOMATION OF CENTRAL EXCISE AND SERVICE TAX (ACES)

The Central Board of Excise & Customs (CBE & C) has developed a new software application called *Automation of Central Excise and Service Tax (ACES),* which aims at improving tax-payer services, transparency, accountability and efficiency in indirect tax administration.

It is a centralized, web based software application which automates various processes of Central Excise and Service Tax for Assessees and Department, and gives complete end to end solution.

In ACES, the various processes of Service Tax automated are —

i. Registration,

ii. Returns,

iii. Refunds,

iv. ST-3A,

v. Dispute Resolution and

vi. Audit.

ACES can be used for:

i. Online registration and amendment of registration details
ii. Electronic filing of documents such as Returns, Claims, Intimations and permissions
iii. Online tracking of the status of applications, claims and permissions
iv. Online facility to view documents like Registration Certificate, Returns, Show Cause Notice, Order-In-Original etc.

Certified Facilitation Centre (CFC)

CFC stand for Certified Facilitation Centre under ACES project of CBEC and is an e-facility, which may be set-up and operated by a Cost Accountant/Chartered Accountant/Company Secretary or a proprietary concern/firm of Cost Accountants or Chartered Accountants or Company Secretary in practice to whom a certificate is issued under the ACES project, where the assessees of Central Excise and Service Tax can avail this facility to file their returns and other documents electronically along with associated facilitation on payment of specified fees.

6.10 ELECTRONIC ACCOUNTING SYSTEM IN EXCISE AND SERVICE TAX (EASIEST)

EASIEST has been developed to make payment of tax easy. An assessee paying service tax manually by filing GAR – 7 challan one single copy of challan and its acknowledgement is sufficient. This facility is available with 28 banks across the India.

Benefits of EASIEST:

(a) One copy of the challan has to be filled (earlier 4 copies were required to file):
(b) Facility of online verification of the status of tax payment using Challan Identification Number.

PRACTICAL PROBLEMS

Registration

Example 14: Sri R is a practicing Chartered Accountant. His Gross taxable services during the year 2015-16 are ₹ 9,50,000. Is Registration compulsory for him? If so in which year?

Answer:

Yes, Registration is compulsory in the year 2015-16 (i.e. exceeded ₹ 9,00,000).

Example 15: Mr. Hari, an engineer, renders the taxable services during the year 2014-15 for ₹ 4,00,000. During current year 2015-16 he rendered the taxable services ₹ 9,00,010 up to the end of the 30th June 2015. Explain for him registration is compulsory? If so what the last date for registration?

Answer:

Yes, Registration is required in the year 2015-16 on or before 30th July 2015.

Example 16: Mr. X is a provider of taxable service under the brand name of others. He started his business in April, 2012. Taxable turnover for the year 2015-16 is ₹ 5 lakh. Is Registration compulsory for him?

Answer:

Yes, Registration is compulsory for service provider irrespective of his turnover, if he provides service under the brand name of others. For Mr. X registration is compulsory under the Finance Act, 1994.

Example 17: Mr. D is provider of taxable services from head office located at Hyderabad and from two branch offices located at Chennai and Mumbai.

(a) Is centralized registration is permissible, if centralized billing and accounting carried out from Head Office?

(b) Who will be the competent authority to grant centralized registration?

(c) Rework (a) and (b) if his turnover is ₹ 8 lacs for the year 2015-16, but acting as input service distributor?

Answer:

(a) Yes, centralized registration is permissible

(b) DGST

(c) Registration is compulsory. Service provider should obtain multiple registrations to act as input service distributor.

Example 18: State briefly whether the following persons are liable to apply for registration under the Finance Act, 1994 and Service tax (Registration Special Category of Persons) Rules, 2005 and if so from which date:

(i) An input service distributor who starts his business with effect from 1st January, 2016.

(ii) A provider of taxable service under an unregistered brand name of another person.

In both cases aggregate value of taxable services was ₹ 6,00,000 upto 31-3-2016.

Answer:

(i) In case of input service distributors registration is compulsory without any threshold limit. Such person has to obtain the registration within 30 days from the date of commencing the business.

(ii) A Job worker or a person who renders taxable services under some other brand name, then such person is not eligible to get the exemption limit. Therefore such a job worker is liable for registration within 30 days from the date of under taking such activities.

Reverse Charge

Example 19: ABT transport providing goods transport services. 'A Ltd' sold goods from Mumbai to 'B Ltd' of Chennai. Freight charged by ABT transport for transporting said goods is ₹ 1,00,000 (exclusive of ST) as per consignment note, dated 1st July 2014. Freight paid by A Ltd on 15th September 2015.

You are required to answer:

(a) Name of provider of service and recipients of service?

(b) Who is liable to pay service tax and why?

(c) Due date of payment of service tax?

(d) Service Tax liability?

Answer :

(a) Service provider→ 'ABT' transport services.

Service recipients→ 'Both 'A Ltd' & 'B Ltd'.

(b) Either 'A Ltd' (or) 'B Ltd' being the recipients of the services. However, in the given case A Ltd is liable to pay service tax, since, freight paid by A Ltd.

(c) 6th October, 2014. In any other case 5th October, 2014.

(d) Service tax liability

	₹
Total amount of freight paid	1,00,000
Less: Abatement of 75% on the value of freight (₹ 1,00,000 x 75%)	(75,000)
Taxable Services	25,000

Service tax = ₹ 3,625 *(i.e.* ₹ 25,000 * 14.5/100)

Example 20: A Ltd. provided services valuing ₹ 8 lakhs during the financial year 2014-15. During 2015-2016, it has provided taxable services valuing ₹ 10 lakhs and has received payments towards payable services ₹ 8.5 lakhs. It has also received services in the nature of transport of goods by road on 1-4-2015, valuing ₹ 50,000 (exclusive of service tax), in respect of which it is the person liable to pay service tax. Freight has been paid on 10-6-2015. Compute the service tax, if any, payable by A Ltd. for the financial year 2015-2016. It is given that goods transport service is exempt to the extent of 75% of value thereof.

Answer :

Value of transport services received	=	₹ 50,000
Less: abatement 75% on ₹ 50,000	=	₹ 37,500
Taxable services		₹ 12,500
Service tax liability in the hands of A Ltd (2015-16)	=	₹ 1,812.50 (i.e. ₹ 12,500 x 14.5/100)

Note:

(i) The company is eligible for small service provider exemption during the financial year 2015-16, as the value of taxable services provided during financial year 2014-15 does not exceed ₹ 10 lakhs.

(ii) For the value of taxable services provided during the financial year 2015-16, no tax liability would arise, as the payments received or services provided do not exceed ₹ 10 lakhs. However, for goods transport agency services received, in respect of which M/s. A Ltd. is the person liable to pay service tax, the company cannot claim for small service provider exemption.

Interest

Example 21: Mr. X practicing Cost Accountant received ₹ 20,00,000 (exclusive of service tax)in the June 2015. He paid service tax on 26th July 2015. Gross receipt in the year 2014-15 is ₹ 25 lakhs.

You are required to calculate Interest on delay payment of service tax.

Answer :

Service tax @14.5% on ₹ 20,00,000 = ₹ 2,90,200.

Due date of payment of service tax = 6th July, 2015.

No. of days delay = 20 days

Interest = ₹ 2,383.56 (i.e. ₹ 2,90,000 × 15/100 × 20/365)

6.11 NEGATIVE LIST, EXEMPTED SERVICES & MEGA EXEMPTIONS

6.11.1 Introduction

In terms of Section 66B of the Act, service tax will be leviable on all services provided in the taxable territory by a person to another for a consideration other than the services specified in the negative list. The services specified in the negative list therefore go out of the ambit of chargeability of service tax. The negative list of service is specified in the Act itself in Section 66 D. In all, there are seventeen heads of services that have been specified in the negative list. The scope and ambit of these is explained in paras below.

Services	**Inclusion in Negative list (it means outside the scope of service tax)**	**Exclusion from Negative list (it means taxable unless exempted from service tax)**	**Remarks**
1) Services provided by Govt. or local Authority	All services provided by Govt., in terms of their sovereign right to business entities. • Grant of mining licenses • Audit of Comptroller and Auditor General, etc.	• Speed post, Express Parcel post, Life insurance and agency services carried out on payment of commission • Services in relation to vessel or an aircraft • Transport of goods and passengers • Support services.	Reverse charge applicable in case of support services Examples: Adv. Service, Construction Works contract, Renting of movable or immovable property, Security Testing and analysis.

(2)	Services provided by RESERVE BANK OF INDIA (RBI)	All type of services provided by RBI.	Services provided to RBI.	Services provided banks to RBI taxable.
(3)	Services Provided by a foreign diplomatic mission located in India	All type of services.	Nil.	Service provided to a foreign diplomatic mission located in india is exempt from service tax.
(4)	Agriculture or agricultural produce	• Cultivation, harvesting, seed testing • Supply of farm labour • Trimming, sorting etc., thereby marketable in the primary market • Renting of agro machinery loading, unloading, packing, storage and warehousing of agricultural produce • Agricultural extention services • Services by any agriculrual Produce marketing committee	• Potato Chips or Tomoto Ketchup • Grinding, sterilizing extraction of packaging in retail packs of agricultural products.	
(5)	Trading of goods	• Forward contracts in commodities • Commodity futures.	• Auxiliary services relating to future contracts or commodity futures provided by commodity exchanges, clearing houses or agents.	
(6)	Process amounting to manufacture or production of goods	• Process for which Excise duty Exempted (i.e. Non-dutiable goods). • Excisable goods for which Central Excise Duty or State Excise are leviable.	Process do not amounting to manufacture. Alcoholic liquor for human consumption are also exempted from negative list.	Exemptions: • Job work in relation to agriculture, printing or textile processing • Cut and polished diamonds, jewellery • E.D. paid by manufacturer • Job work charges Upto ₹ 150 Lacs in relation to parts of cycles or sewing machines provided P.Y. ≤ ₹ 150 Lacs.

(7) Selling of space or time slots for advertisement Except advertisement broad-cast by ratio or television	Selling of space for advertisement in print media	• Sale of space for adv. on radio or T.V. • Sale time slot by a broadcasting org.	
(8) Access to a road or a bridge on payment of toll charges	Toll charges collected to access to National Highways or State Highways.	The activity of toll collection outsourced to any third party agency who undertakes the work for consideration. **Example:** Intertoll India Consultants was under taken a sub-contract to collect toll on commission basis from Noida Toll Bridge Company (i.e. agency authorized to levy toll). Commission is subject to S.T.	
(9) Betting, gambling or lottery	Betting, gambling or lottery	• Auxiliary services used for organising/ promoting betting or gambling events • Discount earned by the lottery distributors/ agents • Service of promotion, marketing, organising etc. of lottery • Distributor or selling agent has option to pay S.T. at composition scheme as per Rule 6(7C) of Service Tax Rules, 1994.	Services by selling/ marketing agent of lottery tickets to a distributor or a selling agent were exempt from service tax. Now, this exemption has been withdrawn. These services are covered under 100% reverse charge and the distributor or selling agent of lottery would be liable to pay service tax.
(10) admission to entertainment events or access to amusement facilities — Not in Negagive List [Service Tax leviable subject to exemptions]			

(11) Transmission or distribution of electricity by an Electricity transmission or distribution utility	Services provided by • The Central Electricity Authority • A State Electricity Board • A State Transmission Utility	Charges collected by a developer or a housing society for distribution of electricity within a residential complex Installation of gensets	
	A Transmission licensee or distribution licensee under the Electricity Act,		
(12) Education services	Services by way of I. Pre-school education and education upto higher secondary school (i.e. XII standard) II. Education as a part of a curriculum for obtaining a qualification recognised by any an Indian law	• Qualifications recognised by a law of foreign country • Services provided to educational institutions • Private tuitions • Services by educational institutions for campus recruitments	
	III. Vocational education course approved by National Council for Vocational Training (NCVT) or National Skill Development Corporation (NSDC)	Exemption from S.T: • Training relating to arts, culture or sports • Auxiliary educational services	
(13) Renting of Residential dwelling for use as residence	I. Govt. Deptt. Allots houses to its employees and charges a license fee II. Flats given on rent for residential purposes	• Residential house taken on rent for commercial purposes • House is given on rent and the same is used as a hotel or a lodge • Rooms in a hotel or a lodge are let out	
(14) Banking, financial and insurance services	I. Extending deposits, loans, or advances in so far as the consideration is represented by way of interest or discount II. Foreign currency exchange amongst banks or authorized dealers	• Interest portion of leasing or hire purchase after claiming an abatement @90%. • All other services of a banker or financial and insurance services • Foreman of chit fund liable to pay service tax without any abatement.	

(15) Services relating to transportation of passengers by any mode of conveyance	**Services by** • A stage carriage • Railways in a class other than first class or AC coach • Metro, monorail or tramway • Inland waterways • Public transport (other than tourism purpose) in a vessel between places located in india and • Metered cabs or auto rickshaws	Public transport predominantly for tourism Exemption: Giving on hire of motor vehicles to State Transport, No S.T.	
(16) Services relating to transportation of goods	I. By road (except GTA and courier angency) II. By aircraft or vessel from a place outside india up to the customs station III. By inland waterways	• Goods Transport Agency (GTA) • Courier Agency	
(17) Funeral, burial, crematorium or mortuary services including transportation of the deceased.	All relevant services	—	

Chapter V of the Finance Act, 1994, is being amended vide Finance Act 2013:

(i) *Definition of 'approved vocational education course' provided in section 65B(11) is being amended: firstly the word , or, State Council of Vocational Training' (SCVT) is being inserted in (i), and secondly, entry at item serial number(iii) is being omitted, for NSDC is not an affiliating body. After the proposed amendment takes effect, a course run by an industrial training institute or an industrial training centre affiliated to the National Council for vocational training or State Council for vocational training offering courses in designated trades notified under the Apprentices Act, 1961.*

(ii) *Definition of "process amounting to manufacture or Production of goods'', in section 65B(40) being amended to include processes on which duties of excise are leviable under the Medicinal and Toilet Preparations (Excise Duties) Act, 1955, or Section 3 of Central Excise Act.*

(iii) *Maximum penalty imposable for failure to obtain registration will be ten thousand rupee only.*

(iv) *Section 78A is being introduced, to make provision for imposition of penalty on director, manager, secretary or other officer of the company, who at the time of specified contravention was in charge of and responsible for the conduct of busines of company was knowingly concerned with such contravention.*

(v) *Section 89 is being amended; (i) in the case of an offence specified in clause (a), (b) and (c) of sub section (1) where the amount exceeds fifty lakh rupees, punishment shall be for a term which may extend to three years, but shall not, in any case, be less than six months; (ii) in the case of failure to pay service tax collected, to the credit of Central Government within six months, an offence specified in section 89(1)(d), if such non-payment exceeds fifty lakh rupees, punishment shall be imprisonment for a term which may extend upto seven years but not less than six months;*

(iii) in the case of any other offence, the punishment shall be imprisonment for a term which may extend to one year.

(vi) Retrospective exemption is being extended to the Indian Railways on the service tax leviable on various taxable services provided by them during the period prior to the 1st day of July 2012, to the extend show cause notices have been issued upto the 28th day of February 2013. Section 99 is being added for this purpose, in chapter V of the Finance Act, 1994.

(vii) Rationalization of Abatement

At present taxable portion for service tax purpose is prescribed as 25% uniform for constructions where value of land is included in the amount charged from the service recipient. This is being rationalized. Accordingly, where the carpet area of residential unit is upto 2000 square feet or the amount charged is less than One Crore Rupees, in the case 'Construction of complex, building or civil structure, or a part thereof, intended for sale to a buyer, wholly or partly except where the entire consideration is received after issuance of completion certificate by the competent authority', taxable portion for service tax purpose will remain as 25%, in all other cases taxable portion for service tax purpose will be 30% . This change will come into effect from the 1st day of March, 2013.

(A) The following exemption are being rationalized:

- Rationalization of exemption limit prescribed for charitable organosations, provided service towards any other object of general public utility. So far, the limit was 25 Lakh Rupees per annum. Now, they will be covered by the threshold exemption.
- Exemption provided to restaurant other than those having (i) air-conditioning and (ii) license to serve liquor, is being rationalized; condition regarding 'license to serve liquor, is being omitted. Therefore, with effect from 1st April 2013, service tax will be leviable on taxable service provided in restaurants with air-conditioning or central air heating in any part of the establishment at any time during the year.
- Rationalization of exemption to transport of goods by road and rail/vessel.

6.11.2 Exempted Services

The need for exemptions is not obviated with the introduction of negative list. While some existing exemptions have been built into the negative list, others, wherever necessary, have been retained as exemptions. In addition some new exemptions are also introduced. For ease of reference and simplicity most of the exemptions are now a part of one single mega exemption notification 25/2012-ST dated 20/6/12. These exemptions have been explained below:

There are broadly two types of exemptions namely general exemptions and mega exemption from service tax levy.

(A) General Exemptions:

(i) Small service provider

A service provider whose previous year taxable services are less than or equal to ₹ 10 Lakhs, in the current year such service provider is called as small service provider. A person who is newly started business or office for the first time is also be called as small service provider if in the current year his taxable services does not exceeds ₹ 10 Lakhs.

The service provider should however satisfy certain conditions in order to avail the benefit of this exemption. The conditions to be noted here are as follows –

- Taxable services provided by a person under a brand name or a trade name (whether registered or not) of another person would **NOT** be eligible for this exemption
- A receiver of services who is liable to pay service tax on the services he has received by virtue of section 68(2) cannot avail the benefit of this exemption with regard to such payments. More

commonly this is relevant for recipient of GTA Services or in case of import of services where no exemption is entitled.

- Once an option is exercised in regard to this exemption during a financial year, it cannot be changed in the same financial year. [This however does not mean that the claiming of the exemption makes it compulsory to claim for the whole year. In between even without reaching ₹10 lakhs the option to pay can be made.]
- No cenvat credit can be availed on inputs or input services used in providing such output service for which exemption is being claimed.
- Cenvat credit cannot be availed on capital goods received in the premises of provider of such service during the exemption period.
- The service provider shall pay an amount equivalent to the cenvat credit taken by him in respect of inputs lying in stock or in process on the date of availment of exemption. After paying such an amount, if there is any balance of cenvat credit remaining unutilized, such balance would lapse.
- The exemption shall apply in respect of the aggregate value of all taxable services provided by the service provider (even if from more than one premises) and not individually.
- Exempted services shall be outside the purview of the exemption of this notification. In other words, the value for ascertaining the limit of ₹ 10 Lakhs would be that of taxable services alone on which service tax is payable.
- The aggregate value of such services provided in the preceding financial year should not exceed the aforesaid exemption limit.

The Small Service Provider whose turnover of all taxable services from one or more premises does not exceeds ₹ 10,00,000 during the previous year, then no service tax in the current year upto ₹ 10,00,000.

How to compute aggregate value (i.e. exemption limit) of ₹ 10,00,000: W.e.f. 1-4-2012 it has been provided that the exemption to the small service provider shall be on the basis of the value of invoice in a financial year and not on the basis of payment received in that year.

As per the amendment, Aggregate value means the sum total of value of taxable services charged in the first consecutive invoices issued or required to be issued, as the case may be, during a financial year but does not include value charged in invoices issued towards such services which are exempt from whole of service tax leviable thereon under section 66 of the Finance Act, 1994

Example 22: M/s X Pvt. Ltd is provider of taxable services namely Construction of Commercial Complexes. The taxable services in the financial year 2014-15 were ₹ 9,50,000. In the current financial year 2015-16 the following services provided and also opted the small service provider exemption.

Invoice Dt.	**Particulars**	**Value in (₹) (exclusive of service tax)**	**Abatement**	**Small Service Provider Exemption limit**	**Remarks**
10-4-2015	Construction of one shop	12,00,000	67%	Applicable for the portion of ₹ 3,96,000 (i.e. ₹ 12 lakhs x 33%)	Exemption limit of ₹ 10 lakhs applicable only for the portion of invoice which is non-exempted from service tax. Therefore, ₹ 3,96,000 exempted from service tax

	Payment received against the previous year bills (2014-15).	9,50,000	Nil	Not applicable.	Exemption to the the small service provider shall be on the basis of the value of invoice in a financial year and not on the basis of payment received in that year.
15-4-2015	Advance received (i.e. services to be provided in May 2015)	28,00,000 (includes ₹ 18 lakhs services provided in the state of Jammu & Kashmir	75%	Applicable for the portion of ₹ 2,50,000. Therefore, fully exempt from service tax	Exempted services, any how exempted from service tax. Therefore, exempted services should not be adjusted against exemption limit of ₹ 10 lakhs.
30-4-2015	Construction of super market	15,00,000	67%	Applicable for the portion of ₹ 3,54,000.	Over and above ₹ 10 lakhs of exemption limit is fully taxable @14.5%. therefore service tax is ₹ 20,445.

Exemption limit of ₹ 10,00,000 not applicable in the following cases

(a) Previous year taxable turnover of a service provider exceeds ₹ 10 Lacs.

(b) Service recipient is liable to pay service tax (i.e. Reverse Charge).

(c) Provider of services under the brand name of others.

(ii) Services provided to United Nations or an International Organization

Services provided to the agencies of the United Nations and to the employees of the United Nations, whether for official or personal purpose. Services rendered to an approved international organization, service tax is exempted.

(iii) Special Economic Zone (SEZ)

(Vide Notification No. 17/2011-ST dt. 1-3-2011, w.e.f. 1-3-2011)

Taxable services provided to a unit of SEZ or a SEZ developer by the service provider is exempted from payment of service tax, if the services are wholly consumed within SEZ. If services are not consumed wholly within SEZ, such services are taxable in the hands of service provider. However, the exemption is available by way of refund of service tax paid on the specified services received for the authorized operations in a SEZ.

Wholly consumed within SEZ

Where the *specified services* has been received and used for authorized operation by a unit of Special Economic Zones (or) SEZ developer will be exempt if the services are "*wholly consumed*" within SEZ, including services liable to tax on reverse charge basis under Section 66A of the Finance Act, 1994.

It has also been specified that all services received by an entity in a SEZ, which does not have any other Domestic Tariff Area (DTA) operations, will constitute "wholly consumed" services w.e.f. 1-3-2011. A service provider shall provide the services wholly consumed within the SEZ, without payment of service tax on obtaining from developer or the unit of SEZ for authorized operation the following documents

(a) List of taxable services for authorized operations approved by the approval committee (i.e. specified services) of the concerned SEZ.

(b) A declaration, where applicable in Form No. A-1 duly verified by the specified officer of SEZ. Since, no service tax has been paid by a unit of SEZ or SEZ developer, refund of service tax does not arise.

Meaning of Service wholly consumed within the SEZ

The concept of wholly consumed has been borrowed from the Export of Services Rules, 2005. The expression "wholly Consumed" refer to following taxable services, received by a Developer or Unit of a SEZ, for the authorized operations, namely:-

(a) Services listed in Rule 3(1) (i) of the Export of Services Rules, 2005, in relation to an immovable property situated within the SEZ; or

(b) Services listed in Rule 3(1)(ii) of the Export of Services Rules, 2005, as are wholly performed within the SEZ; or Services listed in Rule 3(1)(iii) of the Export of Services Rules, 2005, provided to a Developer or Unit of SEZ, who does not own or carry on any business other than the operations in the SEZ.

SEZ units providing taxable service to any person for consumption in Domestic Tariff Area (DTA) is subject to service tax.

***Not wholly* Consumed within SEZ**

Where the *specified services are* provided to a unit of Special Economic Zone (or) SEZ developer will be taxable in the hands of service provider, if the services are not *"wholly consumed"* within SEZ (i.e. shared between authorized operations in SEZ unit and Domestic Tariff Area (DTA) unit). However, a unit of SEZ or SEZ developer can claim refund of service tax paid on the specified services received for the authorized operations in a SEZ.

The refund shall be restricted to the extent of the ratio of export turnover to the total turnover for the given period to which the claim relates.

(iv) Exemption to the extent of R & D Cess paid

The Government has exempted the taxable services provided by a consulting engineer to any person on transfer of technology to the amount of Cess paid (i.e. 5%).

		₹
Service Tax Payable	=	XXXX
Less: 5% Cess Paid	=	(XXX)
Net Service Tax Liability	=	XXXX

Example 23: The value of service provided by a consulting engineer is ₹ 10,00,000. He has paid ₹ 50,000 as cess under section 3 of the Research and Development Cess Act, 1986. What is the amount of service tax payable by him?

Answer:

Value of taxable services = ₹ 10,00,000

Service tax @ 14.5% = ₹ 1,45,000 less cess paid ₹ 50,000, Net service tax payable = ₹ 95,000

6.11.3 Mega Exemptions:

(1) Services provided to the United Nation or a specified international organization:

Services to only specified international organisations are exempt. 'Specified international organisation' has been defined in the notification and means an international organization declared by the Central Government in pursuance of section 3 of the United Nations (Privileges and Immunities) Act, 1947 to which the provisions of the Schedule to the said Act apply.

Illustrative list of specified international organisations are as follows:

(a) International Civil Aviation Organisation

(b) World Health Organisation

(c) International Labor Organisation

(d) Food and Agriculture Organisation of the United Nations

(e) UN Educational, Scientific and Cultural Organisation (UNESCO)

(f) International Monetary Fund (IMF)

(g) International Bank for Reconstruction and Development

(h) Universal Postal Union

(i) International Telecommunication Union

(j) World Meteorological Organisation

(k) Permanent Central Opium Board

(l) International Hydrographic Bureau

(m) Commissioner for Indus Waters, Government of Pakistan and his advisers and assistants

(n) Asian African Legal Consultative Committee

(o) Commonwealth Asia Pacific Youth Development Centre, Chandigarh

(p) Delegation of Commission of European Community

(q) Customs Co-operation Council

(r) Asia Pacific Telecommunity

(s) International Centre of Public Enterprises in Developing Countries, Ljubljana (Yugoslavia)

(t) International Centre for Genetic Engineering and Biotechnology

(u) Asian Development Bank

(v) South Asian Association for Regional Co-operation

(w) International Jute Organisation, Dhaka, Bangladesh

(2) Health Care Services

Services in recognized systems of medicines in India are exempt. Health care services included:

(i) Health care services by a clinical establishment, an authorised medical practitioner or paramedics;

(ii) Services provided by way of transportation of a patient in an ambulance, other than those specified in (i) above.

In terms of the Clause (h) of section 2 of the Clinical Establishments Act, 2010, the following systems of medicines are recognized systems of medicines:

i. Allopathy

ii. Yoga

iii. Naturopathy

iv. Ayurveda

v. Homeopathy

vi. Siddha

vii. Unani

viii. Any other system of medicine that may be recognized by central government

Paramedic Services also exempted:

Services like nursing staff, physiotherapists, technicians, lab assistants etc are called as paramedic services which are exempt from service tax. Services by them in a clinical establishment would be in the capacity of employee and not provided in independent capacity and will thus be considered as services by such clinical establishment. Similar services in independent capacity are also exempted.

However, the following services even if provided by Doctors or Hospitals shall be taxable:

(a) hair transplant or

(b) cosmetic or plastic surgery, except when undertaken to restore or to reconstruct anatomy or function of body affected due to congenital defects, developmental abnormalities, injury or trauma.

(2A) Services provided by cord blood banks by way of preservation of stem cells or any other service in relation to such preservation.

(2B) Services provided by operators of the Common Bio-medical Waste Treatment Facility to a clinical establishment by way of treatment by way of treatment or disposal of bio-medical waste or the processes incidental thereto.

(3) Services by a Veterinary Clinic in relation to health care of animals or birds are exempted from service tax.

(4) Services by an entity registered under section 12AA of the Income tax Act, 1961by way of charitable activities: service provider carry out one or more of the specified charitable activities are exempted from service tax.

Following are the specified charitable activities:-

(a) public health by way of –

(I) care or counseling of (i) terminally ill persons or persons with severe physical or mental disability, (ii) persons afflicted with HIV or AIDS, or (iii) persons addicted to a dependence-forming substance such as narcotics drugs or alcohol; or

(II) public awareness of preventive health, family planning or prevention of HIV infection;

(b) advancement of religion, spirituality or yoga.

(c) advancement of educational programmes or skill development relating to,-

(i) abandoned, orphaned or homeless children;

(ii) physically or mentally abused and traumatized persons;

(iii) prisoners; or

(iv) persons over the age of 65 years residing in a rural area;

(d) preservation of environment including watershed, forests and wildlife; or

(5) Renting of religious place or conducting religious ceremony:

Services by a person by way of

(a) renting of precints of a religious place meant for general public or

(b) conduct of any religious ceremony is also exempted from service tax.

(5A) Services by a specified organization in respect of a religious pilgrimage facilitated by the Ministry of External affairs of the Government of India, under bilateral arrangement.

(6) Services by an Arbitral Tribunal and Advocates:

Services provided by-

(a) an arbitral tribunal to -

(i) any person other than a business entity; or

(ii) a business entity with a turnover up to rupees ten lakh in the preceding financial year;

(b) an individual as an advocate or a partnership firm of advocates by way of legal services to,-

(i) an advocate or partnership firm of advocates providing legal services ;

(ii) any person other than a business entity; or

(iii) a business entity with a turnover up to rupees ten lakh in the preceding financial year; or

(c) a person represented on an arbitral tribunal to an arbitral tribunal;

However, in respect of services provided to business entities, with a turnover exceeding ₹ 10 lakh in the preceding financial year, tax is required to be paid on reverse charge by the business entities. Business entity is defined in section 65B of the Finance Act, 1994 as 'any person ordinarily carrying out any activity relating to industry, commerce or any other business or profession'. Thus it includes sole proprietors as well. The business entity can, however, take input tax credit of such tax paid in terms of Cenvat Credit Rules, 2004, if otherwise eligible. The provisions relating to arbitral tribunal are also on similar lines.

(7) Exemption to clinical research organisation: [Omitted]

(8) Exemption for Recreational coaching or training:

There is exemption from service tax to training or coaching in recreational activities relating to arts, culture or sports. The benefit is available to coaching or training relating to all forms of dance, music, painting, sculpture making, theatre and sports etc.

(9) Exemption for services provided to or by an educational institution:

(a) by an educational institution to its students, faculty and staff;

(b) to an educational institution, by way of

(i) transportation of students, faculty and staff;

(ii) catering, including and mid-day meals scheme sponsored by the Government;

(iii) security or cleaning or housekeeping services performed in such educational institution;

(iv) services relating to admission to, or conduct of examination by, such institution.

(9A) Any services provided by –

(i) the National Skill Development Council set up by the Government of India.

(ii) a Sector Skill Council approved by the National Skill Development Corporation;

(iii) an assessment agency approved by the Sector Skill Council or the National Skill Development Corporation;

(iv) a training partner approved by the National Skill Development Corporation or the Sector Skill Council;

In relation to (a)the National Skill Development Programme implemented by the National Skill Development Corporation; or (b) a vocational skill development course under the National Skill

Certification and Monetary Reward Scheme; or (c) any other Scheme implemented by the National Skill Development Corporation.

(10) Services provided to recognised sports body: Services provided to a recognised sports body by-

(a) an individual as a player, referee, umpire, coach or team manager for participation in a sporting event organized by a recognized sports body;

(b) another recognised sports body; are exempted from service tax. However, services by individuals such as selectors, commentators, curators, technical experts are taxable.

Services of an individual as a player, umpire in a premier league is taxable. The service of a player to a franchisee which is not a recognized sports body is taxable.

However, services of an individual as umpire, referee when provided directly to a recognized sports body shall be exempt.

(11) Services in relation to sponsorship of sporting events organised: Services by way of sponsorship of sporting events organised,-

(a) by a national sports federation, or its affiliated federations, where the participating teams or individuals represent any district, state or zone or country;

(b) by Association of Indian Universities, Inter-University Sports Board, School Games Federation of India, All India Sports Council for the Deaf, Paralympic Committee of India or Special Olympics Bharat;

(c) by Central Civil Services Cultural and Sports Board;

(d) as part of national games, by Indian Olympic Association; or

(e) under Panchayat Yuva Kreeda Aur Khel Abhiyaan (PYKKA) Scheme; are exempted from service tax.

(12) Services provided to the Government, a local authority or a governmental authority by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration:

Exemption is available to the services by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration of:

A. Omitted.

B. a historical monument, archaeological site or remains of national importance, archaeological excavation, or antiquity specified under Ancient Monuments and Archaeological Sites and Remains Act, 1958

C. Omitted.

D. canal, dam or other irrigation works

E. pipeline, conduit or plant for (i) water supply (ii) water treatment, or (iii) sewerage treatment or disposal

F. Omitted.

(13) Services provided by way of construction, erection, commissioning, etc, :

Services provided by way of construction, erection, commissioning, installation, completion, fitting out, repair, maintenance, renovation, or alteration of,-

(a) A road, bridge, tunnel, or terminal for road transportation for use by general public;

(b) a civil structure or any other original works pertaining to a scheme under Jawaharlal Nehru National Urban Renewal Mission or Rajiv Awaas Yojana;

(c) a building owned by an entity registered under section 12 AA of the Income tax Act, 1961(43 of 1961) and meant predominantly for religious use by general public;

(d) a pollution control or effluent treatment plant, except located as a part of a factory; or

(e) a structure meant for funeral, burial or cremation of deceased are exempted from service tax.

(14) Services by way of construction, errection, commissioning or installation of original works:

Services by way of construction, erection, commissioning, or installation of original works are exempted if these services pertaining to,-

(a) railways, including monorail or metro;

(b) a single residential unit otherwise than as a part of a residential complex;

(c) low- cost houses up to a carpet area of 60 square meters per house in a housing project approved by competent authority empowered under the 'Scheme of Affordable Housing in Partnership' framed by the Ministry of Housing and Urban Poverty Alleviation, Government of India;

(d) post- harvest storage infrastructure for agricultural produce including a cold storages for such purposes; or

(e) mechanised food grain handling system, machinery or equipment for units processing agricultural produce as food stuff excluding alcoholic beverages;

(15) Services in relation to temporary transfer or permitting the use or enjoyment of a copyright :

Temporary transfer of a copyright relating to original literary, dramatic, musical, artistic work or cinematographic film (restricted to exhibition of cinematography films in a cinema hall or a cinema theatres) falling under clause (a) or (b) of sub-section (1) of section 13 of the Indian Copyright Act, 1957 is exempt.

Example 24: Mr. X a composer of a song having the copyright for his song. When he allow the recording of the song on payment of some royalty by a music company for further distribution, if so Mr. X is required to pay service tax on the royalty amount received from a music company?

Answer:

No, as the copyright relating to original work of composing song falls under clause (a) of subsection (1) of section 13 of the Indian Copyright Act, 1957 which is exempt from service tax.

Similarly an author having copy right of a book written by him would not be required to pay service tax on royalty amount received from the publisher for publishing the book. A person having the copyright of a cinematographic film would also not be required to pay service tax on the amount received from the film exhibitors for exhibiting the cinematographic film in cinema theatres.

(16) Services by artist in relation to folk or classical art

The following services are exempted from service tax if provided by a performing artist in folk or classical art forms of (i) music, or (ii) dance, or (iii) theatre, excluding services provided by such artist as a brand ambassador; and if the consideration charged for such performance is not more than ₹ one lakh.

The activities by a performing artist in folk or classical art forms of music, dance, or theatre are not subjected to service tax. All other activities by an artist in other art forms e.g. western music or dance, modern theatres, performance of actors in films or television serials would be taxable. Similarly activities of artists in still art forms e.g. painting, sculpture making etc. are taxable.

(17) Services in relation to collecting or providing of News

Services by way of collecting or providing news by an independent journalist, Press Trust of India or United News of India; are exempted from service tax.

(18) Services by a hotel, inn, guest house, club or campsite etc.

Services by a hotel, inn, guest house, club or campsite, by whatever name called, for residential or lodging purposes, having declared tariff of a unit of accommodation below one thousand rupee per day or equivalent.

Declared tariff is includes charges for all amenities provided in the unit of accommodation like furniture, air-conditioner, refrigerators or any other amenities, but without excluding any discount offered on the published charges for such unit. Its relevance is in determining the liability to pay service tax of a hotel, inn, guest house, club, campsite or other commercial places meant for residential or lodging purposes as exemption is available where declared tariff of a unit of accommodation is below rupees one thousand per day or equivalent. However, the tax will be liable to be paid on the amount actually charged i.e. declared tariff minus any discount offered.

Thus if the declared tariff is ₹ 1,200, but actual room rent charged is ₹ 900, tax will be required to be paid on ₹ 900.

When the declared tariff is revised as per the tourist season, the liability to pay tax shall be only on the declared tariff for the accommodation where the published/printed tariff is above Rupees 1000/-. However, the revision in tariff should be made uniformly applicable to all customers and declared when such change takes place.

(19) Services provided by Restaurant

Services provided in relation to serving of food or beverages by a restaurant, eating joint or a mess, other than those having (i) the facility of air-conditioning or central air-heating in any part of the establishment, at any time during the year, are exempted from service tax.

(19A) Services provided in relation to serving of food or beverages by a canteen maintained in a factory covered under the Factories Act, 1948 having the facility of air-conditioning or central air-heating at any time during the year.

(20) Exemption for transportation of certain goods, by rail or a vessel:

Services by way of transportation by rail or a vessel from one place in India to another of the following goods are exempted from service tax; -

(b) relief materials meant for victims of natural or man-made disasters, calamities, accidents or mishap

(c) defence or military equipments;

(f) newspaper or magazines registered with the Registrar of Newspapers;

(g) railway equipments or materials;

(h) agricultural produce;

(i) milk, salt and food grain including flours, pulses and rice;

(j) chemical fertilizer, organic manure and oil cakes; or

(k) cotton, ginned or baled.

(21) Services by transport of essential goods etc by Goods Transport Agency (GTA) & Rail/vessel: Services provided by a goods transport agency by way of transportation of -

(a) Agriculture produce;

(b) goods where gross amount charged for the transportation of goods on a consignment transported in a single goods carriage does not exceed one thousand five hundred rupees; or

(c) goods, where gross amount charged for transportation of all such goods for a single consignee does not exceed rupees seven hundred fifty;

(d) Milk, salt, food grain including flours, pulses and rice;

(e) Chemical fertilizer, organic manure and oil cakes;

(f) Newspaper or magazines registered with the registrar of newspapers;

(g) Relief materials meant for victims of natural or man-made disasters, calamities, accidents or mishap; or

(h) Defense or military equipments:

(i) cotton, ginned or baled

(22) Services by hiring of vehicle: Services by way of giving on hire -

(a) to a state transport undertaking, a motor vehicle meant to carry more than twelve passengers; or

(b) to a goods transport agency, a means of transportation of goods;

Giving on hire a bus to a state transport undertaking is exempt from service tax. If the bus is given on hire to a person other than a state transport undertaking, it will be taxed.

Transport of passengers in a contract carriage for the transportation of passengers, for tourism, conducted tour, charter or hire is taxable.

(23) Services of transport of passengers by different mode of transportation: Transport of passengers, with or without accompanied belongings, by -

(a) air, embarking from or terminating in an airport located in the state of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Sikkim, or Tripura or at Bagdogra located in West Bengal;

(b) non-air conditioned contract carriage other than radio taxi for transportation of passengers, excluding tourism, conducted tour, charter or hire; or

(c) ropeway, cable car or aerial tramway; are exempted from service tax.

(25) Specified services to Government, a local authority or a governmental authority: Services provided to Government, a local authority or a governmental authority by way of -

(a) water supply, public health, sanitation conservancy, solid waste management or slum improvement and upgradation; or

(b) repair or maintenance of a vessel.

(26) Services of General insurance Business under the specified scheme:

Services of general insurance business provided under following schemes are exempted from service tax:

(a) Hut Insurance Scheme;

(b) Cattle Insurance under Swarnajaynti Gram Swarozgar Yojna (earlier known as Integrated Rural Development Programme);

(c) Scheme for Insurance of Tribals;

(d) Janata Personal Accident Policy and Gramin Accident Policy;

(e) Group Personal Accident Policy for Self-Employed Women;

(f) Agricultural Pumpset and Failed Well Insurance;

(g) premia collected on export credit insurance;

(h) Weather Based Crop Insurance Scheme or the Modified National Agricultural Insurance Scheme approved by the Government of India and implemented by the Ministry of Agriculture;

(i) Jan Arogya Bima Policy;

(j) National Agricultural Insurance Scheme (Rashtriya Krishi Bima Yojana);

(k) Pilot Scheme on Seed Crop Insurance;

(l) Central Sector Scheme on Cattle Insurance;

(m) Universal Health Insurance Scheme;

(n) Rashtriya Swasthya Bima Yojana; or

(o) Coconut Palm Insurance Scheme;

(p) Pradhan Mantri Suraksha Bima Yojana.

(26A) Service of Life Insurance business provided under following schemes:

(a) Janashree Bima Yojana (JBY); or

(b) Aam Aadmi Bima Yojana (AABY).

(c) life micro-insurance product as approved by the Insurance Regulatory and Development Authority, having maximum amount of cover of fifty thousand rupees.

(d) Varishtha Pension Bima Yojana

(e) Pradhan Mantri Jeevan Jyoti Bima Yojana

(f) Pradhan Mantri Jan Dhan Yojana.

(27) Services provided by an incubatee:

Services provided by an incubatee up to a total turnover of fifty lakh rupees in a financial year subject to the following conditions, namely:-

(a) the total turnover had not exceeded fifty lakh rupees during the preceding financial year;and

(b) a period of three years has not been elapsed from the date of entering into an agreement as an incubatee;

(28) Services by an Non-Profit Making Organisation/unincorporated body :

Service by an unincorporated body or a non- profit entity registered under any law for the time being in force, to its own members by way of reimbursement of charges or share of contribution -

(a) as a trade union;

(b) for the provision of carrying out any activity which is exempt from the levy of service tax; or

(c) up to an amount of five thousand rupees per month per member for sourcing of goods or services from a third person for the common use of its members in a housing society or a residential complex;

Where Residential Welfare Association (RWA) is working as a pure agent of its members for sourcing of goods or services from a third person, amount collected by RWA from its members may be excluded from the value of taxable service in terms of Rule 5(2) 0f Service Tax (Determination of Value) Rules, 2006 subject to compliance with the specified conditions.

(29) Services by the specified persons in respective categories are exempted from service tax:

Services by the following persons in respective capacities -

(a) sub-broker or an authorised person to a stock broker;

(b) authorised person to a member of a commodity exchange;

(f) selling agent or a distributer of SIM cards or recharge coupon vouchers;

(g) business facilitator or a business correspondent to a banking company with respect to a Basic Savings Bank Deposit Account covered by Pradhan Mantri Jan Dhan Yojana in the banking company's rural area branch, by way of account opening, cash deposits, cash withdrawals, obtaining e-life certificate, Aadhar seeding;

(ga) any person as an intermediary to a business facilitator or a business correspondent with respect to services mentioned in (d) above;

(gb) business facilitator or a business correspondent to an insurance company in a rural area; or

(h) sub-contractor providing services by way of works contract to another contractor providing works contract services which are exempt;

(30) Services by way of job work:

Carrying out an intermediate production process as job work exempted from service tax if these services are in relation to -

(a) agriculture, printing or textile processing;

(b) cut and polished diamonds and gemstones; or plain and studded jewellery of gold and other precious metals, falling under Chapter 71 of the Central Excise Tariff Act ,1 985 (5 of 1986);

(c) any goods excluding alcoholic liquors for human consumption on which appropriate duty is payable by the principal manufacturer; or

(d) processes of electroplating, zinc plating, anodizing, heat treatment, powder coating, painting including spray painting or auto black, during the course of manufacture of parts of cycles or sewing machines upto an aggregate value of taxable service of the specified processes of one hundred and fifty lakh rupees in a financial year subject to the condition that such aggregate value had not exceeded one hundred and fifty lakh rupees during the preceding financial year;

(31) Services in relation to business exhibition:

Services by an organiser to any person in respect of a business exhibition held outside India are exempted from service tax.

(32) Services by making telephone calls:

[Omitted w.e.f. 01.04.2015]

(33) Services by way of slaughtering of animals;

(34) Services by a person located in non-taxable territory:

Services received from a provider of service located in a non- taxable territory by-

(a) Government, a local authority, a governmental authority or an individual in relation to any purpose other than commerce, industry or any other business or profession;

(b) an entity registered under section 12AA of the Income tax Act, 1961 (43 of 1961) for the purposes of providing charitable activities; or

(c) a person located in a non-taxable territory;

(35) Services by public libraries:

Services of public libraries by way of lending of books, publications or any other knowledge-enhancing content or material; are exempted from service tax.

(36) Services by Employee's State Insurance (ESI) Corporation:

Services by Employees' State Insurance Corporation to persons governed under the Employees' Insurance Act, 1948 (34 of 1948) are exempted from service tax.

(37) Services by way of transfer of a going concern:

Services by way of transfer of a going concern, as a whole or an independent part thereof; exempted from service tax. Predominant transfer of activity comprising service is not covered under exemption.

(38) Services by way of public convenience:

Services by way of public conveniences such as provision of facilities of bathroom, washrooms, lavatories, urinal or toilets; are exempted from service tax.

(39) Services by a governmental authority:

Services by a governmental authority by way of any activity in relation to any function entrusted to a municipality under article 243 W of the Constitution exempted from service tax.

(40) Services by way of loading, unloading, packing, storage or warehousing of rice, cotton, ginned or baled.

(41) Services received by the Reserve Bank of India, from outside India in relation to management of foreign exchange reserves.

(42) Services provided by a tour operator to a foreign tourist in relation to a tour conducted wholly outside India.

(43) Services by operator of Common Effluent Treatment Plant by way of treatment of effluent;

(44) Services by way of pre-conditioning, pre-cooling, ripening, waxing, retail packing, labelling of fruits and vegetables which do not change or alter the essential characteristics of the said fruits or vegetables;

(45) Services by way of admission to a museum, national park, wildlife sanctuary, tiger reserve or zoo;

(46) Service provided by way of exhibition of movie by an exhibitor to the distributor or an association of persons consisting of the exhibitor as one of its members;

(47) Services by way of right to admission to,-

(i) exhibition of cinematographic film, circus, dance, or theatrical performance including drama or ballet;

(ii) recognised sporting event;

(iii) award function, concert, pageant, musical performance or any sporting event other than a recognised sporting event, where the consideration for admission is not more than ₹ 500 per person.

The following definitions are useful to understand the various terms used in the above:

(a) "Advocate" has the meaning assigned to it in clause (a) of sub-section (1) of section 2 of the Advocates Act, 1961 (25 of 1961);

(b) "appropriate duty" means duty payable on manufacture or production under a Central Act or a State Act, but shall not include 'Nil' rate of duty or duty wholly exempt;

(c) "arbitral tribunal" has the meaning assigned to it in clause (d) of section 2 of the Arbitration and Conciliation Act, 1996 (26 of 1996);

(d) "authorised medical practitioner" means a medical practitioner registered with any of the councils of the recognised system of medicines established or recognized by law in India and includes a medical professional having the requisite qualification to practice in any recognised system of medicines in India as per any law for the time being in force;

(e) “authorised person” means any person who is appointed as such either by a stock broker (including trading member) or by a member of a commodity exchange and who provides access to trading platform of a stock exchange or a commodity exchange as an agent of such stock broker or member of a commodity exchange;

(f) [Omitted]

(g) “banking company” has the meaning assigned to it in clause (a) of section 45A of the Reserve Bank of India Act,1 934(2 of 1934);

(h) “brand ambassador” means a person engaged for promotion or marketing of a brand of goods, service, property or actionable claim, event or endorsement of name, including a trade name, logo or house mark of any person;

(i) “business facilitator or business correspondent” means an intermediary appointed under the business facilitator model or the business correspondent model by a banking company or an insurance company under the guidelines issued by Reserve Bank of India;

(j) “clinical establishment” means a hospital, nursing home, clinic, sanatorium or any other institution by, whatever name called, that offers services or facilities requiring diagnosis or treatment or care for illness, injury, deformity, abnormality or pregnancy in any recognised system of medicines in India, or a place established as an independent entity or a part of an establishment to carry out diagnostic or investigative services of diseases;

(k) “charitable activities” means activities relating to –

  (i) public health by way of -

    (a) care or counseling of (i) terminally ill persons or persons with severe physical or mental disability, (ii) persons afflicted with HIV or AIDS, or (iii) persons addicted to a dependence-forming substance such as narcotics drugs or alcohol; or

    (b) public awareness of preventive health, family planning or prevention of HIV infection;

  (ii) advancement of religion or spirituality;

  (iii) advancement of educational programmes or skill development relating to,-

    (a) abandoned, orphaned or homeless children;

    (b) physically or mentally abused and traumatized persons;

    (c) prisoners; or

    (d) persons over the age of 65 years residing in a rural area;

  (iv) preservation of environment including watershed, forests and wildlife; or

(l) “commodity exchange” means an association as defined in section 2 (j) and recognized under section 6 of the Forward Contracts (Regulation) Act,1 952 (74 of 1952);

(m) “contract carriage” has the meaning assigned to it in clause (7) of section 2 of the Motor Vehicles Act, 1988 (59 of 1988);

(n) ”declared tariff” includes charges for all amenities provided in the unit of accommodation (given on rent for stay) like furniture, air-conditioner, refrigerators or any other amenities, but without excluding any discount offered on the published charges for such unit;

(o) “distributor or selling agent” has the meaning assigned to them in clause (c) of the rule 2 of the Lottery (Regulation) Rules, 2010 notified by the Government of India in the Ministry of Home Affairs, published in the Gazette of India, Extraordinary, Part-II, Section 3, Sub-section (i), vide number G.S.R. 278(E), dated the 1st April, 2010 and shall include distributor or selling agent authorised by the lottery- organising State;

(oa) "educational Institutional" means an institution providing services specified in clause (l) of section 66D of the Finance Act, 1994.

(p) "general insurance business" has the meaning assigned to it in clause (g) of section 3 of General Insurance Business (Nationalisation) Act, 1972 (57 of 1972);

(q) "general public" means the body of people at large sufficiently defined by some common quality of public or impersonal nature;

(r) "goods carriage" has the meaning assigned to it in clause (14) of section 2 of the Motor Vehicles Act, 1988 (59 of 1988);

(s) "Government authority" means an authority or a board or any other body:

(i) set up by an Act of Parliament or a State Legislature; or

(ii) established by Government

with 90% or more participation by way of equity or control, to carry out any function entrusted to a municipality under article 243W of the Constitution.

(t) "health care services" means any service by way of diagnosis or treatment or care for illness, injury, deformity, abnormality or pregnancy in any recognised system of medicines in India and includes services by way of transportation of the patient to and from a clinical establishment, but does not include hair transplant or cosmetic or plastic surgery, except when undertaken to restore or to reconstruct anatomy or functions of body affected due to congenital defects, developmental abnormalities, injury or trauma;

(u) "incubatee" means an entrepreneur located within the premises of a Technology Business Incubator (TBI) or Science and Technology Entrepreneurship Park (STEP) recognised by the National Science and Technology Entrepreneurship Development Board (NSTEDB) of the Department of Science and Technology, Government of India and who has entered into an agreement with the TBI or the STEP to enable himself to develop and produce hi-tech and innovative products;

(v) "insurance company" means a company carrying on life insurance business or general insurance business;

(w) "legal service" means any service provided in relation to advice, consultancy or assistance 230 I in any branch of law, in any manner and includes representational services before any court, tribunal or authority;

(x) "life insurance business" has the meaning assigned to it in clause (11) of section 2 of the Insurance Act, 1938 (4 of 1938);

(xa) "life micro-insurance product" shall have the meaning assigned to it in clause (e) of regulation 2 of the Insurance Regulatory and Development Authority (Micro-insurance) Regulations, 2005.

(xaa) 'national park' has the meaning assigned to it in the clause (21) of the section 2 of The Wild Life (Protection) Act, 1972 (53 of 1972);

(y) "original works" means has the meaning assigned to it in Rule 2A of the Service Tax (Determination of Value) Rules, 2006;

(z) "principal manufacturer" means any person who gets goods manufactured or processed on his account from another person;

(za) "radio taxi" means a taxi including a radio cab, by whatever name called, which is in two-way radio communication with a central control office and is enable for tracking using Global Positioning System (GPS) or General Packet Radio Service (GPRS).

(zaa) "recognized sports body" means - (i) the Indian Olympic Association, (ii) Sports Authority of India, (iii) a national sports federation recognized by the Ministry of Sports and Youth Affairs of the Central Government, and its affiliate federations, (iv) national sports promotion organisations recognized by the Ministry of Sports and Youth Affairs of the Central Government, (v) the International Olympic Association or a federation recognized by the International Olympic Association or (vi) a federation or a body which regulates a sport at international level and its affiliated federations or bodies regulating a sport in India;

(zab) "recognised sporting event" means any sporting event,-

(i) organised by a recognised sports body where the participating team or individual represent any district, state, zone or country; (ii) covered under entry 11

(zb) "religious place" means a place which is primarily meant for conduct of prayers or worship pertaining to a religion, meditation, or spirituality;

(zc) "residential complex" means any complex comprising of a building or buildings, having more than one single residential unit;

(zd) "rural area" means the area comprised in a village as defined in land revenue records, excluding the area under any municipal committee, municipal corporation, town area committee, cantonment board or notified area committee; or any area that may be notified as an urban area by the Central Government or a State Government;

(ze) "single residential unit" means a self-contained residential unit which is designed for use, wholly or principally, for residential purposes for one family;

(zf) "specified international organization" means an international organization declared by the Central Government in pursuance of section 3 of the United Nations (Privileges and Immunities) Act, 1947 (46 of 1947), to which the provisions of the Schedule to the said Act apply;

(zfa) "specified organization" shall mean –

(a) Kumaon Mandal Vikas Nigam Limited, a Government of Uttarakhand Undertaking; or

(b) 'Committee' or 'State Committee' as defined in section 2 of the Haj Committee Act, 2002.

(zg) "state transport undertaking" has the meaning assigned to it in clause (42) of section 2 of the Motor Vehicles Act, 1988 (59 of 1988);

(zh) "sub-broker" has the meaning assigned to it in sub-clause (gc) of clause 2 of the Securities and Exchange Board of India (Stock Brokers and Sub-brokers) Regulations, 1992;

(zi) "tiger reserve" has the meaning assigned to it in clause (e) of section 38K of the Wild Life (Protection) Act, 1972 (53 of 1972);

(zj) "trade union" has the meaning assigned to it in clause (h) of section 2 of the Trade Unions Act, 1926 (16 of 1926).

(zk) "wildlife sanctuary" means sanctuary as defined in the clause (26) of the section 2 of The Wild Life (Protection) Act, 1972 (53 of 1972);

(zl) "zoo" has the meaning assigned to it in the clause (39) of the section 2 of the Wild Life (Protection) Act, 1972 (53 of 1972).

6.11.4 Abatement Notification – Notification No. 26/2012

TABLE

Sl No.	Description of taxable service	Percentage taxable sevice payable	Conditions
(1)	(2)	(3)	(4)
1	Services in relation to financial leasing including hire purchase	10	*Nil*
2	Transport of goods by rail	30	70% abatement is allowed, if Cenvat credit on — • inputs, capital goods and input services, • used for providing the taxable service, has not been taken under the Cenvat Credit Rules, 2004
3	Transport of passengers, with or without accompanied belongings by rail	30	70% abatement is allowed, if Cenvat credit on — • inputs, capital goods and input services, • used for providing the taxable service, has not been taken under the Cenvat Credit Rules, 2004
4	Bundled service by way of supply of food or any other article of human consumption or any drink, in a premises (including hotel, convention center, club, pandal, shamiana or any other place, specially arranged for organizing a function) together with renting of such premises	70	(i) CENVAT credit on any goods classifiable under Chapters 1 to 22 of the Central Excise Tariff Act, 1985 used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004.
5	Transport of passengers by air, with or without accompanied belongings (i) Economy class (ii) Other than economy class	 40 60	CENVAT credit on inputs and capital goods, used for providing the taxable service, has not been taken under the provisions ot the CENVAT Credit Rules, 2004.
6	Renting of hotels, inns, guest houses, clubs, campsites or other commercial places meant for residential or lodging purposes.	60	Same as above.
7	Services of goods transport agency in relation to transportation of goods.	30	CENVAT credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken by the service provider under the provisions of the CENVAT Credit Rules, 2004.
8	Services provided in relation to chit [withdrawn]		

Sl No.	Description of taxable service	Percentage taxable sevice payable	Conditions
(1)	(2)	(3)	(4)
9	Renting of motor-cab	40	(i) CENVAT credit on inputs and capital goods, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004; (ii) CENVAT credit on input service of renting of motor-cab has been taken under the provisions of the CENVAT Credit Rules, 2004, in the following manner: (a) Full CENVAT credit of such input service received from a person who is paying service tax on forty per cent of the value; or (b) Up to forty per cent CENVAT credit of such input service received from a person who is paying service tax on full value; (iii) CENVAT credit on input services other than those specified in (ii) above, has not been taken under the provisions of the CENVAT Credit Rules, 2004.
9A	Transport of passengers, with or without accompanied, belongings, by a contract carriage other than motor-cab. ***With effect from a date to be notified following Serial No. 9A shall be substituted for the existing Serial No. 9A** **9A.** Transport of passengers, with or without accompanied belongings, by— (a) a contract carriage other than motor-cab. (b) a radio taxi.	40	CENVAT credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004.
10	Transport of goods in a vessel	30	CENVAT credit on inputs, capital goods and input services, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004.
11	Services by a tour operator in relation to,- (i) a package tour	25	(i) CENVAT credit on inputs, capital goods and input services other than the input service of a tour operator, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004. (ii) The bill issued for this purpose indicates that it is inclusive of charges for such a tour.

Sl No.	Description of taxable service	Percentage taxable sevice payable	Conditions
(1)	(2)	(3)	(4)
	(ii) a tour, if the tour operator is providing services solely of arranging or booking accommodation for any person in relation to a tour.	10	(i) CENVAT credit on inputs, capital goods and input services other than the input service of a tour operator, used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004. (ii) The invoice, bill or challan issued indicates that it is towards the charges for such accommodation. (iii) This exemption shall not apply in such cases where the invoice, bill or challan issued by the tour operator, in relation to a tour, only includes the service charges for arranging or booking accommodation for any person and does not include the cost of such accommodation.
	(iii) any services other than specified at (i)and (ii) above.	40	(i) CENVAT credit on inputs, capital goods and input services '[other than the input service of a tour operator], used for providing the taxable service, has not been taken under the provisions of the CENVAT Credit Rules, 2004. (ii) The bill issued indicates that the amount charged in the bill is the gross amount charged for such a tour.
12.	Construction of a complex, building, civil structure or a part thereof, intended for a sale to a buyer, wholly or partly, except where entire consideration is received after issuance of completion certificate by the competent authority,— (a) for a residential unit satisfying both the following conditions, namely:- (i) the carpet area of the unit is less than 2000 square feet; and (ii) the amount charged for the unit is less than rupees one crore; (b) for other than the (a) above.	25 30	(i) CENVAT credit on inputs used for providing the taxable service has not been taken under the provisions of the CENVAT Credit Rules, 2004; (ii) The value of land is included in the amount charged from the service receiver.

6.12 POINT OF TAXATION

Introduction

We must thoroughly understand terms "Point of Taxation", "taxable event" and "value of taxable services" for the following reasons:

i. The amount of service tax is based on the Point of Taxation.

ii. Service tax is payable on the basis of provision of service instead of realization of value of taxable service except in the case of individuals/firms/limited liability partnership firms (LLP's) w.e.f. 1-4-201 2.

iii. If money is received in advance, ahead of completion or rendering of service, service tax is payable as soon as the advance is received.

The point of taxation defines the point in time when a service shall be deemed to have been provided. It has impact on determination of rate of tax, as normally the rate of tax shall apply as prevailing on the date when service shall be deemed to have been provided.

The Government of India has introduced the Point of Taxation Rules, 2011 to remove the disputes about applicability of the rate of tax and for ascertainment of the Point of Taxation. These rules have been explained with the help of examples are as follows:

Rule 1: These rules shall be called the Point of Taxation Rules, 2011

Rule 2: Definitions

Rule 2(a) "Act" means the Finance Act, 1 994;Rule 2(b) **"associated enterprises"** shall have the meaning assigned to it in section 92A of the Income Tax Act, 1961;

Rule 2(ba) **"change in effective rate of tax"** shall include a change in the portion of value on which tax is payable in terms of a notification issued in the Official Gazette under the provisions of the Act, or rules made there under (w.e.f. 1.4.201 2).

Rule 2(c) "**continuous supply of service"** means any service which is provided, or to be provided continuously or on recurrent basis, under a contract, for a period ***exceeding three*** months with the obligation for payment periodically or from time to time or where the Central Govt. by notification in the Official Gazette, prescribes provision of a particular service to be a continuous supply of service, whether or not subject to any condition.

Rule 2(d) **"invoice"** means the invoice referred to in rule 4A of the Service Tax Rules, 1994 and shall include any document as referred to in the said rule;

Rule 2(e) **"point of taxation"** means the point in time when a service shall be deemed to have been provided;

Rule 2(f) "taxable service" (omitted w.e.f. 1-7-201 2)

Rule 2A: "Date of payment" as given in Point of Taxation Rules, 2011

According to Rule 2A of the Point of taxation Rules, 2011, the date of payment shall be the earlier of the following dates,-

(i) Date when the payment is entered in the books of accounts (i.e. payment accounted for in books); or

(ii) Date on which the same is credited in the bank account of the person liable to pay tax (i.e. actually received in hank of the person)

In case of new levy or change in effective rate of tax: During the intermittent period when the payment is accounted for and the same is actually received in the bank, if there is change in the,-

- effective rate of tax; or
- service is taxed for the first time (i.e. new levy),

then,-

Date of payment shall be the date of credit in the bank account, if following conditions are fulfilled,-

(a) the credit in the bank account is after **4 working days from the date where there is change in the effective rate of tax or service** is taxed for the first time; and

(b) the payment is made by way of an instrument which is credited to a bank account,

If any rule requires determination of the time or date of payment received, the expression 'date of payment' shall be construed to mean such date on which payment is received. **[Inserted w.e.f. 1-4-2012]**

Example 26: The invoice of ₹20,00,000 is issued for services on 01-06-2015. A cheque for the same is received and accounted for in the books on 15-06-2015. The amount on the cheque was credited in the bank on 06-07-2015. Meanwhile, on 01-07-2015, the aforesaid service was brought in the ambit of taxable service. What will be the date of payment?

Answer:

Here, as the new levy is introduced on 01-07-2015 (i.e during the intermittent period when the payment was accounted for in the books and the same was actually received in the bank), the credit in the bank account is after 4 working days from the date of the new levy [i.e after (01-07-2015 + 4 working days)], therefore, the date of credit in the bank account shall be taken as the date of payment. Thus, the date of payment, here, will be 06-07-2015.

Rule 3: Determination of point of taxation:

(a) Date of invoice or payment, whichever is earlier, if the invoice is issued within the prescribed period of 30 days from the date of completion of the provision of service (w.e.f. 1-4-2012).

(b) Date of completion of the provision of service or payment, whichever is earlier if the invoice is not issued within the prescribed period as state in rule 4A of the Service Tax Rules, 1994.

w.e.f. 1-4-2012, in case of continuous supply of service where the provision of the whole or part of the service is determined periodically on the completion of an event in terms of a contract, which requires the receiver of service to make any payment to service provider, the date of completion of each such event as specified in the contract shall be deemed to be the date of completion of provision of service.

Example 27: In the case of construction services if the payments are linked to stage-by-stage completion of construction, the provision of service shall be deemed to be completed in part when each stage of construction is completed.

Wherever the provider of taxable service receives a payment up to ₹ 1,000 in excess of the amount indicated in the invoice, the point of taxation to the extent of such excess amount, at the option of the provider of taxable service, shall be the date of receipt of such amount.

Example 28: M/s X Pvt. Ltd. provided services for ₹ 1,00,000 and service tax charged separately @14.5% vide invoice dated 1-4-2015. Payment received ₹ 1,15,400 on 1st July 2015. It means excess payment received is ₹ 900. Hence, no need to issue separate invoice for the same. Hence, the point of taxation for the invoice value is 1-4-2015, whereas for ₹ 900 the point of taxation is 1st July 2015.

POT = Point of Taxation

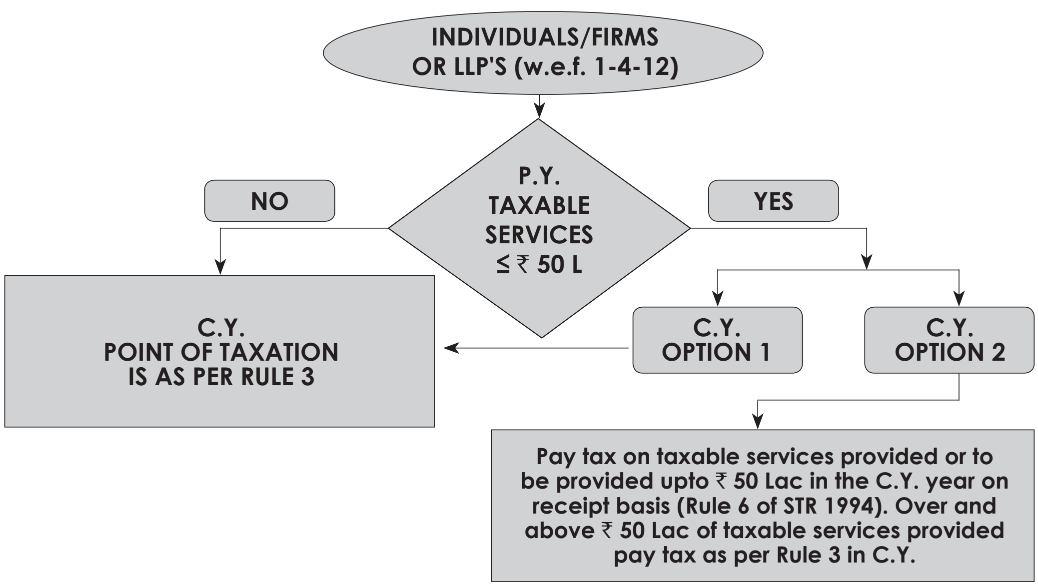
Example 29: The applicability of the rule will be clear from the following table:

M/s X Pvt. Ltd. is provider of service.

SL. No.	Date of completion of service	Date of invoice	Date on which payment recd.	Point of Taxation	Due date of payment	Remarks
1.	April 10, 2015	April 20, 2015	June 30, 2015	April 20, 2015	6th May 2015	Invoice issued in 30 days from the date of completion of service. Dt. of invoice or Dt. of payment whichever is earlier
2.	April 10, 2015	May 26, 2015	June 30, 2015	April 10, 2015	6th May 2015	Invoice not issued within 30 days and payment received after completion of service
3.	May 10, 2015	May 20, 2015	April 15, 2015	April 15, 2015	6th May 2015	Invoice issued in 30 days but payment received before invoice
4.	April 10, 2015	May 26, 2015	April 5, 2015 (part) and May 25, 2015 (remaining)	April 5, 2015 And April 10, 2015 for respective amounts	6th May 2015	Invoice not issued in 30 days. Part payment before completion, remaining later

Service Tax liability on receipt basis for Individuals and Partnership Firms including LLP's (w.e.f. 1-4-2012)

It is pertinent to note point of taxation in case of individuals and partnership firms whose aggregate value of taxable services provided from one or more premises is ₹ 50 lakhs or less in the previous financial year, the service provider shall have the option to pay tax on taxable services provided or to be provided by him up to a total of ₹ 50 lakhs in the current financial year, by the dates specified in the Rule 6 of Service Tax Rules, 1994, with respect to the relevant quarter, in which payment is received.



P.Y = Previous Year, C.Y= Current Year.

Example 30: Mr. C, Practicing C.A. started profession in the year 2015-16 has been chosen the option to pay service tax on receipt basis in the current year.

(₹ in lakhs)

Particulars	1st qtr.	2nd qtr.
services provided	20	2
services to be provided (i.e. advance)	35	NIL
TOTAL	55	2
S.T. @14.5% Note: small service provider exemption not availed	5.08	0.29

Note:

Services provided or to be provided exceeds ₹ 50 lakhs in the 1st quarter itself. Entire value of ₹ 35 lakhs is taxable on receipt basis as per point of taxation rule 3.

Services provided in the 1st quarter for ₹ 20 lakhs will be taxable on receipt basis.

Service provided or to be provided in the 2nd quarter fully taxable as per Point of Taxation Rule 3.

Example 31: Mr. C, Practicing C.A. started profession in the year 2015-16 has been chosen the option to pay service tax on receipt basis in the current year.

(₹ in lakhs)

Particulars	1st qtr.	2nd qtr.
services provided	55	2
services to be provided (i.e. advance)	NIL	NIL
TOTAL	55	2
S.T. @14.5%	7.98	0.29

Note 1:

(i) small service provider exemption not availed

(ii) Since, ₹ 50 lakhs exceeds in the 1st quarter, services provided over and above ₹ 50 lakhs is taxable as per point of taxation rule 3.

Service tax is payable on ₹ 5 lakhs on provisional basis and balance ₹ 50 lakhs will be taxable on receipt basis.

From 2nd quarter onwards services are taxable based on point of taxation rule 3

Example 32: Mr. C, Practicing C.A. started profession in the year 2015-16 has been chosen the option to pay service tax on receipt basis in the current year.

(₹ in lakhs)

Particulars	1st qtr.	2nd qtr.
services provided	NIL	2
services to be provided (i.e. advance)	55	NIL
TOTAL	55	2
S.T. @14.5%	7.98	0.29

Note:

(i) small service provider exemption not availed

(ii) Since, in the 1st quarter services to be provided for which advance received exceeds ₹ 50 lakhs, then the entire value on receipt basis taxable, and subsequently service provider is liable to pay service tax as per Point of Taxation Rule 3.

Rule 4: Determination of point of taxation in case of change in effective rate of tax:

Notwithstanding anything contained in rule 3, the point of taxation in cases where there is a *change in effective rate* of tax in respect of a service, shall be determined in the following manner, namely:-

(a) in case a taxable service has been provided before the change in effective rate,—

(i) where the invoice for the same has been issued and the payment received after the *change in effective rate,* the point of taxation shall be date of payment or issuing of invoice, whichever is earlier; or

(ii) where the invoice has also been issued prior to *change in effective rate* but the payment is received after the change in effective rate, the point of taxation shall be the date of issuing of invoice; or

(iii) where the payment is also received before the *change in effective rate,* but the invoice for the same has been issued after the *change in effective rate,* the point of taxation shall be the date of payment;

Example 33: (a) The applicability of the rule will be clear from the illustrations in the following table:

Sl.No.	Date of provision of service	Date of Invoice	Date on which payment received	Point of taxation
(i)	Before change	After change	After change	Date of payment or invoice, whichever is earlier
(ii)	Before change	Before change	After change	Date of invoice
(iii)	Before change	After change	Before change	Date of payment

(b) In case a taxable service has been provided after the change in effective rate,-

(i) where the payment for the invoice is also made after the change in effective rate but the invoice has been issued prior to the change in effective rate, the point of taxation shall be the date of payment; or

(ii) where the invoice has been issued and the payment for the invoice received before the change in effective rate, the point of taxation shall be the date of receipt of payment or date of issuance of invoice, whichever is earlier; or

(iii) where the invoice has also been raised after the change in effective rate but the payment has been received before the change in effective rate, the point of taxation shall be date of issuing of invoice.

Example 34: The applicability of the rule will be clear from the illustrations in the following table:

S. No.	Date of provision of service	Date of Invoice	Date on which payment received	Point of taxation
(i)	After change	Before change	After change	Date of payment
(ii)	After change	Before change	Before change	Date of payment or invoice, whichever is earlier
(iii)	After change	After change	Before change	Date of invoice

Explanation: For the purposes of this rule, "change in effective rate of tax" shall include a change in the portion of value on which tax is payable in terms of a notification issued under the provisions of Finance Act, 1994 or rules made thereunder.

Alternative: there are three voters namely date of provision of service, date of invoice and date of payment received and two candidates'namely new rate of tax and old rate of tax. Hence, majority wins.

Example 35:

S.No.	Date of provision of service	Date of Invoice	Date on which payment received	Effective rate of S.T.
(i)	Before change	After change	After change	New Rate
(ii)	Before change	Before change	After change	Old Rate
(iii)	Before change	After change	Before change	Old Rate
(iv)	After change	Before change	After change	New Rate
(v)	After change	Before change	Before change	Old Rate
(vi)	After change	After change	Before change	New Rate

Rule 5: Payment of tax in cases of new services:

Where a service, not being a service covered by rule 6, is taxed for the first time, then,—

(a) no tax shall be payable to the extent the invoice has been issued and the payment received against such invoice before such service became taxable;

Example: Food King Pvt. Ltd., provider of restaurant services having facility of air conditioning and license to serve alcoholic beverages in relation to serving of food or beverage. These services are taxable w.e.f. 1-5-2011. Payment received and invoice raised prior to 1-5-2011 are not taxable.

(b) no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within 14 days of the date when the service is taxed for the first time (w.e.f. 1-4-2012).

Example 36: Queen Pvt. Ltd., provider of taxable services. These services are taxable w.e.f. 1-5-2012. Payment was received from a customer for ₹ 5,00,000 on 20-4-2012. The invoice has been issued on 4-5-2012 (i.e. within 14 days of the date when the service is taxed for the first time). Hence, service provider not liable to pay service tax on the entire value of ₹ 5,00,000.

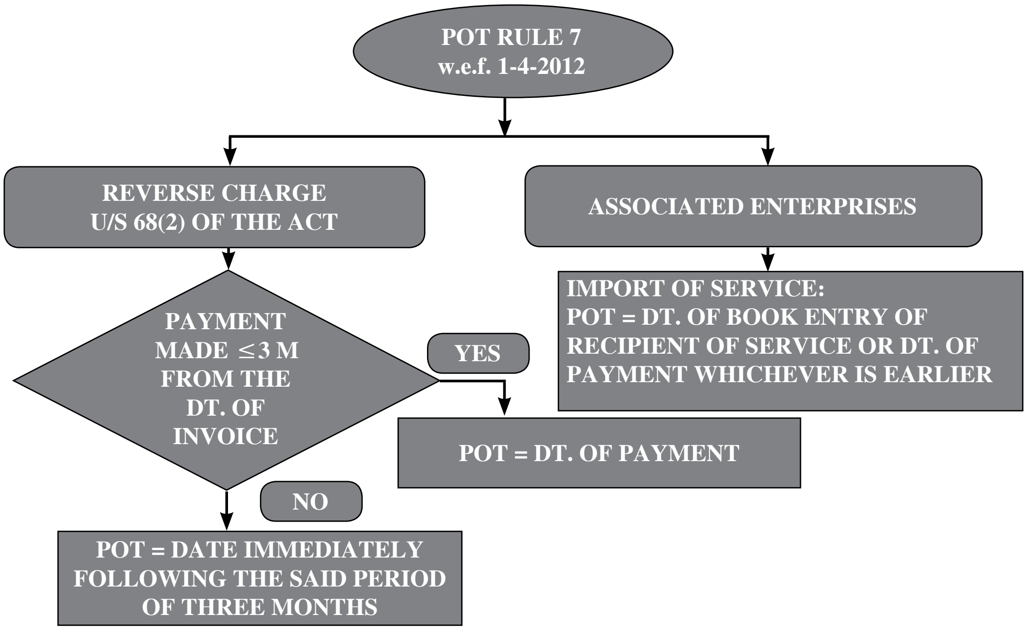
Rule 6: Determination of point of taxation in case of continuous supply of service (Omitted w.e.f. 1-4-2012)

Rule 7: Determination of point of taxation in case of specified services or persons (w.e.f. 1-4-2012)

Notwithstanding anything contained in rules 3, 4 or 8, the Point of Taxation in respect of the persons required to pay tax as recipients of service under the rules made in this regard in respect of services notified under section 68(2) of the Finance Act, 1994 shall be the date on which payment is made.

Provided that the payment is not made within a period of three months of the date of invoice, the point of taxation shall be the date immediately following the said period of three months.

In case of "associated enterprises", where the person providing the service is located outside India, the point of taxation shall be the date of debit in the books of account of the person receiving the service or date of making the payment whichever is earlier.



Rule 8: Determination of point of taxation in case of copyrights, etc.

In respect of royalties and payments pertaining to copyrights, trademarks, designs or patents, where the whole amount of the consideration for the provision of service is not ascertainable at the time when service was performed, and the payment for the benefit of such service is made subsequently. In this case, point of taxation will be each time when the payment received or the date when the invoice is issued by the provider of service, whichever is earlier.

Rule 8A: POT in other cases [Best Judgment Assessment of POT]

For determination of POT in other cases whereby in the cases where date of invoice or date of payment is not available, the C.E.O. (Central Excise Officer) can conduct best judgment assessment to determine the point of taxation.

Rule 9: Transitional Provisions:

Nothing contained in these rules shall be applicable

(i) where the provision of service is completed; or

(ii) where invoices are issued

prior to the date on which these rules come into force.

Rule 10: Determination of point of taxation if payment is made after specified period

Notwithstanding anything contained in the first proviso to rule 7, if the invoice in respect of a service, for which point of taxation is determinable under rule 7 has been issued before the 1st day of October, 2014 but payment has been made as on the said day, the point of taxation shall:-

(a) if payment is made within a period of six months of the date of invoice, be the date on which payment is made;

(b) if payment is not made within a period of six months of the date of invoice, be determined as if rule 7 and this rule do not exist.

6.13 TAXABLE EVENT IN SERVICE TAX

Taxable event and tax liability do not happen at the same time. Taxable event happens when a taxable service is rendered. Tax liability is required to pay as per Point of Taxation Rules, 2011 (w.e.f. 1-4-2011).

6.13.1 Point of Taxation as per the Point of Taxation Rules, 2011,

- Date of Invoice (or)
- Payment received (or)
- Completion of the provision of service

Whichever is earlier.

As per the Point of Taxation Rules, discussed above, different points of time have been chosen when a service shall be deemed to have been provided, whereas the rules has made by introducing a deeming fiction when a service shall be deemed to have been provided, but no such provisions have been made in the Finance Act, 1994.

However, the said provision is not applicable for those service providers named under Rule 7 of the Point of Taxation Rules, 2011 namely determination of point of taxation in case of specified services or persons. For them taxable event is rendering of taxable service only.

6.13.2 When Service Provider Receives an Advance

Payment may be received in advance (i.e. ahead of rendering of complete service) or in arrears (i.e. after rendering of service).

When the service provider receives an advance payment in respect of a taxable service being rendered by him, the liability to pay service tax arises as soon as he receives the advance.

When the service provider receives an advance payment in respect of a non-taxable service which is not taxable at the time the advance is being received, there will be service tax liability if the services are taxable at the time of rendering the services.

Service tax is payable on value of taxable service actually billed, even though the value of taxable services yet to be received.

If the amount of invoice is renegotiated due to deficient provision or in any other way changed in terms of conditions of the contract (e.g. contingent on the happening or non-happening of a future event), the tax will be payable on the revised amount provided the excess amount is either refunded or a suitable credit is issued to the service receiver.

6.13.3 Concession is not available for bad debts

If an assessee issues invoice, say for ₹ 5,00,000 and realized only ₹ 4,80,000 from his client and ₹ 20,000 becomes bad debt, then he cannot claim that he has paid excess tax for ₹ 20,000 and in such a situation, he shall not be entitled to make any adjustment of tax paid in respect of ₹ 20,000, which has become a bad debt.

Example 37: The service provider, a chartered accountant whose previous year (2014-15) turnover less than ₹ 50 lakhs, received an amount of ₹ 1,00,000 in April 2015, for a consulting engagement worth ₹ 5,00,000 which he completes in the month of July 2015 and for which balance payment is received on August 2015. Service tax is payable on ₹ 1,00,000 for the quarter April to June on or before 6th July 2015. Service tax liability for the balance of ₹ 4,00,000 for the quarter July to September, on or before 6th October 2015. Service provider is liable to pay service tax on receipt basis as per rule 3 of the Point of Taxation Rules, 2011 read with rule 6 of Service Tax Rules, 1994 (w.e.f. 1-4-2012).

Example 38: Information technology software services provided by X Ltd. for ₹ 25,00,000 lakhs and an invoice issued on 1st July 2015. Service provider has not been received consideration upto the end of 31st July, 2015. As per rule 3 of the Point of Taxation Rules, 2011 service provider is liable to pay service tax on the value of invoice on or before 6th August, 2015.

Example 39: A Ltd., being an interior decorator received the advance money from his customer of ₹ 30,000 in the month of July 2015, for which he is going to work in the month of September, 2015. A Ltd. being service provider is liable to pay the service tax @ 14.5% on ₹ 30,000 for the month of July, 2015 on or before 6th August, 2015. The order has been cancelled on 25th August, 2015. Hence, A Ltd. can file refund for the amount paid as service tax. Alternatively he can adjust the same against any taxable output services.

Example 40: X Ltd. provided cargo handling services for ₹ 15,00,000 in the month of 15th May, 2015. Invoice issued on 1st July 2015. 50% has been received on 1st April, 2015 and balance on 5th July, 2015.

You are required to find out due dates of payment of service tax.

Answer:

As per rule 3 of the Point of Taxation Rules, 2011, point of taxation for the first 50% received on 1st April, 2015 (i.e. date of completion of service or date of receipt of payment whichever is earlier, since, invoice has not been issued within 30 days of completion of service).

Therefore, due date of payment of service tax is 6th May, 2015.

Point of taxation for the balance 50% is 15th May, 2015 (i.e. date of completion of service or date of receipt of payment whichever is earlier, since, invoice has not been issued within 30 days of completion of service).

Therefore, due date of payment of service tax is 6th June, 2015.

Example 41: A provider (X Ltd.) of information technology software services received on advance of ₹ 10 lakhs on 21st July 2015 and the balance ₹ 40 lakhs on 1st October 2015. Information technology software service was listed as a taxable service w.e.f. 16-5-2008. Services actually rendered on 1st August 2015 and invoice issued on 10th August 2015. There will be service tax liability @14.5% on ₹ 10 lakhs for the month of July 2015, and on ₹ 40 lakhs for the month of August 2015.

6.14 PLACE OF PROVISION OF SERVICES RULES, 2012

The 'Place of Provision of Services Rules, 2012' specifies the manner to determine the taxing jurisdiction for a service. Hitherto, the task of identifying the taxing jurisdiction was largely limited in the context of import or export of services. For this purpose rules were formulated which handled the subject of place of provision of services somewhat indirectly, confining to define the circumstances in which a provision of service would constitute import or export.

These rules are primarily meant for persons who deal in cross-border services. They will also be equally applicable for those who have operations with suppliers or customers in the state of Jammu and Kashmir.

Additionally service providers operating within India from multiple locations, without having centralized registration will find them useful in determining the precise taxable jurisdiction applicable to their operations. The rules will be equally relevant for determining services that are wholly consumed within a SPEICAL ECONOMIC ZONE (SEZ), to avail the outright exemption.

Rule 1: place of provision of services rules, 2012 (w.e.f. 1-7-2012) Definitions.- In these rules, unless the context otherwise requires,-

(a) "Act" means the Finance Act, 1994;

(b) "account" means an account bearing interest to the depositor, and includes a non-resident external account and a non-resident ordinary account;

(c) "banking company" has the meaning assigned to it in clause (a) of section 45A of the Reserve Bank of India Act, 1934 (2 of 1934);

(d) "continuous journey" means a journey for which a single or more than one ticket or invoice is issued at the same time, either by one service provider or through one agent acting on behalf of more than one service provider, and which involves no stopover between any of the legs of the journey for which one or more separate tickets or invoices are issued;

(e) "financial institution" has the meaning assigned to it in clause (c) of section 45-I of the Reserve Bank of India Act,1 934 (2 of 1934);

(f) "intermediary" means a broker, an agent or any other person, by whatever name called, who arranges or facilitates a provision of a service (hereinafter called the 'main' service) or a supply of goods between two or more persons, but does not include a person who provides the main service or supplies the goods on his account (w.e.f. 1.10.2014);

(g) "leg of journey" means a part of the journey that begins where passengers embark or disembark the conveyance, or where it is stopped to allow for its servicing or refueling, and ends where it is next stopped for any of those purposes;

(h) "location of the service provider" means-

(a) where the service provider has obtained a single registration, whether centralized or otherwise, the premises for which such registration has been obtained;

(b) where the service provider is not covered under sub-clause (a):

(i) the location of his business establishment; or

(ii) where the services are provided from a place other than the business establishment, that is to say, a fixed establishment elsewhere, the location of such establishment; or

(iii) where services are provided from more than one establishment, whether business or fixed, the establishment most directly concerned with the provision of the service; and

(iv) in the absence of such places, the usual place of residence of the service provider.

(i) "location of the service receiver" means:-

(a) where the recipient of service has obtained a single registration, whether centralized or otherwise, the premises for which such registration has been obtained;

(b) where the recipient of service is not covered under sub-clause (a):

(i) the location of his business establishment; or

(ii) where services are used at a place other than the business establishment, that is to say, a fixed establishment elsewhere, the location of such establishment; or

(iii) where services are used at more than one establishment, whether business or fixed, the establishment most directly concerned with the use of the service; and

(iv) in the absence of such places, the usual place of residence of the recipient of service.

Explanation:- For the purposes of clauses (h) and (i), "usual place of residence" in case of a body corporate means the place where it is incorporated or otherwise legally constituted.

Explanation 2:- For the purpose of clause (i), in the case of telecommunication service, the usual place of residence shall be the billing address.

(j) "means of transport" means any conveyance designed to transport goods or persons from one place to another;

(k) "non-banking financial company" means137

   (i) a financial institution which is a company; or

   (ii) a non-banking institution which is a company and which has as its principal business the receiving of deposits, under any scheme or arrangement or in any other manner, or lending in any manner; or

   (iii) such other non-banking institution or class of such institutions, as the Reserve Bank of India may, with the previous approval of the Central Government and by notification in the Official Gazette specify;

(l) "online information and database access or retrieval services" means providing data or information, retrievable or otherwise, to any person, in electronic form through a computer network;

(m) "person liable to pay tax" shall mean the person liable to pay service tax under section 68 of the Act or under sub-clause (d) of sub-rule (1) of rule (2) of the Service Tax Rules, 1994;

(n) "provided" includes the expression "to be provided";

(o) "received" includes the expression "to be received";

(p) "registration" means the registration under rule 4 of the Service Tax Rules, 1994;

(q) "telecommunication service" means service of any description (including electronic mail, voice mail, data services, audio tex services, video tex services, radio paging and cellular mobile telephone services) which is made available to users by means of any transmission or reception of signs, signals, writing, images and sounds or intelligence of any nature, by wire, radio, visual or other electro-magnetic means but shall not include broadcasting services.

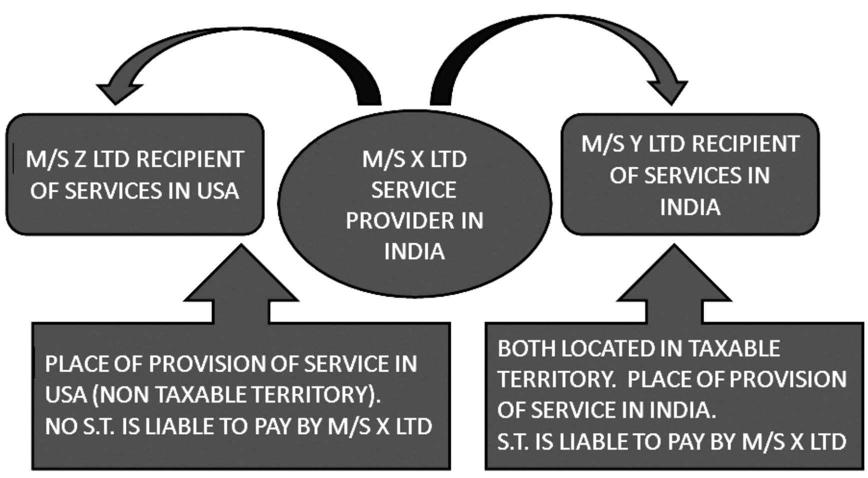
(r) words and expressions used in these rules and not defined, but defined in the Act, shall have the meanings respectively assigned to them in the Act.

Rule 3: Location of the receiver:

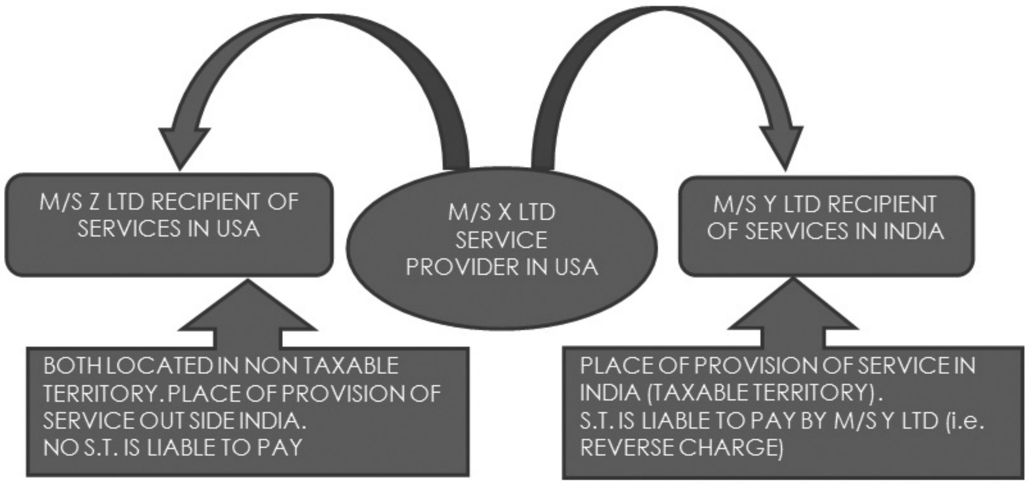
The place of provision of a service shall be the location of the recipient of service:

Provided that in case the location of the service receiver is not available in the ordinary course of business, the place of provision shall be the location of the provider of service.

Example 42:



Example 43:



Rule 4: Performance based Services:

Place of provision of service shall be the location where the services are actually performed. However services provided by way of electronic means in relation to tangible goods, the place of provision of service shall be the actual location of goods:

Rule 4(a): services that are provided "in respect of goods that are made physically available, by the receiver to the service provider in order to provide the service"	Rule 4(a): not covers where supply of goods by the receiver is not material to the rendering of services
i. Repair or reconditioning or any other job work on goods (not amounting to manufacture) ii. Storage and warehousing iii. Courier services iv. Cargo handling services v. Technical testing /inspection/certification/analysis of goods vi. Dry cleaning etc.,	i. Consultancy report commissioned by a person is given on pen drive belonging to the customer ii. Market research service etc.,

The clause shall not apply in case of a service provided in respect of goods that are temporarily imported into India for repairs and are exported after the repairs without being put to any use in the taxable territory, other than that which is required for such repair. (w.e.f. 1.10.2014).

Place of provision of service shall be the location where the services are actually performed:

Rule 4(b): services that are provided "to an individual which required the physical presence of the receiver with the provider for provision of the service" and includes a person acting on behalf of the receiver.	Rule 4(b): not covers where physical presence of an individual is not required being recipient of service
i. Cosmetic or plastic surgery, ii. Beauty treatment services iii. Personal security services iv. Class room teaching v. Photographic services vi. Internet cafe services	i. Auditing ii. Interior decoration etc.,

Rule 5: Location of Immovable Property:

Place of provision of service is where the immovable property is located or intended to be located:

The place of provision of services relating to immovable property located in the taxable territory includes:	The place of provision of services relating to immovable property located in the taxable territory does not includes:
i. Lease or a right to use, occupation enjoyment or provision of hotel accommodation by a hotel, guest house, club	i. Repair and maintenance of machinery
ii. Construction service	ii. Advice relating to land prices
iii. Architects	iii. Real estate feasibility studies
iv. Interior decorators	iv. Services of an agent who arranges finance
v. Renting of immovable property etc.,	v. Legal opinion
	vi. Computation of tax for rent of immovable property

Rule 6: Services relating to Events:

Place of provision of service shall be the place where the event is actually held:

The place of provision of services relating to events in the taxable territory includes:	The place of provision of services relating to events does not includes:
Services in relation to admission as well as organisation of events such as conventions, i. Conferences, exhibitions, fairs, ii. Seminars, iii. Workshops, iv. Weddings, v. Sports and cultural events , vi. Artistic vii. Scientific, educational, viii. Entertainment events ix. Services ancillary to such admission	i. A service of courier agency used for distribution of entry tickets for an event is a service that is not ancillary to admission to the event

Rule 7: Part Performance of a Service at Different Locations:

Place of provision of service will be the place in the taxable territory where the greatest proportion of services is provided.

Where any service stated in rules 4, 5, or 6 is provided at more than one location, including a location of taxable territory, its place of provision shall be the location in the taxable territory where the greatest proportion of the service is provided

Rule 8: Service Provider and Receiver in Taxable Territory:

The place of provision of service will be the location of the receiver, notwithstanding the earlier rules (i.e. 4 to 6).

Rule 9: Specified Services:

Place of provision is location of the service provider.

SPECIFIED SERVICES INCLUDES:

(a) Services provided by a banking company, or financial company, or a NBFC to account holders

(b) Online information and database access or retrieval services

(c) Intermediary services (i.e. travel agent, tour operator, commission agent etc)

(d) Services consisting of hiring of all means of transport, other than, – (i) aircrafts, and (ii) vessels except yachts upto a period of one month w.e.f. 1.10.2014.

Rule 10: Place of Provision of a Service of Transportation of Goods:

Place of provision of service of transportation of goods is the place of destination of goods, except in the case of services provided by a G.T.A (in case of GOODS TRANSPORT AGENCY the place of provision of service is the location of the person liable to pay service tax).

Covered under rule 10	Not covered under rule 10
Goods transported by • Air • Vessel • Rail • Road	Goods transported by • Courier • Mail

Rule 11: Passenger Transportation Services:

The place of provision of a passenger transportation service is the place where the passenger embarks on the conveyance for a continuous journey.

Rule 12: Services Provided on Board Conveyances:

Any service provided on board a conveyance (air craft, vessel, rail, or rodways bus) will be covered here. The place of provision of service is the first scheduled point of departure of that conveyance for the journey.

Example 44: A video game or a movie on demand is provided as on board entertainment during the Kolkata – Delhi leg of a Bangkok-Kolkata-Delhi flight. The place of provision of this service will be Bangkok (outside taxable territory) and hence not taxable,

Rule 13: Power to Notify Services or Circumstances:

In order to prevent double taxation or non-taxation of the provision of a service or for the uniform application of rules.

Rule 14: Order of Application of Rules:

When two or more rules may appear equally applicable then rule that occurs later among the rules preferable.

Place of Provision of Services Rules, 2012

(adopted from Educational Guide issued by TRU, CBE&C, MoF, GoI)

Rules at a glance:

Rule 3	**Location of the Receiver**
Rule 4	**Performance based Services**
Rule 5	**Location of Immovable Property**
Rule 6	**Services relating to Events**
Rule 7	**Part performance of a service at different locations**
Rule 8	**Services where the Provider as well as Receiver is located in Taxable Territory**
Rule 9	**Specified services- Place of provision is location of the service provider**
Rule 10	**Place of Provision of a service of transportation of goods**
Rule 11	**Passenger Transportation Services**
Rule 12	**Services provided on board conveyances**
Rule 13	**Power to notify services or circumstances**
Rule 14	**Order of application of Rules**

Rule 3- Location of the Receiver

6.14.1 What is the implication of this Rule?

The main rule or the default rule provides that a service shall be deemed to be provided where the receiver is located.

The main rule is applied when none of the other later rules apply (by virtue of rule 14 governing the order of application of rules- see para 5.14 of this guidance paper). In other words, if a service is not covered by an exception under one of the later rules, and is consequently covered under this default rule, then the receiver's location will determine whether the service is leviable to tax in the taxable territory.

The principal effect of the Main Rule is that:-

A. Where the location of receiver of a service is in the taxable territory, such service will be deemed to be provided in the taxable territory and service tax will be payable.

B. However if the receiver is located outside the taxable territory, no service tax will be payable on the said service.

6.14.2. If the place of provision of a taxable service is the location of service receiver, who is the person liable to pay tax on the transaction?

Service tax is normally required to be paid by the provider of a service, except where he is located outside the taxable territory and the place of provision of service is in the taxable territory.

Where the provider of a service is located outside the taxable territory, the person liable to pay service tax is the receiver of the service in the taxable territory, unless of course, the service is otherwise exempted.

Following illustration will make this clear:-

A company ABC provides a service to a receiver PQR, both located in the taxable territory.

Since the location of the receiver is in the taxable territory, the service is taxable. Service tax liability will be discharged by ABC, being the service provider and being located in taxable territory.

However, if ABC were to supply the same service to a recipient DEF located in non-taxable territory, the provision of such service is not taxable, since the receiver is located outside the taxable territory.

If the same service were to be provided to PQR (located in taxable territory) by an overseas provider XYZ (located in non-taxable territory), the service would be taxable, since the recipient is located in the taxable territory. However, since the service provider is located in a nontaxable territory, the tax liability would be discharged by the receiver, under the reverse charge principle (also referred to as "tax shift").

6.14.3 Who is the service receiver?

Normally, the person who is legally entitled to receive a service and, therefore, obliged to make payment, is the receiver of a service, whether or not he actually makes the payment or someone else makes the payment on his behalf.

Illustration 1:

A lady leaves her car at a service station for the purpose of servicing. She asks her chauffer to collect the car from the service station later in the day, after the servicing is over. The chauffer makes the payment on behalf of the lady owner and collects the car.

Here the lady is the 'person obliged to make the payment' towards servicing charges, and therefore, she is the receiver of the service.

6.14.4 What would be the situation where the payment for a service is made at one location (say by the headquarters of a business) but the actual rendering of the service is elsewhere (i.e. a fixed establishment)?

Occasionally, a person may be the person liable to make payment for the service provided on his behalf to another person. For instance, the provision of a service may be negotiated at the headquarters of an entity by way of centralized sourcing of services whereas the actual provision is made at various locations in different taxing jurisdictions (in the case of what is commonly referred to as a multi-locational entity or MLE). Here, the central office may act only as a facilitator to negotiate the contract on behalf of various geographical establishments.

Each of the geographical establishments receives the service and is obligated to make the payment either through headquarters or sometimes directly. When the payment is made directly, there is no confusion. In other situations, where the payment is settled either by cash or through debit and credit note between the business and fixed establishments, it is clear that the payment is being made by a geographical location. Wherever a fixed establishment bears the cost of acquiring, or using or consuming a service through any internal arrangement (normally referred to as a "recharge", "reallocation", or a "settlement"), these are generally made in accordance with corporate tax or other statutory requirements. These accounting arrangements also invariably aid the MLE's management in budgeting and financial performance measurement.

Various accounting and business management systems are generally employed to manage, monitor and document the entire purchasing cycle of goods and services (such as the ERP Enterprise Resource Planning System). These systems support and document the company processes, including the financial and accounting process, and purchasing process.

Normally, these systems will provide the required information and audit trail to identify the establishment that uses or consumes a service.

It should be noted that in terms of proviso to section 66B, the establishments in a taxable and non-taxable territory are to be treated as distinct persons. Moreover, the definition of "location of the receiver" clearly states that "where the services are "used" at more than one establishment, whether business or fixed, the establishment most directly concerned with the use of the service" will be the location. Thus, the taxing jurisdiction of service, which is provided under a 'global framework agreement' between two multinational companies with the business establishment located outside the taxable territory, but which is used or consumed by a fixed establishment located in the taxable territory, will be the taxable territory.

6.14.5 What is the place of provision where the location of receiver is not ascertainable in the ordinary course of business?

Generally, in case of a service provided to a person who is in business, the provider of the service will have the location of the recipient's registered location, or his business establishment, or his fixed establishment etc, as the case may be. However, in case of certain services (which are not covered by the exceptions to the main rule), the service provider may not have the location of the service receiver, in the ordinary course of his business. This will also be the case where a service is provided to an individual customer who comes to the premises of the service provider for availing the service and the provider has to, more often than not, rely on the declared location of the customer. In such cases the place of provision will be the location of the service provider. It may be noted that the service provider is not required to make any extraordinary efforts to trace the address of the service receiver. The address should be available in the ordinary course of business.

In case of certain specified categories of services, the place of provision shall be the place where the services are actually performed. These are discussed in the following paragraphs.

Rule 4- Performance based Services

6.14.6 What are the services that are provided "in respect of goods that are made physically available, by the receiver to the service provider, in order to provide the service"?- sub-rule (1):

Services that are related to goods, and which require such goods to be made available to the service provider or a person acting on behalf of the service provider so that the service can be rendered, are covered here. The essential characteristic of a service to be covered under this rule is that the goods temporarily come into the physical possession or control of the service provider, and without this happening, the service cannot be rendered. Thus, the service involves movable objects or things that can be touched, felt or possessed. Examples of such services are repair, reconditioning, or any other work on goods (not amounting to manufacture), storage and warehousing, courier service, cargo handling service (loading, unloading, packing or unpacking of cargo), technical testing/ inspection/certification/ analysis of goods, dry cleaning etc. It will not cover services where the supply of goods by the receiver is not material to the rendering of the service e.g. where a consultancy report commissioned by a person is given on a pen drive belonging to the customer. Similarly, provision of a market research service to a manufacturing firm for a consumer product (say, a new detergent) will not fall in this category, even if the market research firm is given say, 1000 nos. of 1 kilogram packets of the product by the manufacturer, to carry for door-to-door surveys.

6.14.7 What is the implication of the proviso to sub-rule (1)?

The proviso to this rule states as follows:-
"Provided further that where such services are provided from a remote location by way of electronic means, the place of provision shall be the location where goods are situated at the time of provision of service."
In the field of information technology, it is not uncommon to provide services in relation to tangible goods located distantly from a remote location. Thus the actual place of performance of the service could be quite different from the actual location of the tangible goods. This proviso requires that the place of provision shall be the actual location of the goods and not the place of performance, which in normal situations is one and the same.

6.14.8 What are the services that are provided "to an individual … which require the physical presence of the receiver … with the provider for provision of the service."?- sub-rule (2)

Certain services like cosmetic or plastic surgery, beauty treatment services, personal security service, health and fitness services, photography service (to individuals), internet café service, classroom teaching, are examples of services that require the presence of the individual receiver for their provision. As would be evident from these examples, the nature of services covered here is such as are rendered in person and in the receiver's physical presence.

Though these are generally rendered at the service provider's premises (at a cosmetic or plastic surgery clinic, or beauty parlor, or health and fitness centre, or internet café), they could also be provided at the customer's premises, or occasionally while the receiver is on the move (say, a personal security service; or a beauty treatment on board an aircraft).

6.14.9 What is the significance of "..in the physical presence of an individual, whether represented either as the service receiver or a person acting on behalf of the receiver" in this rule?

This implies that while a service in this category is capable of being rendered only in the presence of an individual, it will not matter if, in terms of the contractual arrangement between the provider and the receiver (formal or informal, written or oral), the service is actually rendered by the provider to a person other than the receiver, who is acting on behalf of the receiver.

Illustration 2:

A modelling agency contracts with a beauty parlour for beauty treatment of say, 20 models. Here again is a situation where the modelling agency is the receiver of the service, but the service is rendered to the models, who are receiving the beauty treatment service on behalf of the modelling agency. Hence, notwithstanding that the modelling agency does not qualify as the individual receiver in whose presence the service is rendered, the nature of the service is such as can be rendered only to an individual, thereby qualifying to be covered under this rule.

Rule 5- Location of Immovable Property

In the case of a service that is 'directly in relation to immovable property', the place of provision is where the immovable property (land or building) is located, irrespective of where the provider or receiver is located.

6.14.10 What is "immovable property"?

"Immovable Property" has not been defined in the Finance Act, 1994. However, in terms of section 4 of the General Clauses Act, 1897, the definition of immovable property provided in sub-section 3 (26) of the General Clauses Act will apply, which states as under:

"Immovable Property" shall include land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth."

It may be noted that the definition is inclusive and thus properties such as buildings and fixed structures on land would be covered by the definition of immovable property. The property must be attached to some part of earth even if underwater.

6.14.11 What are the criteria to determine if a service is 'directly in relation to' immovable property located in taxable territory?

Generally, the following criteria will be used to determine if a service is in respect of immovable property located in the taxable territory:

(i) The service consists of lease, or a right of use, occupation, enjoyment or exploitation of an immovable property;

(ii) the service is physically performed or agreed to be performed on an immovable property (e.g. maintenance) or property to come into existence (e.g. construction);

(iii) the direct object of the service is the immovable property in the sense that the service enhances the value of the property, affects the nature of the property, relates to preparing the property for development or redevelopment or the environment within the limits of the property (e.g. engineering, architectural services, surveying and sub-dividing, management services, security services etc);

(iv) the purpose of the service is:

   (a) the transfer or conveyance of the property or the proposed transfer or conveyance of the property (e.g., real estate services in relation to the actual or proposed acquisition, lease or rental of property, legal services rendered to the owner or beneficiary or potential owner or beneficiary of property as a result of a will or testament);

   (b) the determination of the title to the property.

   There must be more than a mere indirect or incidental connection between a service provided in relation to an immovable property, and the underlying immovable property. For example, a legal firm's general opinion with respect to the capital gains tax liability arising from the sale of a commercial property in India is basically advice on taxation legislation in general even though it relates to the subject of an immovable property. This will not be treated as a service in respect of the immovable property.

6.14.12 Examples of land-related services

(i) Services supplied in the course of construction, reconstruction, alteration, demolition, repair or maintenance (including painting and decorating) of any building or civil engineering work;

(ii) Renting of immovable property;

(iii) Services of real estate agents, auctioneers, architects, engineers and similar experts or professional people, relating to land, buildings or civil engineering works. This includes the management, survey or valuation of property by a solicitor, surveyor or loss adjuster;

(iv) Services connected with oil/gas/mineral exploration or exploitation relating to specific sites of land or the seabed;

(v) The surveying (such as seismic, geological or geomagnetic) of land or seabed;

(vi) Legal services such as dealing with applications for planning permission;

(vii) Packages of property management services which may include rent collection, arranging repairs and the maintenance of financial accounts;

(viii) The supply of hotel accommodation or warehouse space.

6.14.13 What if a service is not directly related to immovable property?

The place of provision of services rule applies only to services which relate directly to specific sites of land or property. In other words, the immovable property must be clearly identifiable to be the one from where, or in respect of which, a service is being provided. Thus, there needs to be a very close link or association between the service and the immovable property.

Needless to say, this rule does not apply if a provision of service has only an indirect connection with the immovable property, or if the service is only an incidental component of a more comprehensive supply of services.

For example, the services of an architect contracted to design the landscaping of a particular resort hotel in Goa would be land-related. However, if an interior decorator is engaged by a retail chain to design a common décor for all its stores in India, this service would not be land related.

The default rule i.e. Rule 3 will apply in this case.

6.14.14. Examples of services which are not land-related

(i) Repair and maintenance of machinery which is not permanently installed. This is a service related to goods.

(ii) Advice or information relating to land prices or property markets because they do not relate to specific sites.

(iii) Land or Real Estate Feasibility studies, say in respect of the investment potential of a developing suburb, since this service does not relate to a specific property or site.

(iv) Services of a Tax Return Preparer in simply calculating a tax return from figures provided by a business in respect of rental income from commercial property.

(v) Services of an agent who arranges finance for the purchase of a property.

Rule 6- Services relating to Events

6.14.15. What is the place of provision of services relating to events?

Place of provision of services provided by way of admission to, or organization of a cultural, artistic, sporting, scientific, educational, entertainment event, or a celebration, conference, fair, exhibition, or any other similar event and of services ancillary to such admission, shall be the place where the event is held.

6.14.16. What are the services that will be covered in this category?

Services in relation to admission as well as organization of events such as conventions, conferences, exhibitions, fairs, seminars, workshops, weddings, sports and cultural events are covered under this Rule.

Illustration 3:

A management school located in USA intends to organize a road show in Mumbai and New Delhi for prospective students. Any service provided by an event manager, or the right to entry (participation fee for prospective students, say) will be taxable in India.

Illustration 4:

An Indian fashion design firm hosts a show at Toronto, Canada. The firm receives the services of a Canadian event organizer. The place of provision of this service is the location of the event, which is outside the taxable territory. Any service provided in relation to this event, including the right to entry, will be non-taxable.

6.14.17. What is a service ancillary organization or admission to an event?

Provision of sound engineering for an artistic event is a prerequisite for staging of that event and should be regarded as a service ancillary to its organization. A service of hiring a specific equipment to enjoy the event at the venue (against a charge that is not included in the price of entry ticket) is an example of a service that is ancillary to admission.

6.14.18. What are event-related services that would be treated as not ancillary to admission to an event?

A service of courier agency used for distribution of entry tickets for an event is a service that is not ancillary to admission to the event.

Rule 7- Part performance of a service at different locations

6.14.19. What does this Rule imply?

This Rule covers situations where the actual performance of a service is at more than one location, and occasionally one (or more) such locations may be outside the taxable territory.

This Rule states as follows:-

"Where any service stated in rules 4, 5, or 6 is provided at more than one location, including a location in the taxable territory, its place of provision shall be the location in the taxable territory where the greatest proportion of the service is provided".

The following example illustrates the application of this Rule:-

Illustration 5:

An Indian firm provides a 'technical inspection and certification service' for a newly developed product of an overseas firm (say, for a newly launched motorbike which has to meet emission standards in different states or countries). Say, the testing is carried out in Maharashtra (20%), Kerala (25%), and an international location (say, Colombo 55%).

Notwithstanding the fact that the greatest proportion of service is outside the taxable territory, the place of provision will be the place in the taxable territory where the greatest proportion of service is provided, in this case Kerala.

This rule is, however, not intended to capture insignificant portion of a service rendered in any part of the taxable territory like mere issue of invoice, processing of purchase order or recovery, which are not by way of service actually performed on goods.

It is clarified that this rule is applicable in performance-based services or location-specific services (immovable property related or event-linked). Normally, such services when provided in a non-taxable territory would require the presence of separate establishments in such territories. By virtue of an explanation of sub-clause (44) of section 65B, they would constitute distinct persons and thus it would be legitimate to invoice the services rendered individually in the two territories.

Rule 8- Services where the Provider as well as Receiver is located in Taxable Territory

6.14.20 What is the place of provision of a service where the location of the service provider and that of the service receiver is in the taxable territory?

The place of provision of a service, which is provided by a provider located in the taxable territory to a receiver who is also in the taxable territory, will be the location of the receiver.

6.14.21 What is the implication of this Rule?

This Rule covers situations where the place of provision of a service provided in the taxable territory may be determinable to be outside the taxable territory, in terms of the application of one of the earlier Rules i.e. Rule 4 to 6, but the service provider, as well as the service receiver, are located in the taxable territory.

The implication of this Rule is that in all such cases, the place of provision will be deemed to be in the taxable territory, notwithstanding the earlier rules. The presence of both the service provider and the service receiver in the taxable territory indicates that the place of consumption of the service is in the taxable territory. Services rendered, where both the provider and receiver of the service are located outside the taxable territory, are now covered by the mega exemption.

Illustration 6:

A helicopter of Pawan Hans Ltd (India based) develops a technical snag in Nepal. Say, engineers are deputed by Hindustan Aeronautics Ltd, Bangalore, to undertake repairs at the site in Nepal. But for this rule, Rule 4, sub-rule (1) would apply in this case, and the place of provision would be Nepal i.e. outside the taxable territory. However, by application of Rule 7, since the service provider, as well as the receiver, are located in the taxable territory, the place of provision of this service will be within the taxable territory.

Rule 9- Specified services- Place of provision is location of the service provider

6.14.22. What are the specified services where the place of provision is the location of the service provider?

Following are the specified services where the place of provision is the location of the service provider:-

i) Services provided by a banking company, or a financial company, or a non-banking financial company to account holders;

ii) Online information and database access or retrieval services;

iii) Intermediary services;

iv) Service consisting of hiring of means of transport, up to a period of one month.

6.14.23. What is the meaning of "account holder"? Which accounts are not covered by this rule?

"Account" has been defined in the rules to mean an account which bears an interest to the depositor. Services provided to holders of demand deposits, term deposits, NRE (non-resident external) accounts and NRO (non-resident ordinary) accounts will be covered under this rule. Banking services provided to persons other than account holders will be covered under the main rule (Rule 3- location of receiver).

6.14.24. What are the services that are provided by a banking company to an account holder (holder of an account bearing interest to the depositor)?

Following are examples of services that are provided by a banking company or financial institution to an "account holder", in the ordinary course of business:-

i) services linked to or requiring opening and operation of bank accounts such as lending, deposits, safe deposit locker etc;

ii) transfer of money including telegraphic transfer, mail transfer, electronic transfer etc.

6.14.25. What are the services that are not provided by a banking company or financial institution to an account holder, in the ordinary course of business, and will consequently be covered under another Rule?

Following are examples of services that are generally NOT provided by a banking company or financial institution to an account holder (holder of a deposit account bearing interest), in the ordinary course of business:-

i) financial leasing services including equipment leasing and hire-purchase;

ii) merchant banking services;

iii) Securities and foreign exchange (forex) broking, and purchase or sale of foreign currency, including money changing;

iv) asset management including portfolio management, all forms of fund management, pension fund management, custodial, depository and trust services;

v) advisory and other auxiliary financial services including investment and portfolio research and advice, advice on mergers and acquisitions and advice on corporate restructuring and strategy;

vi) banker to an issue service.

In the case of any service which does not qualify as a service provided to an account holder, the place of provision will be determined under the default rule i.e. the Main Rule 3. Thus, it will be the location of the service receiver where it is known (ascertainable in the ordinary course of business), and the location of the service provider otherwise.

6.14.26. What are "Online information and database access or retrieval services"?

"Online information and database access or retrieval services" are services in relation to online information and database access or retrieval or both, in electronic form through computer network, in any manner. Thus, these services are essentially delivered over the internet or an electronic network which relies on the internet or similar network for their provision. The other important feature of these services is that they are completely automated, and require minimal human intervention.

Examples of such services are:-

i) online information generated automatically by software from specific data input by the customer, such as web-based services providing trade statistics, legal and financial data, matrimonial services, social networking sites;

ii) digitized content of books and other electronic publications, subscription of online newspapers and journals, online news, flight information and weather reports;

iii) Web-based services providing access or download of digital content.

The following services will not be treated as "online information and database access or retrieval services":-

i) Sale or purchase of goods, articles etc over the internet;

ii) Telecommunication services provided over the internet, including fax, telephony, audio conferencing, and videoconferencing;

iii) A service which is rendered over the internet, such as an architectural drawing, or management consultancy through e-mail;

iv) Repair of software, or of hardware, through the internet, from a remote location;

v) Internet backbone services and internet access services.

6.14.27. What are "Intermediary Services"?

Generally, an "intermediary" is a person who arranges or facilitates a supply of goods, or a provision of service, or both, between two persons, without material alteration or further processing. Thus, an intermediary is involved with two supplies at any one time:

i) the supply between the principal and the third party; and

ii) the supply of his own service (agency service) to his principal, for which a fee or commission is usually charged.

For the purpose of this rule, an intermediary in respect of goods (such as a commission agent i.e. a buying or selling agent, or a stockbroker) is excluded by definition.

Also excluded from this sub-rule is a person who arranges or facilitates a provision of a service (referred to in the rules as "the main service"), but provides the main service on his own account.

In order to determine whether a person is acting as an intermediary or not, the following factors need to be considered:-

Nature and value: An intermediary cannot alter the nature or value of the service, the supply of which he facilitates on behalf of his principal, although the principal may authorize the intermediary to negotiate a different price. Also, the principal must know the exact value at which the service is supplied (or obtained) on his behalf, and any discounts that the intermediary obtains must be passed back to the principal.

Separation of value: The value of an intermediary's service is invariably identifiable from the main supply of service that he is arranging. It can be based on an agreed percentage of the sale or purchase price. Generally, the amount charged by an agent from his principal is referred to as "commission".

Identity and title: The service provided by the intermediary on behalf of the principal is clearly identifiable.

In accordance with the above guiding principles, services provided by the following persons will qualify as 'intermediary services':-

i) Travel Agent (any mode of travel)

ii) Tour Operator

iii) Commission agent for a service [an agent for buying or selling of goods is excluded]

iv) Recovery Agent

Even in other cases, wherever a provider of any service acts as an intermediary for another person, as identified by the guiding principles outlined above, this rule will apply. Normally, it is expected that the intermediary or agent would have documentary evidence authorizing him to act on behalf of the provider of the 'main service'.

Illustration 7:

A freight forwarder arranges for export and import shipments. There could be two possible situations here- one when he acts on his own account, and the other, when he acts as an intermediary.

When the freight forwarder acts on his own account (say, for an export shipment)

A freight forwarder provides domestic transportation within taxable territory (say, from the exporter's factory located in Pune to Mumbai port) as well as international freight service (say, from Mumbai port to the international destination), under a single contract, on his own account (i.e. he buys-in and sells fright transport as a principal), and charges a consolidated amount to the exporter. This is a service of transportation of goods for which the place of supply is the destination of goods. Since the destination of goods is outside taxable territory, this service will not attract service tax. Here, it is presumed that ancillary freight services (i.e. services ancillary to transportation- loading, unloading, handling etc) are "bundled" with the principal service owing to a single contract or a single price (consideration).

On an import shipment with similar conditions, the place of supply will be in the taxable territory, and so the service tax will be attracted.

When the freight forwarder acts as an intermediary

Where the freight forwarder acts as an intermediary, the place of provision will be his location.

Service tax will be payable on the services provided by him. However, when he provides a service to an exporter of goods, the exporter can claim refund of service tax paid under notification for this purpose.

Similarly, persons such as call centres, who provide services to their clients by dealing with the customers of the client on the client's behalf, but actually provided these services on their own account, will not be categorized as intermediaries.

6.14.28 What is the service of "hiring of means of transport"?

Normally the following will constitute means of transport:-

i) Land vehicles such as motorcars, buses, trucks;

ii) Vessels;

iii) Aircraft;

iv) Vehicles designed specifically for the transport of sick or injured persons;

v) Mechanically or electronically propelled invalid carriages;

vi) Trailers, semi-trailers and railway wagons.

The following are not 'means of transport':-

i) Racing cars;

ii) Containers used to store or carry goods while being transported;

iii) Dredgers, or the like.

6.14.29 What if I provide a service of hiring of a fleet of cars to a company on an annual contract? What will be place of provision of my service if my business establishment is located in New Delhi, and the company is located in Faridabad (Haryana)?

This Rule covers situations where the hiring is for a period of upto one month. Since hiring period is more than one month, this sub-rule cannot be applied to the situation. The place of provision of your service will be determined in terms of Rule 3 i.e. receiver location, which in this case is Faridabad (Haryana).

Rule 10- Place of Provision of a service of transportation of goods

6.14.30 What are the services covered under this Rule?

Any service of transportation of goods, by any mode of transport (air, vessel, rail or by a goods transportation agency), is covered here. However, transportation of goods by courier or mail is not covered here.

6.14.31 What is the place of provision of a service of transportation of goods?

Place of provision of a service of transportation of goods is the place of destination of goods, except in the case of services provided by a Goods Transportation Agency in respect of transportation of goods by road, in which case the place of provision is the location of the person liable to pay tax (as determined in terms of rule 2(1)(d) of Service Tax Rules, 1994 (since amended).

Illustration 8:

A consignment of cut flowers is consigned from Chennai to Amsterdam. The place of provision of goods transportation service will be Amsterdam (outside India, hence not liable to service tax). Conversely, if a consignment of crystal ware is consigned from Paris to New Delhi, the place of provision will be New Delhi.

6.14.32 What does the proviso to this Rule imply?

The proviso to this Rule states as under:-

"Provided that the place of provision of services of transportation of goods by goods transportation agency shall be the location of the person liable to pay tax."

Sub-rule 2(1)(d) of Service Tax Rules, 1994 provides that where a service of transportation of goods is provided by a 'goods transportation agency', and the consignor or consignee is covered under any of the specified categories prescribed therein , the person liable to tax is the person who pays, or is liable to pay freight (either himself or through his agent) for the transportation of goods by road in a goods carriage. If such person is located in non-taxable territory, then the person liable to pay tax shall be the service provider.

Illustration 9:

A goods transportation agency ABC located in Delhi transports a consignment of new motorcycles from the factory of XYZ in Gurgaon (Haryana), to the premises of a dealer in Bhopal, Madhya Pradesh. Say, XYZ is a registered assessee and is also the person liable to pay freight and hence person liable to pay tax, in this case. Here, the place of provision of the service of transportation of goods will be the location of XYZ i.e. Haryana.

Illustration 10:

A goods transportation agency ABC located in Delhi transports a consignment of new motorcycles from the factory of XYZ in Gurgaon (Haryana), to the premises of a dealer in Jammu (non-taxable territory). Say, as per mutually agreed terms between ABC and XYZ, the dealer in Jammu is the person liable to pay freight. Here, in terms of amended provisions of rule 2(1)(d), since the person liable to pay freight is located in non-taxable territory, the person liable to pay tax will be ABC. Accordingly, the place of provision of the service of transportation of goods will be the location of ABC i.e. Delhi.

Rule 11- Passenger Transportation Services

6.14.33 What is the place of provision of passenger transportation services?

The place of provision of a passenger transportation service is the place where the passenger embarks on the conveyance for a continuous journey.

6.14.34 What does a "continuous journey" mean?

A "continuous journey" means a journey for which:-

(i) a single ticket has been issued for the entire journey; or

(ii) more than one ticket or invoice has been issued for the journey, by one service provider, or by an agent on behalf of more than one service providers, at the same time, and there is no scheduled stopover in the journey

6.14.35 What is the meaning of a stopover? Do all stopovers break a continuous journey?

"Stopover" means a place where a passenger can disembark either to transfer to another conveyance or break his journey for a certain period in order to resume it at a later point of time. All stopovers do not cause a break in continuous journey. Only such stopovers will be relevant for which one or more separate tickets are issued. Thus a travel on Delhi-London- New York-London-Delhi on a single ticket with a halt at London on either side, or even both, will be covered by the definition of continuous journey. However if a separate ticket is issued, say New York-Boston-New York, the same will be outside the scope of a continuous journey.

Rule 12- Services provided on board conveyances

6.14.36 What are services provided on board conveyances?

Any service provided on board a conveyance (aircraft, vessel, rail, or roadways bus) will be covered here. Some examples are on-board service of movies/music/video/ software games on demand, beauty treatment etc, albeit only when provided against a specific charge, and not supplied as part of the fare.

6.14.37 What is the place of provision of services provided on board conveyances?

The place of provision of services provided on board a conveyance during the course of a passenger transport operation is the first scheduled point of departure of that conveyance for the journey.

Illustration 11:

A video game or a movie-on-demand is provided as on-board entertainment during the Kolkata-Delhi leg of a Bangkok-Kolkata-Delhi flight. The place of provision of this service will be Bangkok (outside taxable territory, hence not liable to tax).

If the above service is provided on a Delhi-Kolkata-Bangkok-Jakarta flight during the Bangkok-Jakarta leg, then the place of provision will be Delhi (in the taxable territory, hence liable to tax).

Rule 13- Power to notify services or circumstances

6.14.38 What is the implication of this Rule?

This Rule states as follows:-

"In order to prevent double taxation or non-taxation of the provision of a service, or for the uniform application of rules, the Central Government shall have the power to notify any description of service or circumstances in which the place of provision shall be the place of effective use and enjoyment of a service."

The rule is an enabling power to correct any injustice being met due to the applicability of rules in a foreign territory in a manner which is inconsistent with these rules leading to double taxation. Due to the cross border nature of many services it is also possible in certain situations to set up businesses in a non-taxable territory while the effective enjoyment, or in other words consumption, may be in taxable territory. This rule is also meant as an anti-avoidance measure where the intent of the law is sought to be defeated through ingenious practices unknown to the ordinary ways of conducting business.

Rule 14- Order of application of Rules

6.14.39 What is the implication of this Rule?

Rule 14 provides that where the provision of a service is, prima facie, determinable in terms of more than one rule, it shall be determined in accordance with the rule that occurs later among the rules that merit equal consideration.

This Rule covers situations where the nature of a service, or the business activities of the service provider, may be such that two or more rules may appear equally applicable.

Following illustrations will make the implications of this Rule clear:-

Illustration 12:

An architect based in Mumbai provides his service to an Indian Hotel Chain (which has business establishment in New Delhi) for its newly acquired property in Dubai. If Rule 5 (Property rule) were to be applied, the place of provision would be the location of the property i.e. Dubai (outside the taxable territory). With this result, the service would not be taxable in India.

Whereas, by application of Rule 8, since both the provider and the receiver are located in taxable territory, the place of provision would be the location of the service receiver i.e. New Delhi. Place of provision being in the taxable territory, the service would be taxable in India.

By application of Rule 14, the later of the Rules i.e. Rule 8 would be applied to determine the place of provision.

Illustration 13:

For the Ms Universe Contest planned to be held in South Africa, the Indian pageant (say, located in Mumbai) avails the services of Indian beauticians, fashion designers, videographers, and photographers. The service providers travel as part of the Indian pageant's entourage to South Africa. Some of these services are in the nature of personalized services, for which the place of provision would normally be the location where performed (Performance rule-Rule 4), while for others, under the main rule (Receiver location) the place of provision would be the location of receiver.

Whereas, by application of Rule 8, since both the provider and the receiver are located in taxable territory, the place of provision would be the location of the service receiver i.e. New Delhi. Place of provision being in the taxable territory, the service would be taxable in India.

By application of Rule 15, the later of the Rules i.e. Rule 8 would be applied to determine the place of provision.

6.14.40 Taxability of 'bundled services'

'Bundled service' means a bundle of provision of various services wherein an element of provision of one service is combined with an element or elements of provision of any other service or services. An example of 'bundled service' would be air transport services provided

by airlines wherein an element of transportation of passenger by air is combined with an element of provision of catering service on board. Each service involves differential treatment as a manner of determination of value of two services for the purpose of charging service tax is different.

Two rules have been prescribed for determining the taxability of such services in clause (3) of section 66F of the Act. These rules, which are explained below, are subject to the provisions of the rule contained in sub section (2) of section 66F.

6.14.40.1 Services which are naturally bundled in the ordinary course of business

The rule is – 'If various elements of a bundled service are naturally bundled in the ordinary course of business, it shall be treated as provision of a single service which gives such bundle its essential character'

Illustrations 14:

- A hotel provides a 4-D/3-N package with the facility of breakfast. This is a natural bundling of services in the ordinary course of business. The service of hotel accommodation gives the bundle the essential character and would, therefore, be treated as service of providing hotel accommodation.
- A 5 star hotel is booked for a conference of 100 delegates on a lump sum package with the following facilities:
    - Accommodation for the delegates
    - Breakfast for the delegates,
    - Tea and coffee during conference
    - Access to fitness room for the delegates
    - Availability of conference room
    - Business centre

As is evident a bouquet of services is being provided, many of them chargeable to different effective rates of tax. None of the individual constituents are able to provide the essential character of the service. However, if the service is described as convention service it is able to capture the entire essence of the package. Thus the service may be judged as convention service and chargeable to full rate. However it will be fully justifiable for the hotel to charge individually for the services as long as there is no attempt to offload the value of one service on to another service that is chargeable at a concessional rate.

6.14.40.2 Services which are not naturally bundled in the ordinary course of business

The rule is – 'If various elements of a bundled service are not naturally bundled in the ordinary course of business, it shall be treated as provision of a service which attracts the highest amount of service tax.'

Illustrations 15:

A house is given on rent one floor of which is to be used as residence and the other for housing a printing press. Such renting for two different purposes is not naturally bundled in the ordinary course of business. Therefore, if a single rent deed is executed it will be treated as a service comprising entirely of such service which attracts highest liability of service tax. In this case renting for use as residence is a negative list service while renting for non-residence use is chargeable to tax. Since the latter category attracts highest liability of service tax amongst the two services bundled together, the entire bundle would be treated as renting of commercial property.

6.14.40.3 Significance of the condition that the rule relating to 'bundled service' is subject to the provisions of sub-section (2) of section 66F

Sub-section (2) of section 66 lays down **:** 'where a service is capable of differential treatment for any purpose based on its description, the most specific description shall be preferred over a more general description'. This rule predominates over the rule laid down in sub-section (3) relating to 'bundled services'. In other words, if a bundled service falls under a service specified by way of a description then such service would be covered by the description so specified. The illustration, relating to a bundled service wherein a pandal and shamiana is provided in combination with catering service, given in the second bullet in para 9.1.2 above explains the operation of this rule.

6.14.40.4 Manner of determining if the services are bundled in the ordinary course of business

Whether services are bundled in the ordinary course of business would depend upon the normal or frequent practices followed in the area of business to which services relate. Such normal and frequent practices adopted in a business can be ascertained from several indicators some of which are listed below –

- The perception of the consumer or the service receiver. If large number of service receivers of such bundle of services reasonably expect such services to be provided as a package then such a package could be treated as naturally bundled in the ordinary course of business.
- Majority of service providers in a particular area of business provide similar bundle of services. For example, bundle of catering on board and transport by air is a bundle offered by a majority of airlines.
- The nature of the various services in a bundle of services will also help in determining whether the services are bundled in the ordinary course of business. If the nature of services is such that one of the services is the main service and the other services combined with such service are in the nature of incidental or ancillary services which help in better enjoyment of a main service. For example service of stay in a hotel is often combined with a service or laundering of 3-4 items of clothing free of cost per day. Such service is an ancillary service to the provision of hotel accommodation and the resultant package would be treated as services naturally bundled in the ordinary course of business.

Other illustrative indicators, not determinative but indicative of bundling of services in ordinary course of business are –

- There is a single price or the customer pays the same amount, no matter how much of the package they actually receive or use.
- The elements are normally advertised as a package.
- The different elements are not available separately.
- The different elements are integral to one overall supply – if one or more is removed, the nature of the supply would be affected.

No straight jacket formula can be laid down to determine whether a service is naturally bundled in the ordinary course of business. Each case has to be individually examined in the backdrop of several factors some of which are outlined above.

When two or more rules may appear equally applicable then rule that occurs later among the rules preferable.

6.15 VALUATION OF TAXABLE SERVICES (Section 67)

Section 67 provides for valuation of taxable services provided by different service providers for charging of the service tax. Determination of value of services for all type of services should be made as per the provisions of this section and guided by the principles followed for the valuation of excisable goods under Section 4 of the Central Excise Act, 1944.

Section 67 was substituted by the Finance Act, 2006 w.e.f. 18.4.2006. Unlike the erstwhile system of valuation of taxable services based on gross amount charged subject to some exclusions and inclusions, the new valuation norms provide for a three tier valuation mechanism and for the first time in service tax legislation, provisions for valuation of non-monetary consideration is being provided for. The valuation of services shall be done three fold as under -

(i) Where the provision of service for such consideration in money	Gross amount charged by this for service provider services provided or to be provided
(ii) Where the provision of service is consideration not wholly or partly consisting of money (i.e. partly in cash, partly in kind)	Amount of money with addition of service tax, equivalent to the consideration
(iii) Where the provision of service is consideration which is not ascertainable	Amount as may be determined in prescribed manner

6.15.1 Determination of Value

The value of taxable service means, the gross amount received by the service provider for the taxable service provided or to be provided by him. Taxable value has to be determined as per the provisions of the Section 67 of the Finance Act, 1994 read with Service Tax (Determination of Value) Rules, 2006.

According to CBEC Letter No. B1/4/2006-TRU dated 19.04.2006, section 67 provides for valuation of taxable services for charging service tax. The salient features of the new section 67 are-

- Where the consideration received for provision of services is wholly in money, the value shall be the gross amount charged by the service provider for provision of service.
- Where the consideration received for provision of service is not wholly consisting of money, the value in such cases shall be the gross amount charged by the service provider for provision of similar service to any other person in the ordinary course of trade.
- If the value of similar service provided by the same service provider is not available, then the value has to be determined.
- Money value of non-money consideration received should be determined by the service provider.
- If the consideration received is not wholly consisting of money, equivalent money value of the consideration determined by the service provider shall be the taxable value for charging service tax.
- If the consideration received is partly in money and partly in non-money terms, the sum of consideration received in money and the equivalent money value of the non-money consideration determined by the service provider shall be the taxable value for charging service tax.
- The taxable value shall be determined by the service provider but the value so determined for the purpose of paying service tax should not be less than the cost of provision of such service.

The section 67 and the rules notified for this purpose enable charging of service tax in cases where the consideration received is not in money terms. Where the service tax is charged on the basis of similar services provided by the same person, the same should be based on a normal transaction between two independent persons at an arm's length price.

It was further clarified that in view of the comprehensive provisions on value of taxable services, all the circulars issued relating to value of taxable services are withdrawn. This has been further reteriated vide Circular No. 93/04/2007 dated 10-5-2007 stating that certain portion of various circulars relate to issue of valuation of taxable services. Any such portion, which is inconsistent with the Service Tax (Determination of Value) Rules, 2006 stand withdrawn w.e.f. 19-4-2006 vide para 4,1.13 of Instruction No. B1/4/2006-TRU, dated 19-4-2006. Therefore, in all cases, the value of a taxable services is to be determined strictly in terms of the Service Tax (Determination of Value) Rules, 2006 read with section 67 of the Finance Act, 1994.

Normally, the “value of taxable service” means, the gross amount received by the service provider for the taxable service provided or to be provided by him. Section 67 of the Finance Act, 1994 read with Service Tax (Determination of Value) Rules, 2006, has to be followed to arrive at the taxable value.

For certain services, a specified percentage of abatement is allowed from the gross amount collected for rendering the services, subject to the conditions, inter alia, that Cenvat Credit has not been availed by the service provider and cost of goods sold in the process of providing the subject service is not deducted in terms of Notification No. 12/2003-ST, dated 20.6.2003. (Since rescinded w.e.f. 1-7-2012 vide Notification No. 34/2012-ST, dated 20.6.2012)

Exemption to Education Cess Vide Circular No. 134/3/2011-ST -- F. No. 354/42 2011-TRU, dated 8.4.2011, CBEC has issued directions for not initiating proceedings to recover education cess and secondary & higher education cess where ‘whole of service tax’ stands exempted under any Notification. Similarly, where education cess has been refunded to exporters alongwith service tax by virtue of exemption notification where ‘whole of service tax’ is exempt, the same need not be recovered.

The Circular states as follows-

1. Representations have been received from the field formations, seeking clarification regarding the applicability of service tax exemption to Education Cess (refers to both Education Cess leviable under Finance (No.2) Act, 2004 and Secondary and Higher Education Cess leviable under Finance Act, 2007), under notifications where ‘whole of service tax’ stands exempted. Apparently the doubt arises in the context of Tribunal’s Order in the matter of M/s. Balasore Alloys Ltd. v. CCE, Customs and Service Tax, BBSR-I (2010-TIOL-1659-CESTAT-KOL).

2. The issue has been examined. Though Tribunal’s Order referred above is in favor of revenue, it is inconsistent with the policy intention of the Government to exempt education cess in addition to service tax, where ‘whole of service tax’ stands exempted. According to section 95(1) of Finance (No.2) Act, 2004 and section 140(1) of Finance Act, 2007, Education Cess and Secondary and Higher Education Cess are leviable and collected as service tax, and when whole of service tax is exempt, the same applies to education cess as well, Since Education Cess is levied and collected as percentage of service tax, when and wherever service tax is NIL by virtue of exemption, Education Cess would also be NIL.

3. This being the principle, field formations are directed not to initiate proceedings to recover the education cess, where ‘whole of service tax’ stands exempted under the notification. Extending the same principle, where education cess has been refunded to exporters along with service tax, by virtue of exemption notifications where ‘whole of service tax’ is exempt, the same need not be recovered”.

Following terms have been explained in Section 67 by way of an Explanation-

(i) “consideration” includes any amount that is payable for the taxable services provided or to be provided;

(ii) any reimbursable expenditure or cost incurred by the service provider and charged, in the course of providing or agreeing to provide a taxable service, except in such circumstances, and subject to such conditions, as may be prescribed;

(iii) any amount retained by the lottery distributor or selling agent from gross sale amount of lottery ticket in addition to the fee or commission, if any, or, as the case may be, the discount received, that is to say, the difference in the face value of lottery ticket and the price at which the distributor or selling agent gets such ticket.

As per Explanation (a) to section 67 of the Act "consideration" includes any amount that is payable for the taxable services provided or to be provided.

Since this definition is inclusive it will not be out of place to refer to the definition of 'consideration' as given in section 2 (d) of the Indian Contract Act, 1872 as follows-

"When, at the desire of the promisor, the promisee or any other person has done or abstained from doing, or does or abstains from doing, or promises to do or to abstain from doing, something, such act or abstinence or promise is called a consideration for the promise".

In simple terms, 'consideration' means everything received or recoverable in return for a provision of service which includes monetary payment and any consideration of non-monetary nature or deferred consideration as well as recharges between establishments located in a non-taxable territory on one hand and taxable territory on the other hand.

According to CBEC Letter No. 334/1/2012-TRU dated 16.3.2012, the definition of 'consideration' as given in the Indian Contract Act, 1872 can safely be adopted to understand the concept of consideration. When so applied to the Act, 'consideration' for a service provided or agreed to be provided by service provider would mean anything which the service receiver or any other person has done or abstained from doing, or does or abstain from doing, or promises to do or to abstain from doing for receiving the service.

In Commission of European Communities v. French Republic (2012) 36 STT 690 (ECJ), it was held that gratuities or voluntary tips paid by the customer spontaneously and directly to employees as a token of satisfaction of service, over and above the service charges are not includible in taxable value.

Tips or service charges are compulsory price supplements which are included in the total price charged to the customer and which are generally borne by the customer by way of remuneration for the 'service provided in certain establishments', i.e. 'service charge'. A service charge is to be distinguished from gratuities or voluntary tips paid by the customer spontaneously and directly to employees of the establishment in question as a token of his satisfaction, over and above the service charge itself.

The consideration received or receivable by the supplier for the provision of a service, which constitutes the taxable amount arising from that operation, must be capable of being expressed in terms of the consideration actually received for it, which is a subjective value and not a value estimated according to objective criteria. The consideration must be capable of being expressed in money.

In Apple and Pear Development Council vs. Commissioner of Customs & Excise (2012) 36 STT 678 (ECJ), it was held that for the provision of services to be taxable, there must be a direct link between the service provided and the consideration received. Concept of supply of services effected for consideration presupposes the existence of a direct link between the service provided and the consideration received.

Following are the implications of the condition that activities should be carried out for a consideration'-

- To be taxable an activity should be carried out by a person for another for a 'consideration'.
- Activity carried out without any consideration like donations, gifts or free charities are therefore outside the ambit of service. For example grants given for a research where the researcher is under no obligation to carry out a particular research would not be a consideration for such research.
- An act by a charity for consideration would be a service and taxable unless otherwise exempted.

- Conditions in a grant stipulating merely proper usage of funds and furnishing of account also will not result in making it a provision of service.
- Donations to a charitable organization are not consideration unless charity is obligated to provide something in return e.g. display or advertise the name of the donor in a specified manner or such that it gives a business advantage to the donor.

Monetary consideration means any consideration received in the form of money. 'Money' includes not only cash but also cheque, promissory note, bill of exchange, letter of credit, draft, pay order, traveller's cheque, money order, postal or electronic remittance or any such similar instrument when used as consideration to settle an obligation.

Non-monetary consideration could be in the form of following:

- Supply of goods and services in return for provision of service
- Refraining or forbearing to do an act in return for provision of service
- Tolerating an act or a situation in return for provision of a service
- Doing or agreeing to do an act in return for provision of service

The non-monetary consideration also needs to be valued for determining the tax payable on the taxable service since service tax is levied on the value of consideration received which includes both monetary consideration and money value of non-monetary consideration.

The value of non-monetary consideretion is determined as per section 67 of the Act and the Service Tax (Determination of Value) Rules 2006, which is equivalent money value of such consideration and if it is not ascertainable, then as follows:-

- On the basis of gross amount charged for similar service provided to other person in the ordinary course of trade;
- Where value cannot be so determined, the equivalent money value of such consideration, not less than the cost of provision of service.

CBEC Guidance Note dated 20-6-2012 also clarifies on certain payments as to whether such payments could be considered as 'consideration' as follows-

Sl. No.	Nature of payment	Whether consideration for service?
1.	Amount received in settlement of dispute.	Would depend on the nature of dispute. Per se such amounts are not consideration unless it represents a consideration for an activity that has been carried out. If the dispute itself pertains to consideration relating to service then it would be a part of consideration.
2.	Amount received as advances for performance of service.	Such advances are consideration for the agreement to perform a service.
3.	Deposits returned on cancellation of an agreement to provide a service.	Returned deposits are in the nature of a returned consideration. If tax has already been paid the tax payer would be entitled to refund to the extend specified subject to provisions of law in this regard.
4.	Advances forfeited for cancellation of an agreement to provide a service.	Since service becomes taxable on an agreement to provide a service such forfeited deposits would represent consideration for the agreement that was entered into for provision of service.

5.	Security deposit that is returnable on completion of provision of service.	Returnable deposit is in the nature of security and hence do not represent consideration for service. However, if the deposit is in the nature of a colourable device wherein the interest on the deposit substitutes for the consideration for service provided or the interest earned has a perceptible impact on the consideration charged for service then such interest would form part of gross amount received for the service. Also security deposit should not be in lieu of advance payment for the service.
6.	Security deposits forfeited for damages done by service receiver in the course of receiving a service	If the forfeited deposits relate to accidental damages due to unforeseen actions not relatable to provision of service then such forfeited deposits would not be a consideration in terms a clause proposed to be inserted in rule 6 of the Valuation Rules.
7.	Excess payment made as a result of a mistake	If returned it is not consideration. If not returned and retained by the service provider it becomes a part of the taxable value.
8.	Demurrages payable for use of services beyond the period initially agreed upon e.g. retention of containers beyond the normal period.	This will be consideration and is covered by clause (x) of sub-rule (1) to Rule 6 of the Valuation Rules.

Following points are also relevant -

- To be taxable an activity should be carried out by a person for a 'consideration'
- Activity carried out without any consideration like donations, gifts or free charities are therefore outside the ambit of service. For example grants given for a research where the researcher is under no obligation to carry out a particular research would not be a consideration for such research.
- An act by a charity for consideration would be a service and taxable unless otherwise exempted.
- Conditions in a grant stipulating merely proper usage of funds and furnishing of account also will not result in making it a provision of service.
- Donations to a charitable organization are not consideration unless charity is obligated to provide something in return e.g. display or advertise the name of the donor in a specified manner or such that it gives a desired advantage to the donor.

The consideration for a service may be provided by a person other than the person receiving the benefit of service as long as there is a link between the provision of service and the consideration. For example, holding company may pay for services that are provided to its associated companies.

The consideration for a service may be provided by a person other than the person receiving the benefit of service as long as there is a link between the provision of service and the consideration. For example, holding company may pay for works contract service or architect services that are provided to its associated companies.

In Mahabola Mannur vs. CCE 2011 (22) STR. 419 (CESTAT, Bangalore), it was held that the interpretation of gross amount charged by the appellant is not in line with the provisions of law. Section 67 clearly provides that for calculating value of a service, consideration in monetary as well as non-monetary terms are required to be taken into account and where consideration is not ascertainable, it has to be determined in the prescribed manner as per Service Tax (Determination of Value on Rules), 2006. Exclusions of value of materials supplied by service recipient is not available under Section 67 of Finance Act, 1994 after amendment from 18-4-2006.

'Money has been defined to include all forms of money except the currency that is held for its numismatic value. It will include any -

- Currency
- Cheques
- promissory notes
- letter of credit
- draft
- pay orders
- traveller's cheque
- money order
- postal remittance (order)
- any other similar instrument.

Any other similar instrument is a residual entry which will cover all types of bills of exchange, hundi, cash in transit etc., but not goods for value of money.

Finance Act, 2012 has, however, omitted the above definition of money as provided in explanation (b) to section 67. However, a new definition of 'money' has been provided in clause (33) to section 65B (w.e.f. 1-7-2012) which reads as under -

"money" means legal tender, cheque, promissory note, bill of exchange, letter of credit, draft, pay order, traveller's cheque, money order, postal or electronic remittance or any similar instrument but shall not include any currency that is held for its numismatic value;

The new definition is a much wider definition. Readers may also refer to Topic No. 36 of the Book.

Gross amount charged has been defined to include payments by way of -

(i) cheque

(ii) credit card

(iii) deduction from account

(iv) any form of payment by issue of credit notes or debit notes and book adjustments

(v) any amount credited or debited to any account, whether called suspense account or other account, in the book of person liable to pay tax, in case of a transaction with associated enterprise.

The gross amount charged for the taxable service shall include any amount received towards the taxable service before, during or after the provision of taxable service.

Cheque does not mean only a cheque but would cover all such similar instruments. Credit cards would also include other payment or charge cards. The most concerning items in the aforementioned definition is any form of payment by issue of credit note or debit note and book adjustments. This will not only create lots of confusion but also be a subject matter of dispute between department and the assessee. It is a common practice to issue debit notes or credit notes or to do book adjustments for any reason and it is not necessary that such note on adjustment would tantamount to payment. For example, a service provider raises a bill on the service receiver for ₹10000 but he finally settles the bill for ₹8000 only and while final settlement takes place, he raises a credit note on him. Such notes may not be considered as payment or gross amount charged.

6.15.2 Date of determination of rate of tax, value of taxable service and value of exchange [Section 67A]

New section 67A has been inserted by the Finance Act, 2012 to provide for:

(a) date of determination of rate of tax,

(b) value of taxable service, and

(c) rate of exchange (as referred in section 14 of Customs Act, 1962)

This will be effective from 1-7-2012.

The provisions of section 67A reads as follows -

The rate of service lax, value of a taxable service and rate of exchange, if any, shall be the rate of service tax or value of a taxable service or rate of exchange, as the case may be, in force or as applicable at the time when the taxable service has been provided or agreed to be provided".

It provides that value of taxable services (particularly in case of import, and export of taxable services) and the rate of tax shall be determined in terms of Point of Taxation Rules, 2011. Accordingly, date, value and rate of exchange, as the case may be, shall be as in force or as applicable at the time when taxable service has been provided or agreed to be provided.

"Rate of Exchange" means the rate of exchange determined in accordance with such rules as may be precribed.

Cum Tax Value

Section 67(2) provides that where the gross amount charged by the service provider for the taxable services provided or to be provided is inclusive of service tax payable, the value of taxable service in such case shall be the amount as with the addition of service tax payable, is equal to the gross amount charged.

In such cases, gross value of taxable service shall be considered as inclusive of service tax. Also, as per Section 67(3), gross amount charged for taxable service shall include any amount received towards the taxable service before, during or after the rendering of such service. A similar provision existed in earlier provisions of Section 67.

In Robot Detective & Security Agency GCE Chennai vs. CCE, Cheenai (2009) 16 STJ 305; (2009) 14 STR 689; (2009) 20 STT 42 (CESTAT, Chennai), where assessee was providing taxable services and charged gross value without indicating the service tax element separately, it was held that taxable value realized has to be treated as inclusive of service lax due and that service tax liability was to be redetermined.

In CCE & C vs. Advantage Media Consultant (2008) 14 STJ 172 (CESTAT Kolkata), it was held that when no tax is collected separately, the gross amount has to be adopted to quantify the tax liability treating it as a value of taxable service plus service tax payable.

In Turret Industrial Security Pvt. Ltd vs. CCE (2008) 18 VST 348; (2009) STR 564 (CESTAT,Kolkata) where the assessee had not collected service tax separately from its clients, it was held that the value of services received from such clients has to be taken as the value plus tax and accordingly, a bifurcation has to be done to determine the tax amount payable on such receipts.

In Shakti Motors vs. CST, Ahmedabad (2008) 12 STR 710 (CESTAT, Ahmedabad) it was held that in terms of section 67(2) of the Finance Act, 1994, if invoice specifically does not say that gross amount charged includes service tax, it can not be treated as cum service tax price. Cum tax benefit is not extendable in absence of evidence to show that invoice is prepared in this manner.

In Multi Mantec International Pvt. Ltd. vs. CST Ahmedabad (2008) 15 STJ 251 (CESTAT, Ahmedabad), it was held that when price is inclusive of taxes, it would mean that all taxes have been collected, unless otherwise provided through specific evidence.

P. Sugumar vs. CCE, Pondicherry (2009) 23 STT 173 (CESTAT Chennai), where assessee had not received any separate amount towards service tax, it was held that gross amount received by him should be taken as cum- tax value and tax amount was to be recalculated.

In Mackintosh Burn Ltd vs. CST, Kolkata (2010) 19 STR 682 (CESTAT, Kolkata), it was held that where separate bills were raised on customers, mere non payment by customer does not mean that service charges collected to be treated as cum-tax value and as such, cum-tax benefit was not permissible.

In BSNL vs. CCE. Jaipur-I (2011) 24 STR 435 (CESTAT, Delhi), where Service Tax could not be collected from customer though Service Tax was payable, it was held that demand was to be made out on the basis of cum tax value, i.e, amount received by service provider less tax payable. As such, demand amount would have to be reduced.

In National Refrigeration & Conditioning Engg. vs, CCE, Ludhiana (2011) 33 STT 154 (CESTAT, New Delhi), it was held that since assessee had not charged service tax separately, the assessee was entitled to cum-tax benefit.

In Kopran Ltd vs. CCE, Raigad (2011) 331 STT 228(CESTAT, Mumbai), it was affirmed that when no service tax is collected separately, gross amount has to be adopted to quantify tax liability, treating it as value of service plus service tax payable. The assessee was entitled to deduct service tax from gross amount charged, for arriving at taxable value of service [Also see CCE vs. Advantage Media Consultant (2008) 14 STT 483 (CESTAT, Kolkata); Amrit Agro Industries Ltd vs, CCE (2007) 210 ELT 183 (SC); ABN Arnro Bank vs. CCE, Noida (2011) 23 STR 529 (CESTAT, New Delhi).

Book Adjustments

In business, the books most frequently referred to are the books of account in which business transactions are recorded. Books of account are normally considered to be legal documents. Books of account contain various accounts (say, debtors and creditors). Such accounts mean an account or register of debt or credit in a book. A "book account" means a book containing a statement in detail of the transactions between parties, including prices, made contemporaneously with the transaction, and entered in a book.

Adjustment in finance and accounts means to correct figures or make allowances for charges, credits etc. It involves alteration in debit or credit balances by way of allowances or charges posted in an account by means of debit or credit notes. It is a process of adjusting financially the sums due or owed. Such adjustments are done by way of adjusting entries by way of journal entries without directly affecting the cash flows. Such adjustments are absolutely legal and an universally accepted accounting practice.

According to Dictionary of Accounting Terms, 'adjustment' means --

(a) increase or decrease to an account resulting from an adjusting journal entry. For example, the accrual of wages at year-end will cause an increase in both salary expense and salary payable.

(b) changing an account balance because of some happening or event. For example, a customer who returns merchandise will receive a credit adjustment to the account.

According to Black's Law Dictionary, 8th edition 2004, 'suspense account' means temporary record used in book keeping to track receipts and disbursements or an uncertain nature until they are identified and posted in the appropriate ledgers and journals. A suspense account does not appear in a final financial statement. It is a useful tool when, for example, a lump-sum receipt or expenditure must be broken down to match several transactions before posting.

Suspense accounts are accounts of transactions which being impossible to enter in the normal books of accounts in a regular way for one reason or the other are thus required to be held in suspense for the time being. Suspense account is a temporary account that records part of a transaction before complete analysis of that transaction, or that records sums to correct errors.

In common parlance, it means an account in which the amount is held in deposit in favour of the person who remitted it and may be refunded in future, if the same is not appropriated or utilised for the purpose for which it was remitted. (LIC vs. Prasanana Devaraj, 1994 (2) KLT 541 at 545)

The expression 'suspense account' in the common parlance, means an account in which the amount is held in deposit in favour of the person who remitted it and may be refunded in future, if the same is not appropriated or utilised for the purpose for which it was remitted.

LIC of India vs. Prasanna Devraj, (1995) 82 Comp cases 611, 616 (Ker).

Suspense account is a temporary account in which entries of credits or charges are made until then proper disposition can be determined. Entries in suspense accounts are generally transitional. It is an account used temporarily to any doubtful receipts and disbursements or discrepancies pending their analysis and permanent classification.

Associated enterprises

CBEC has clarified as follows in respect of levy of service tax on transactions between associated enterprises vide Circular No. 334/112008-TRU dated 29.2.2008 -

Service tax is levied at the rate of 14.5% of the value of taxable services (section 66). Section 67 pertaining to valuation of taxable service for charging service tax states that value shall be the gross amount charged for the service provided or to be provided and includes book adjustment. As per rule 6 of the Service Tax Rules, 1994, service tax is required to be paid only after receipt of the payment.

It has been brought to the notice that the provision requiring payment of service tax after receipt of payment are used for tax avoidance especially when the transaction is between associated enterprises. There have been instances wherein service tax has not been paid on the ground of non-receipt of payment even though the transaction has been recognized as revenue/expenditure in the statement of profit and loss account for the purpose of determining corporate tax liability.

As an anti-avoidance measure, it is proposed to clarify that service tax is leviable on taxable services provided by the person liable to pay service tax even if the amount is not actually received, but the amount is credited or debited in the books of account of the service provider. In other words, service tax is required to be paid after receipt of payment or crediting/debiting of the amount in the books of accounts, whichever is earlier, llowever, this provision is restricted to transaction between associated enterprises. This provision shall also apply to service tax payable under reverse charge method (Section 66A) as taxable services received from associated enterprises. For this purpose section 67 and rule 6(1) are being amended.

The term 'associated enterprise' has the same meaning as assigned to it in section 92A of the Income Tax Act, 1961. It is a relative concept i.e. an enterprise is an associated enterprise when it is viewed in relation to other enterprises. This concept is used in the Income Tax Act for applying transfer pricing provisions. An enterprise which participates, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise is considered as associated enterprise. It also covers an enterprise in respect of which one or more persons who participate, directly or indirectly, or through one or more intermediaries, in the management or control or capital of the other enterprise.

Section 92A(2) of the Income Tax Act specifies various situations under which two enterprises shall be deemed to be associated enterprises. Enterprise means a person who is engaged in the provision of any services of any kind. For details, relevant provisions of Income Tax Act may be referred to."

Free Services (Services without Consideration)

Service Tax (Determination of Value) Rules, 2006 in rule 3 addresses the issue of determining the value of taxable service. It addresses two situations -- one where consideration is not wholly or partly in money and two, where consideration is not ascertainable. In both the cases, there must be some consideration, whether in money form or in non-ascertainable form. The valuation rules shall apply only when some consideration is received or given. There is no deeming provision in section 67 or the rules framed thereunder.

If there is no consideration, there is no value of taxable service or its value is nil and therefore, there cannot be any levy of service tax thereon [also see Chandravadan Desai vs. CCE, Calcutta-I (1998) 98 ELT 515 (CESTAT, Calcutta)]. The Tribunal held that section 67 does not have the concept of deeming provision of valuation of taxable service. The departmental appeal before Supreme Court was dismissed. [(1999) 105 ELT A 193 (Supreme Court)].

The definition of 'consideration' as explained in Section 67 is clear i.e., any amount that is payable for the taxable services provided. If no amount is paid (including past, present and future liability), there is no consideration involved. In general understanding, consideration means, something in return. It is an act or forbearance or its promise. Section 2(d) of Indian Contract Act, 1972 defines consideration to mean anything regarded as compensation or equivalent for what one does or undertakes for another's benefit.

The Service Tax (Determination of Value) Rules shall come into operation only when -

(i) Consideration is involved.

(ii) Consideration is partly in cash or partly in other than cash (say, kind).

(iii) Consideration is there but it is not ascertainable or cannot be determined.

(iv) All costs are not included in the value of taxable service and reimbursement of expenses are excluded from the value.

(v) Question of 'pure agent' has to be decided.

Notification No. 24/2012-ST, dated 1-7-2012 has amended valuation rules w.e.f 1-7-2012. Accordingly, in relation to works contracts, outdoor caterers and restaurant services, it has been provided that taxable value will include fair market value of all goods and services supplied.

Supreme Court's View on Valuation of Services

Supreme Court has held that section 67 of the Finance Act, 1994 does not have the concepts of deeming provision of valuation of taxable service. Following is the summary of the order-

The Supreme Court Bench on 16.11.1998 dismissed the Civil Appeal No, 3188 of 1998 filed by Commissioner of Central Excise, Calcutta against the CEGAT Order No.S/628/A-1168/CAL/97 dated 3.9.1997 and reported in 1998 (98) E.L.T 515 (Tribunal) (Chandravadan Desai vs. Commissioner).

The Appellate tribunal in its order in question had held that ex facie there was no allegation in the order of the Superintendent of Central Excise, Service Tax Cell that he resorted to the best judgment under Section 72 of the finance Act, 1994. The order was also not mentioning that the accounts of assessee was rejected as incorrect or incomplete. It was also not given in the order that on what basis the Superintendent has stated that the brokerage must be charged in all cases and there was no free service provided by a stock broker at all having regard to the practice of the trade. The tribunal also held that Section 67 of the said Finance Act relating to service tax does not have the concept of deeming provision of valuation of taxable service. In the circumstances the Tribunal held that the authorities below have not prima facie passed a correct order and allowed the Stay Petition unconditionally.

In Federation of Hotel and Restaurant association of India vs. Union of India (1989) 178 ITR 97 (Supreme Court), it was held that the subject of a tax is different from the measure of the levy. The measure of the tax is not determinative of its essential character or of the competence of the legislature. Following this, in Tamil Nadu Kalyana Mandapam Owners' Association v. Union of Indio and Others (2002) 253 ITR 250 Madras High Court held that there can be no dispute that section 67(1) is nothing but the measure of the tax which can not be considered while considering the true nature of the tax.

In C. K. Jidheesh v. Union of India (2005) 3 STJ 985 (Supreme Court), where the explanation to Section 67 only exempted the cost of unexposed films during the course of providing the service, in case of photography services, service tax on which was levied w.e.f. 16th July, 2001 vide Notification No. 4/2001-ST dated 9.7.2001, a clarificatory Circular (No. F No. B11/1/2001 TRU dated 9.7.2001) was also issued by TRU of Ministry of Finance, clarifying various issues in relation to levy of service tax in respect of new services taxed in the Finance Act, 2001. The Circular being challenged in the subject writ petition stated that the value of taxable service is the gross amount charged from the customer for the service rendered. However, the cost of unexposed photography films sold to the customer is excluded. The service provider claiming benefit of the cost of film should he advised to show them clearly on the invoices along with description and particulars of the film. Otherwise, the claim will not be considered as admissible. No other cost (such as photographic paper, chemicals, etc.) is excluded from the taxable value.

The court observed that while the challenge is to letter dated 09.07.2001 issued by Ministry, the real challenge is to amendment in the Finance Act. That letter under question only clarifies what amended section 67 provides for. A mere challenge to such a clarificatory letter is not enough and the challenge has to be to the provisions of the Act. Such a challenge to the statutory provisions was made in Kerala Colour Lab Association v Union of India (2002) 168 Taxation 563 (Kerala), where in it was held that levy of service tax on photography services does not impose any unreasonable restriction on the fundamental right and was held to be constitutionally valid. The Petitioner has also challenged the discriminatory altitude of the Respondent in levying service tax on gross receipts in photographic business when on other pure service providers like stock brokers, travel agent etc, the tax is levied only on the commission. On the issue of discrimination in levying the service tax on gross receipts, it was held that there is no discrimination. Such cases were contracts of service, pure and simple. In other cases, there is a bifurcation because service is provided and goods are sold.

In Bharat Sanchar Nigam Ltd. v. Union of India (2005) 4 STJ (Supreme Court), it was held that the aspect theory would not apply to enable the value of the services to be included in the sale of goods or the price of goods in the value of the services. The value of services cannot be included in the meaning of goods. In a telecom service, what could comprise as a sale is the sale of handset only and not the service component.

Free Supply of Goods

Valuation of taxable services covers gross amount charged or collected from service receiver against a service which also, includes monetary equivalent of non-monetary consideration.

According to section 67 of Finance Act, 1994 as amended and Service Tax (Determination of Value) Rules, 2006, gross amount is chargeable to service tax. The inclusion of money value of free supplies of items in taxable value of services rendered is consistent with intention of legislative as reflected in the language of Act and Valuation Rules. If this value is not included, the assessee will also not get the benefit of exemption under Notification No. 1/2006 or 12/2003, as the case may be.

Receipt of free supply of items by a manufacturer is similar to receipt of materials free of cost by a service provider, as both the manufacturer and the service provider will have to otherwise incur cost of these items to produce excisable goods or to render taxable service. In both the cases, receipt of free supply of materials does not yield any additional return to the assessee. However, it is well recognized that for the purpose of section 4 of the Central Excise Act, free supply of items constitutes additional consideration received by a manufacturer. Therefore, inclusion of money value of free supply on items in the taxable value of the-service rendered is consistent with the intention of the Legislature as reflected in the language of the Act as well as the Service Tax (Determination of Value) Rules, 2006. In a case where the service recipient does not provide such items to the service provider, the assessee will include the value of the materials used in rendering the taxable service and charge the same from the client. The assessee cannot exclude the value of these material in computing the taxable value. The Commissioner rightly relied on the judgment of Supreme Court in Burn Standard Co. Ltd v. Union of India (1992) 60 ELT 671 wherein it was held that value of free supply of items was includible in the assessable value under section 4 of Central Excise Act. (Refer VPR Mining Infrastructure Pvt. Ltd v. CCE, Hyderabad (2011) 32 STT 1; (2011) 23 STR 279 (CESTAT, Bangalore).

Notification No. 24/2012-ST, dated 1-7-2012 has amended valuation rules w.e.f 1-7-2012. Accordingly, in relation to works contracts, outdoor caterers and restaurant services, it has been provided that taxable value will include fair market value of all goods and services supplied.

Gross Value - Some Points to be Noted

(i) Service tax is chargeable on gross value of taxable services rendered as determined in terms of Service Tax (Determination of Value) Rules, 2006.

(ii) Where gross amount charged is inclusive of service tax, value of taxable service shall be an amount which with addition of service tax would be equal to gross amount charged.

(iii) Services provide free (without any consideration) shall not attract any service tax as value will be nil.

(iv) Gross amount charged includes amounts received before, during and after the provision of taxable service.

(v) Gross amount would include payment by cheque, credit card, deduction from account, credit notes, debit notes, book adjustments and amounts debited or credited to any account including suspense account in case of transactions with associated enterprises.

(vi) Gross consideration would include reimbursement of expenses unless incurred by a pure agent on behalf of the client.

(vii) Value of taxable service is total amount of consideration whether split into various components or not.

(viii) Value of goods and material supplied will not be included in the gross amount charged except in case of works contract/outdoor catering/restaurant services (Refer Notification No. 24/2012-ST, dated 6-6-2012).

(ix) Gross value of taxable services and service tax should be indicated in invoices.

(x) Abatements, if any allowed, are to be calculated on the gross amount charged.

(xi) TDS is to be deducted on gross amount charged.

(xii) Value of taxable services will exclude Sales tax, VAT etc.

(xiii) Service tax returns should indicate gross amount charged for all taxable services.

(xiv) Only gross value of taxable service determines the liability of service tax.

(xv) CENVAT credit should be taken before depositing service tax on value of taxable service.

In Quadrant Communication Ltd. v. CCE, Pune III (2012) 26 STR 33 (CESTAT, Mumbai), it was held that appellant was liable to pay service tax on the gross amount charged from the clients in respect of advertising services rendered. The value added tax practiced in India is on "invoice basis". The service tax liability has to be discharged on the gross amount charged to the client and the service provider can avail Service Tax/excise duty paid on the inputs or input services used in or in relation to the provision of output. Rule 5 of the Service Tax (Determination of Value) Rules, 2006 makes it abundantly clear that where any expenditure or costs are incurred by the service provider in the course of providing taxable service, all such expenditure or costs shall he treated as consideration for the taxable service provided and shall be included in the value for the purpose of charging service tax on the said service.

6.15.3 Valuation w.e.f. 1.7.2012

With the introduction of system of taxation of services based on the negative list there has been no fundamental change in the manner of valuation of service for the purpose of payment of service tax. The broad scheme remains the same barring some marginal changes carried out to align the scheme of valuation of taxable services and the Service Tax (Determination of Value) Rules, 2006 with the new system of taxation, Broadly these changes in the Valuation Rules are as follows:-

(i) As compared to the existing two schemes for valuation of works contract services - one under the rule 2A of the Valuation Rules and second under the Works Contract (Composition Scheme for Payment of Service Tax) Rules 2007 has been replaced with a unified scheme under the new rule 2A of Service Tax (Determination of Value) Rules, 2006.

(ii) A new Rule 2C has been inserted for determining the value of service involved in supply of food or any other article of human consumption or any drinks in a restaurant or as outdoor catering. The existing scheme of determination of value of such services through prescribed abatements in various exemption notifications has been done away with.

(iii) There are certain changes in rule 6 of the Service Tax (Determination of Value) Rules, 2006.

(iv) All notifications that prescribed the abatements for working out the taxable value from the gross amount charged have been merged into one single exemption notification i.e., Notification No. 26/2012- ST dated 20/6/12.

The manner of value of service is provided in Section 67. As per sub-section (1) of Section 67 wherever Service Tax is chargeable on any taxable service with regard to its value then its value shall -

(i) in a case where the provision of service is for a consideration in money, be the gross amount charged by the service provider for such service provided or to be provided by him;

(ii) in a case where the provision of service is for a consideration not wholly or partly consisting of money, be such amount in money as, with the addition of service tax charged, is equivalent to the consideration;

(iii) in a case where the provision of service is for a consideration which is not ascertainable, be the amount as may be determined in the prescribed manner.

There may be several situations wherein it may be difficult to determine the consideration received by service provider for provision of a service. Such situations can arise on account of several factors such as consideration of service being embedded in the total amount received as consideration for a composite activity involving elements of provisions of service and element of sale of goods or consideration for service being included in the gross amount charged for a particular transaction or consideration of service being wholly or partly in the nature of non-monetary consideration.

The manner has been prescribed under Service Tax (Determination of Value) Rules 2006. These rules inter-alia provide provisions in respect of the following situations:

(i) Determination of value of service portion involved in execution of works contract.

(ii) Determination of value of service in relation to money changing.

(iii) Determination of value of service portion involved in supply of food and any other article of human consumption or any drinks in a restaurant or as outdoor catering.

(iv) Determination of value where such value is not ascertainable.

(v) The said rules also specify certain expenditures or costs that are incurred by the service provider which have to be included or excluded

(vi) The said rules also specify certain commissions or costs that are received by the service provider that have to be included or excluded while arriving at the taxable value.

In addition to the Service Tax (Determination of Value) Rules 2006, certain sub-rules in rule 6 of the Service Tax Rules, 1994 also provide simplified compounded mechanism for determination of value of taxable services in specified situations.

6.15.4 Determination of value under the Service Tax (Determination of Value) Rules, 2006 - Notification No. 12/2006-S.T., dated 19-4-2006 as amended :

The Service Tax (Determination of Value) Rules, 2006 has been notified vide Notification No. 12/2006-S.T., dated 19-4-2006. The said Rule has been amended from time to time. The salient features of changes made to the said Rules of 2006 are as follows :

(i) The Works Contract (Composition Scheme for Payment of Service Tax) has been merged into valuation of works contract service in rule 2A vide Notification No. 24/2012-S.T., dated 6-6-2012 and Notification No. 11/2014-S.T., dated 11-7-2014 w.e.f. 1-10-2014.

(ii) The new rule 2C is for determining the value of service involved in supply of food or any other article of human consumption or outdoor catering.

(iii) There are changes in rules 3, 5 and 6.

(iv) Rule 7 has been omitted.

(v) All notifications that prescribed the abatements for working out the taxable value from the gross amount charged have been merged into one single Notification No. 26/2012-S.T., dated 20-6-2012.

(A) Determination of value of taxable services involved in execution of works contract - Rule 2A of the Rules of 2006 as substituted vide Notification No. 24/2012-S.T., dated 6-6-2012 w.e.f. 1-7-2012 and amended Notification No. 11/2014-S.T., dated 11-7-2014 :

Rule 2A, as substituted vide Notification No. 24/2012-S.T., dated 6-6-2012, stipulates about determination of value of service portion in the execution of a works contract. Subject to the provisions of section 67, the value of service portion in the execution of a works contract, referred to in clause (h) of section 66E of the Act, shall be determined in the following manner.

(i) Value of service portion in the execution of a works contract shall be equivalent to the gross amount charged for the works contract less the value of property in goods transferred in the execution of the said works contract. When 'A' states that the gross amount charged for the works contract is ₹ 20 lakhs, the value of property in goods which is say ₹ 15 lakhs shall have to be excluded from the declared value of works contract of ₹ 20 lakhs. The explanation provides to exclude the value added tax or as the case may be sales tax from the said value of works contract but the value has to include the cost incurred in execution of works contract.

The Provisions are as below :

Explanation. - For the purposes of this clause,-

(a) gross amount charged for the works contract shall not include value added tax or sales tax, as the case may be, paid or payable, if any, on transfer of property in goods involved in the execution of the said works contract; but the value of works contract service shall include, -

(i) labour charges for execution of the works;

(ii) amount paid to a sub-contractor for labour and services;

(iii) charges for planning, designing and architect's fees;

(iv) charges for obtaining on hire or otherwise, machinery and tools used for the execution of the works contract;

(v) cost of consumables such as water, electricity, fuel used in the execution of the works contract;

(vi) cost of establishment of the contractor relatable to supply of labour and services;

(vii) other similar expenses relatable to supply of labour and services; and

(viii) profit earned by the service provider relatable to supply of labour and services;

Where value added tax or sales tax has been paid or payable on the actual value of property in goods transferred in the execution of the works contract, then, such value adopted for the purposes of payment of value added tax or sales tax, shall be taken as the value of property in goods transferred in the execution of the said works contract for determination of the value of service portion in the execution of works contract under this clause.

(ii) Where the value has not been determined in the manner explained supra, the person liable to pay tax on the service portion involved in the execution of the works contiact shall determine the service tax payable in the following manner, namely :-

(A) in case of works contracts entered into for execution of original works, service tax shall be payable on forty per cent, of the total amount charged for the works contract;

(B) in case of works contracts, not covered under sub-clause (A), including works contract entered into for,-

(i) maintenance or repair or reconditioning or restoration or servicing of any goods,

(ii) maintenance, repair, completion and finishing services such as glazing or plastering or floor and wall tiling or installation of electrical fittings of an immovable property;

Service tax shall be payable on seventy per cent, of total amount charged for the works contract.

The explanation has defined the terms 'original works', 'total amount' and not availing Cenvat credit as specified below:

Explanation 1. - For the purposes of this rule,-

(a) "original works" means-

(i) all new constructions;

(ii) all types of additions and alterations to abandoned or damaged structures on land that are required to make them workable;

(iii) erection, commissioning or installation of plant, machinery or equipment or structures, whether pre-fabricated or otherwise;

(b) "total amount" means the sum total of the gross amount charged for the works contract and the fair market value of all goods and services supplied in or in relation to the execution of the works contract, whether or not supplied under the same contract or any other contract, after deducting-

(i) the amount charged for such goods or services, if any; and

(ii) the value added tax or sales tax, if any, levied thereon :

Provided that the fair market value of goods and services so supplied may be determined in accordance with the generally accepted accounting principles.

Explanation 2. - For the removal of doubts, it is clarified that the provider of taxable service shall not take CENVAT credit of duties or cess paid on any inputs, used in or in relation to the said works contract, under the provisions of CENVAT Credit Rules, 2004.

The non-availability of Cenvat is in relation to the work contract and not service portion of the work contract.

(B) Determination of value of service in relation to money changing - Rule 2B :

Rule 2B was inserted vide Notification No. 2/2011-S.T., dated 1-3-2011 w.e.f. 1-4-2011 and further amended by Notification No. 24/2012-S.T. omitting the words, brackets, letters and figures "referred to in sub-clauses (zm) and (zk) of clause (105) of section 65 of the Act". The value of taxable service in relation to purchase and sale of foreign currency including money changing shall be determined by the service provider in the following manner :

1. For a currency, when exchanged from or to Indian Rupees, the value shall be equal to the difference in buying rate or selling rate, as the case may be, and the Reserve Bank of India reference rate of that currency at that time, multiplied by total units of currency.

2. Where the RBI reference rate for that currency is not available, the value shall be 1% of the gross amount of Indian Rupees provided or received by the person changing the money.

3. Where neither of the currencies exchanged is Indian Rupees, the value shall be equal to 1% of lesser of the two amounts the person changing the money would have received by converting any of the two currencies into Indian Rupees on that day at the reference rate provided by RBI.

(C) Determination of value of taxable service involved in supply of food and drinks in a restaurant or as outdoor catering - Rule 2C - Notification No. 24/2012-S.T., dated 6-6-2012 :

Subject to the provisions of section 67, the value of service portion, in an activity wherein goods being food or any other article of human consumption or any drink (whether or not intoxicating) is supplied in any manner as a part of the activity at a restaurant or as outdoor catering, shall be the specified percentage of the total amount charged for such supply, in terms of the following Table. The rule 2C provides abatement when food or any other article of human consumption is supplied as part of the activity of restaurant or catering service. The explanations clarify the connotation of 'total amount' and non-availment of Cenvat credit while rendering such service at percentage as specified in the table below :

TABLE

Sl. No.	Description	Percentage of the total amount
(1)	(2)	(3)
1.	Service portion in an activity wherein goods, being food or any other article of human consumption or any drink(whether or not intoxicating) is supplied in any manner as a part of the activity, at a restaurant	40
2.	Service portion in outdoor catering wherein goods, being food or any other article of human consumption or any drink(whether or not intoxicating) is supplied in any manner as a part of such outdoor catering	60

Explanation 1. - For the purposes of this rule, "total amount" means the sum total of the gross amount charged and the fair market value of all goods and services supplied in or in relation to the supply of food or any other article of human consumption or any drink (whether or not intoxicating), whether or not supplied under the same contract or any other contract, after deducting-

(i) the amount charged for such goods or services, if any; and

(ii) the value added tax or sales tax, if any, levied thereon :

Provided that the fair market value of goods and services so supplied may be determined in accordance with the generally accepted accounting principles.

Explanation 2. - For the removal of doubts, it is clarified that the provider of taxable service shall not take CENVAT credit of duties or cess paid on any goods classifiable under Chapters 1 to 22 of the Central Excise Tariff Act, 1985 (5 of 1986).".

(D) Manner of determination of value - Rule 3 :

Notification No. 24/2012-S.T., dated 6-6-2012 has replaced the words "where the consideration received is not wholly or partly consisting of money" by the words "where such value is not ascertainable". The value of taxable services where such value is not ascertainable shall be determined in the following manner:

(i) The value of taxable service shall be equivalent to the gross amount charged by the service provider to provide similar service to any other person in the ordinary course of trade and the gross amount charged is the sole consideration. When 'A' provides service of consultancy to 'B' free of charge, whereas for similar consultancy, 'A' charges 'C ₹ 1000, the value of ₹ 1000 is to be adopted for levy of service tax for service of consultancy provided to 'B'.

(ii) Where the value cannot be determined under clause (i) above, the service provider shall determine the equivalent money value of such consideration which shall, in no case be less than the cost of provision of such taxable service. If the cost of providing service of testing a product is ₹ 55, the value shall not be less than ₹ 55.

(E) Rejection of declared value by the Central Excise Officer - Rule 4 :

Rule 4 of the said Rules states that notwithstanding the provisions in Rule 3 supra, the central excise officer can determine the value of taxable service after calling information, document, etc from the service provider and there after following the due process of law i.e. issue of notice and affording adequate opportunity of explaining his case by the notice shall determine the value. The instructions issued vide F. No. B-1/4/2006-TRU, dated 19-4-2006 has clarified that the department shall use this provision with extreme care and caution. Such verification shall be undertaken only after the written instructions from the divisional AC/DC. After verification of the records, if the department is of the view that the value so determined and adopted for payment of service tax warrants revision, the issue should be decided after issue of show cause notice and observing the prescribed procedure. Before issue of any show cause notice on matters relating to valuation, concurrence of '[Principal Commissioner or Commissioner] shall be obtained.

(F) Inclusion & Exclusion of expenses from value of certain expenditure or costs - Rule 5 :

Notification No. 24/2012-S.T., dated 6-6-2012 has substituted the terms "the value of the telecommunication service shall be the gross amount paid by the person to whom telecommunication service has been actually provided" in place of "services specified in sub-clause (zzzx) of clause (105) of section 65 of the Finance Act, 1994, the value of taxable service shall be the gross amount paid by the person to whom telecom service is provided by the telegraph authority".

Rule 5 of the said Rules refers to inclusion or otherwise of the reimbursable expenditure. Since value as provided in Section 67 of the Act, is the gross amount received as consideration for provision of service, all expenditures or costs incurred by the service provider in the course of providing such service shall form the integral part of the taxable value and are includible in the .value irrespective of the facts whether such expenditures/costs are separately indicated in the invoice or bill issued by the service provider to his client. The value of the telecommunication service shall be the gross amount paid by the person to whom telecommunication service is actually provided.

However, Rule 5(2) states that the expenditure or costs incurred by the service provider, as ***pure agent of the recipient of service*** shall be excluded from the value of service subject to fulfilment of all conditions mentioned in the said sub-rule. The conditions stipulate therein are as follows :

1. The service provider acts as pure agent of the recipient of service when he makes payment to third party for the goods or services so procured.
2. The recipient of services receives and uses the goods or services so procured by the service provider in his capacity as pure agent of the recipient of service.
3. The recipient of service is liable to make payment to the third party.
4. The recipient of service authorizes the service provider to make payment in his behalf.
5. The recipient of service knows that the goods and services for which payment has been made by the service provider shall be provided by third party.
6. The payment made by the service provider on behalf of the recipient of service has been separately indicated in the invoice issued by the service provider to the recipient of service.
7. The service provider recovers from the recipient of service only such amount as has been paid by him to the third party.
8. The goods or services procured by the service provider from the third party as pure agent of the recipient of service are in addition to the services he provides on his account.

The explanation defines pure agent to mean a person who:

(a) enters into a contractual agreement with the recipient of service to act as his pure agent to incur expenditure or costs in the course of providing taxable service;

(b) neither intends to hold nor holds any title to the goods or services so procured or provided as pure agent of the receiver of service;

(c) does not use such goods or services procured; and

(d) receives only the actual amount incurred to procure such goods or services.

The second explanation further states that 'the value of taxable service is the total amount of consideration consisting of all components of taxable service and it is immaterial that the details of individual components of the total consideration are indicated separately in the invoice'.

There are four illustrations as to inclusion of cost of expenditure to the gross amount. Cost of advertisement for selling property is input service and has to be included by the real estate agent. The cost incurred for traveling, postage, telecommunication etc. even if shown separately in the invoice is not reimbursable expenses as those have been incurred while rendering the service and not as pure agent. If the expenditure on food and accommodation of the driver is realized from the customer, the same has to be included for determination of gross amount.

The same service cannot be taxed twice and the provisions have been made to avoid such eventuality.

Illustration 1.

X contracts with Y, a real estate agent to sell his house and thereupon Y gives an advertisement in newspaper. Y billed X including charges for newspaper advertisement and paid service tax on the total consideration billed. In such a case, consideration for the service provided is what X pays to Y. X cannot contend that Y acted as agents on his behalf when obtaining newspaper advertisement even if the cost of newspaper advertisement is mentioned separately in the bill. Such services are in the nature of input services for the estate agent in order to enable or facilitate him to perform his services as an estate agent.

Illustration 2.

To provide a taxable service, a service provider incurs costs such as travelling expenses, postage, telephone, etc., in the course of providing a taxable service and may indicate these items separately on the invoice to the recipient of service. In such a case, the service provider is not acting as an agent of the recipient of service but procure the inputs or input service on his own account for providing the taxable service. Merely because such expenses are shown separately in an invoice do not mean that they are reimbursable expenditure.

Illustration 3.

A contracts with B, an architect for building a house. During the course of providing the taxable service B incurs expenses such as telephone charges, air travel tickets, hotel accommodation, etc., to enable him effectively to perform the provision of services to A. In such a case, in whatever form B recovers such expenditure from A, whether as a separately itemised expense or as part of an inclusive overall fee, service tax is payable on the total amount charged by B. It is quite immaterial how the service provider computes the charges or how they break their invoice or bill down. Consideration for the service is what A pays B which is the taxable value for the purposes of levy of service tax.

Illustration 4.

To provide a taxable service of rent-a-cab, company X provides chauffeurs for overseas visitors. The chauffeur is given a lump sum amount during the tour to cover his food and overnight accommodation and any other incidental expenses such as parking fees. At the end of the tour, he returned the balance of the amount with a statement of his expenses and the relevant bills. Company X charged these amounts from the recipients of service. In such a case, the cost incurred by the chauffeur and billed to the recipient of service constituted part of the consideration for the provision of services by the company.

An explanation has been added after rule 5(1) of the Service Tax (Determination of Value) Rules, 2006 clarifying that for the purpose of telecommunication service [Section 65(105)(zzzx)] the value shall be the gross amount paid by the person to whom the service is provided by the telegraph authority. Thus, in case of service provided by way of recharge coupons or prepaid cards or the like, the value shall be the gross amount charged from the subscriber or the ultimate user of the service and not the amount paid by the distributor or any such intermediary to the telegraph authority. This amendment shall come into force on 1.3.2011. Vide Notification No. 24/2012-ST, dated 6-6-2012, it has been provided that w.e.f. 1-7-2012, value of telecommunication services shall be the gross amount paid by the person to whom telecommunication service is actually provided.

On reimbursable expenditure, it has been clarified by CBEC vide Letter No. B1/4/2006 dated 19.4.2006 as under -

Value for the purpose of charging service tax is the gross amount received as consideration for provision of service. All expenditures or costs incurred by the service provider in the course of providing a taxable service forms integral part of the taxable value and are includable in the value. It is not relevant that various expenditure or costs are separately indicated in the invoice or bill issued by the service provider to his client.

The service provider in the course of providing any taxable service may incur certain expenditure or cost as a pure agent of the client. The service provider seeks to exclude such expenditure or cost incurred by him as a pure agent of his client (generally known as reimbursable expenditure) from the value of the taxable services.

There could be situations where the client of the service provider specifically engages the service provider, as his agent, to contract with the third party for supply of any goods or services on his behalf. In those cases such goods or services so procured are treated as supplied to the client rather than to the contracting agent. The service provider in such cases incurs the expenditure purely on behalf of his client in his capacity as agent of the client. Amounts paid to the third party by the service provider as a pure agent of his client can be treated as reimbursable expenditure and not includible in the taxable value. However, if the service provider acts as an undisclosed agent i.e. acting in his own name without disclosing that he is actually acting as an agent of his client, he cannot claim the expenditure incurred by him as reimbursable expenditure. Whether the expenditure or cost incurred by the service provider in his capacity as a pure agent of the client or incurred on his own account is a question of fact and law and is to be determined carefully.

Indication of different elements of the transaction in the invoice or bill could often be misleading. One has to carefully examine the exact legal nature of the transactions and other material facts before taking a view as to whether or not the expenditure sought to be excluded from the value is reimbursable expenditure. Not only the form, but also the substance of the transaction should be duly taken into account.

Rule 5 pertains to reimbursable expenditure incurred by the service provider as a pure agent of his client. Explanation (1) to rule 5(2) clearly specifies the criteria to decide whether the service provider acts as a pure agent or not in a given situation. In the case of agency function, the agent neither intends to hold nor holds any title to the goods or services and also never uses such goods or services so procured. It is also important to note that the service provider only receives the actual amount incurred to procure such goods or services.

The service provider who seeks to claim exclusion of certain value from the taxable value should also fulfill all the conditions specified in rule 5(2).

In Rolex Logistics Pvt. Ltd vs. CST Bangalore (2009) 13 STR 1471; (2009) 20 STT 431 (CESTAT, Bangalore), it was held that reimbursement of expresses are not for services rendered but expenditure incurred on behalf of client by service provider. Gross amount for service rendered means only for services rendered. It also interpreted `reimbursement' as payments made on behalf of service recipient by service provider in the course of rendering services. The gross receipt for the services rendered means only for the services rendered.

It held as follows;

What is a reimbursement? When a service provider provides service to a service receiver or a client, on behalf of his client he incurs various expenditure and these expenditure are all for different purposes. The Service Tax liability in terms of Section 67 is only on the gross amount received towards the services rendered. If the service provider in the course of rendering service has to make certain payments on behalf of the service receiver, they are known as reimbursements. The reimbursements are actually not towards the service rendered but they are only towards other expenditure incurred on behalf of the client by the service provider. Normally, the service provider incurs these expenditures in the interest of quicker service. Suppose the service provider has to first receive the money and then render the service, it would cause lot of delay. Therefore, while providing service to the client, the service provider has to incur various expenditure in order to save time and avoid delay, hence, the expenditure is incurred by the service provider and later these are reimbursed by the client. In fact, the client is supposed to pay all these amounts. For example, take the case of a Custom House Agent in the course of clearance of the goods, the importer may have to incur different expenditures towards the port, stevedoring clearances, stationery, all that. These expenditures are actually to be paid by the importer but the CHA initially incurs all these expenditure and then later collects from the client. These are reimbursements. So what is to be borne in mind is that these reimbursements are not for the services rendered. The gross receipt for the services rendered means only for the services rendered. The amount of money received only for the services rendered not for all the other expenditure which is to be incurred normally by the client."

The above judgment clearly specifies the reimbursements that can be excluded from the taxable value by citing of the example of CHA who incurs expenses such as port charges, customs duties on importation, demurrage charges payable to the wharf etc., actually payable by the client but incurred on behalf of the latter, which were reimbursed on actual basis, and qualify for abatement from the taxable value of CHA which includes his charges for clearing the goods from the customs and the above analogy also holds good for `pure agent' of the Valuation Rules, as these expenses are not related to the service rendered at all.

The Apex Court in the case of All India Federation of Tax Practitioners v. Union of India [2007] 10 STT 166 held that service tax is destination based consumption tax and that may be either performance based or property based. Economic services are provided for valuable consideration without being rendered charitable. No service which is uneconomical or commercially unviable is provided in the commercial world. Various elements of cost contribute to the provision of economic services. Expenses which are indispensable and inevitably incurred to make the economic service performable that contribute to the gross value of service. The provider of economic service recovers his entire cost involved in providing such service in the best possible manner that may be viable to him and the service recipient.

In Intercontinental Conslt. & Tech. Pvt. Ltd. v Union of India (2008) 12 S.T.R. 689 (Delhi), it was held by high court that the demand on reimbursement of expenses like air travel, hotel stay, room rent, boarding and lodging charges etc. after including such amounts in taxable value in case of consulting engineer's services can not be coerced. The petitioner contended that reimbursable expenses were not forming part of services and such amounts were also indicated separately in bills. It was held that while proceedings pursuant to SCN may continue, coercive steps need not to be taken till passing of adjudication order.

In Scott Wilson Kirkpatrick (I) Ltd. vs. Commissioner of Service Tax, (2007) 5 STR 118 (CESTAT, Bangalore), it was held that reimbursable expenses were not subject to service tax at the relevant time.

In Sri Bhagavathy Traders v CCE (2011) 24 S.T.R. 290 (CESTAT - LB, Bangalore), it was held that reimbursement arises only when person actually paying under no obligation to pay and pays amount on behalf of buyer while recovering same from buyers. Only when service recipient is having obligation, legal or contractual to pay certain amount to any third party and said amount is paid by service provider on behalf of service recipient, question of reimbursing expenses arises.

Reimbursement of expenses has been a contentious issue and actual reimhursements of expenses is not subject to levy of Service Tax; more so when these reimbursements can be substantiated by evidence. Reference can be made to following judicial pronouncements -

(i) Alathur Agencies vs, CCE & C (2007) 8 STT 204 (CESTAT, Bangalore)

(ii) Nandini Warehousing Corporation vs. CCE (2008) 12 STT 120 (CESTAT, Bangalore)

(iii) Hassan Hajee & Co vs. CCE (2007) 5 STR 397 (CESTAT, Bangalore)

(iv) M.P.R. Mercantile Syndicate vs. CCE, Cochin (2011) 22 STR 443 (CESTAT, Bangalore).

(v) Sri Sastha Agencies Pvt. Ltd. vs.Asst. Commr. of C.Ex & Cus. Palakkad [2007 (6) STR 185 (CESTAT, Bangalore)]

(vi) Bhagyanagar Services vs. CCE, Hyderabad [2006 (4) STR 22 (CESTAT, Bangalore.)]

(vii) CCE, C & ST, BBSR-I vs. M/s. Nilaiohita Enterprises [2007 (6) STR 318 (CESTAT, Kolkata)]

(viii) Sangamitra Services Agency vs. CCE, Chennai [2007 (8) STR 233 (CESTAT, Chennai)]

(ix) Apco Agencies vs. CCE, (2008) 10 STR 169 (CESTAT, Bangalore).

(x) S & K Enterprises vs. CCE (2008) 10 STR 171(CESTAT, Bangalore).

(xi) E.V. Mathai & Co. vs. CCE (2006) 3 STR 116 (CESTAT, Bangalore).

(xii) Keralam Enterprises vs. CCE (2008) 9 STR 503 (CESTAT, Bangalore).

(xiii) M/s U.M. Thariath & Company, M/s S.J.C. Pharma vs. CCE. Cochin [2007 (8) STR 161 (CESTAT, Bangalore)]

(xiv) Al -Baith Steel Pvt. Ltd. vs. CCE (2008) 10 STR 554 (CESTAT, Bangalore).

(xv) Jayalaxmi Enterprises vs. CCE Mungalore [2008 (9) STR 19 (CESTAT, Bangalore)]

(xvi) M/s. B.S. Refrigeration Ltd. vs. CST, Bangalore [2006 (4) S.T.R. 103 (CESTAT, Bangalore)]

(xvii) Rolex Logistics Pvt. Ltd. vs. CST (2009) 13 STR 147 (CESTAT, Bangalore).

(xviii) K.D. Sales Corporation vs. CCE, Belgaum [2007 (6) STR 418 (CESTAT, Bangalore)]

However, on the other hand, in the following cases, Tribunals have held that the reimbursement charges to be included in gross value of the taxable services rendered :

Sl No.	Citation	Decision
1.	Kirloskar Pneumatics Co. Ltd vs. CCE 2011 (23) S.T.R. 161(Cestat - Mumbai)	It was held that the reimbursement of the expenses incurred by service provider in connection with the services provided - Such recoveries were made under statutory invoices issued to the customers, but Service tax was not paid on expenses reimbursed by the customers - Prima facie entire amount collected by appellant from their customers would constitute gross taxable value for the purpose of payment of Service tax.
2.	Naresh Kumar & Co. Pvt. Ltd, vs. CST (2008) 11 S.T.R. 578 (Cestat - Kolkata)	It was held if an expenditure is indispensable and inevitably incurred to provide a service, such cost should essentially form part of cost of service itself and shall contribute to value of taxable service.

Thus, it is seen that the Tribunals have differed in their pronouncements on the same issue of the taxability of reimbursement of expenses and the matter refereed to larger bench.

In Harveen & Co vs. CCE, Chandigarh (2012) 26 STR 14 (CESTAT, Delhi), in a case relating to clearing and forwarding agency, it was held that expenses of dispatch inspection, octroi and detention charges are not towards any activity that would constitute service rendered by assessee. Clerkage and office telephone expenses even if billed separately to client can not be considered reimbursable expenses. In case of godown rent, if it is for discharging obligation under a contract, rent would form part of taxable value even if it is reimbursed separately by client.

(G) Inclusion of commission/brokerage/initial deposit - Rule 6(1):

The value of taxable service as stipulated in Rule 6 of the said Rules shall include the followings:

1. The commission/brokerage charged by a broker on sale of securities including the commission or brokerage paid by the broker to the sub-broker.
2. The adjustment made by provider of telecommunication service from any amount paid by the subscriber at the time of application for providing telecommunication facility but excludes the initial deposit made by the subscriber.
3. The amount of premium charged by the insurer from the policyholder.
4. The commission received by the air travel agent from the airline excluding airfare collected.
5. The commission/fee or any other sum received by an actuary or intermediary or insurance agent or intermediary from the insurer.
6. The reimbursement received by the authorized service station from the manufacturer.
7. The commission or any amount received by the rail travel agent from the railways or the customer excluding rail fare collected.
8. Remuneration/commission paid by the client to the C&F agent.
9. The commission/fee/any amount paid to agent by the insurer appointing such agent in relation to insurance auxiliary service provided by an insurance agent.
10. The amount realized as demurrage or by any other name whatever called for the provision of a service beyond the period originally contracted or in any other manner relatable to the provision of service. This clause has been inserted by Notification No. 24/2012-S.T., dated 6-6-2012.

(H) Exclusion of deposit, fares, interest, etc., from determination of value - Rule 6(2):

The value of taxable service does not include the following :

1. Initial deposit made by the subscriber at the time of application for telecommunication service.
2. The air fare collected by air travel agent in respect of service provided by him.
3. The rail fare collected by rail travel agent in respect of service provided by him.
4. Interest on delayed payment of any consideration for the provision of services or sale of property, whether moveable or immoveable.
5. The taxes levied by any Government on any passenger travelling by air, if shown separately on the ticket, or the invoice for such ticket issued to the passenger.
6. Accidental damages due to unforeseen actions not relatable to the provision of service.
7. Subsidies and grants disbursed by the Government, not directly affecting the value of service.

The entries at serial Nos. 5 to 7 has been added vide Notification No. 24/2012-S.T., dated 6-6-2012

Illustration 5.

- Insurance Companies provide insurance services to the clients for which the premium is charged. The premium charged is a consideration for the insurance service provided. However, in case due to an unforeseen action, like an accident etc., a compensation is paid by the insurance company to the client then the money would not be included as part of value of taxable service as it is not relatable to the provisions of service but is only in the nature of consequence of provisions of insurance service.
- In case a landlord who has rented out his office building to a tenant receives compensation from the tenant for the damage caused to the building by an unforeseen action then such compensation would not form part of the value of taxable service related to tenant of his building as an unforeseen damage caused by the tenant is not relatable to provision of service of renting of the office building.

The exclusion entry relating to subsidies and grants disbursed by the Government, not in the nature of directly influencing the value of service has also been inserted by the Service Tax (Determination of Value) Second Amendment Rules, 2012. A subsidy influences the price directly when the price goes down proportionately to the amount of subsidy. In terms of this exclusion any subsidy or grant disbursed by the Government cannot form part of the value of taxable service unless such subsidy or grant directly influences the value of such service.

In Keeping Newcastle Warm Ltd. (2012) 36 STT 702 (ECJ), where assessee received energy advice grants for providing energy advice, it was held by the European Court of Justice that energy advice grants paid by the public authority constituted a subsidy.

Since taxable amount comprises of everything which makes up consideration for service, every advice grants were received by assessee in consideration for service provided by the assessee and hence taxable.

In Office Des Products Walloons ASBL v. Belgian State (2012) 36 STT 683 STT (ECJ), it was held that operating subsidies covering a part of running costs always affect the cost price of the goods and services supplied by the subsidised body. However, the mere fact that a subsidy may affect the price of the goods or services supplied by the subsidised body is not enough to make that subsidy taxable. For the subsidy to be directly linked to the price of such supplies, it is also necessary that it be paid specifically to the subsidised body to enable it to provide particular goods or services. Only in that case, the subsidy can be regarded as consideration for the supply of goods or services, and therefore be taxable.

Subsidy is identifiable only if there is significant relation between price and subsidy. In order to determine whether the consideration represented by the subsidy is identifiable, the Court may either compare the price at which the goods are sold in relation to their normal cost price, or examine whether the amount of the subsidy has been reduced once those goods are no longer produced. If the factors examined are significant, it must be concluded that the part of the subsidy allocated to the production and sale of the goods in question constitutes a subsidy directly linked to the price, In that regard, it is not necessary for the subsidy to correspond exactly to the diminution in the price of the goods supplied, it being sufficient if the relationship between the diminution in price and the subsidy, which may be at a flat rate, is significant.

6.15.8 Value of Taxable Service to be the Actual Consideration where Services provided from outside India (Rule 7)

According to Rule 7, in cases where the taxable services are provided by person from outside India in India (Section 66A cases), the value of taxable services received shall be taken at such amount as is equal to the actual consideration charged for the services so provided or to be provided. This could, therefore, be taken as actual remittance made to service provider abroad.

In case of services partly performed in India, the value of taxable services shall be the total consideration paid by the recipient for such services including the value of service partly performed outside India.

Rule 7 stands omitted by Notification No. 11/2012-ST, dated 17-3-2012 and as superceded by Notification No. 24/2012-ST, dated 6-6-2012 w.e.f. 1-7-2012.

6.15.9 Adjudication

No forms have been prescribed for seeking determination of value of taxable services and it is expected that in case of difference of amount between the value of taxable service as determined by the service provider and that as per the opinion of Central Excise Officer, the matter could be decided by way of adjudication by giving a show cause notice and an opportunity of being heard.

If the assessee does not agree with the valuation, he may also prefer an appeal.

Withdrawal of Circulars on Valuation

Consequent upon notification of Service Tax (Determination of Value) Rules, 2006, all circulars on valuation of taxable services or portions thereof, which are inconsistent with the new valuation rules have been withdrawn B1/4/2006 dated 19-4-2006. These same has been retriated vide Circular No. 93/04/2007, dated 10-5-2007.

6.15.10 Value of Director's Services

So far as payment to Directors towards their services is concerned, value of services shall include -

- Director's fee, by whatever name called
- Commission based on profits or otherwise
- Bonus
- Value of service for company car provided
- Share in profit
- Benefit in form of ESOPs etc.
- Travel reimbursements.

However, reimbursement of expenses in terms of contractual obligations may not be taxable if they fall within the scope of 'reimbursements' and 'pure agents' as per Service Tax (Determination of Value) Rules, 2005.

The following amounts received by the directors from the company will not attract Service Tax as such amounts does not represent service provided by directors-

(i) interest on loan by director to company

(ii) dividend on shares

(iii) other professional charges on account of services not rendered as a director (in professional capacity)

On reimbursement of expenses incurred by the director being liable to Service Tax, it may be noted that directors are considered to be agent of the company and as such expenses are reimbursed to them as an agent. Moreover, taxability shall be subject to the valuation rules and criteria of 'pure agency' shall have to be satisfied.

On whether sitting fee paid to directors for attending board meetings only are taxable or any amount paid as fees whether for board meetings or committee meetings will be taxable, it may be noted that all amounts paid as remuneration except salary to directors shall be liable to Service Tax, whether for attending board meetings or committee meetings or for any other service rendered in the capacity of a director. If an employed director gets sitting fee for attending the meeting, it may be liable to Service Tax as Department is likely to view it that way. There is need for clarification on this issue.

Since there is a monetary limit on payment of remuneration to directors beyond which it requires approval of the Central Government u/s 197 of the Companies Act, 2013, there is doubt that whether Service Tax paid by the company under reverse charge shall be deemed to be a part of such remuneration. Under the scheme of Service Tax, though taxable services are rendered by the directors, the burden of payment of Service Tax has been shifted on the companies on whose board, such directors serve. In certain cases which are already at the top of the ceiling, payment of Service Tax by company will result in exceeding the monetary limit of 1 per cent or 3 per cent of net profit, as the case may be. Ministry of Corporate Affairs (MCA) has vide General Circular No. 24/2012 dated 9.8.2012 clarified that for the financial year 2012-13, any increase in remuneration solely as a result of application of Service Tax on commission shall not require Central Government's approval (though deemed to be a part of remuneration as per income Tax) u/s 197 of the Companies Act, 2013. It may be noted that this relaxation is only for the financial year 2012-13 and only applies to non-whole time director's remuneration.

In case of any remuneration, by whatever name called, accruing to persons employed by the company as managing director or whole time directors, entire gross amount shall not be taxable as it is earned in the course of employment and is not covered within the scope of service at all. If the service itself is not taxable, there is no question of Service Tax being payable on the remuneration which is a part of contract of employment. On the other hand, even if the remuneration is termed as salary for a part-time/non-official/ independent director, it shall be subject to levy of Service Tax.

6.5.11 Service Tax and TDS

Service tax is payable on gross amount payable to service provider. Since TDS is deducted on behalf of the payee, gross amount for the purpose of service tax would be the amount inclusive of or before deduction of TDS.

On TDS on payments made to service providers, CBDT vide Letter No F. No. 275/1/2006-IT (B) dated 21.7.2006 addressed to CIT, Mumbai clarified that tax deduction u/s 194-J of Income Tax Act 1961 would be required to be made on the sums payable by the deductors inclusive of any service tax.

So far as TDS on rent is concerned, CBDT has clarified vide Circular No. 4 dated 28.4.2008 that service lax paid by the tenant does not partake of the nature of income of landlord. The landlord only acts as a collection agency for the Government for collection of service tax. Therefore, TDS under section 194-J of the Income Tax Act, 1961 would be required to be made on the amount of rent paid or payable without including the service tax.

In CCE, Jaipur I vs. Louis Berger International Inc. (2009) 13 STR 381; (2008) 18 STT 312 (CESTAT, New Delhi), it was held that amount of tax deducted at source (TDS) is not excludible from gross amount for determining tax liability. The TDS amount deducted was payable only on behalf of the appellant to income tax department and there was no justification to exclude TDS amount from gross amount for the purpose of determining service tax liability.

Example 45: US$1000 are sold by a customer at the rate of ₹ 45 per US$.

RBI reference rate for US$ is ₹ 45.50 at that time.	₹
RBI reference rate for US$ at that time	= 45.50
Less: selling rate by a customer	= 45.00
Difference (irrespective of Plus or Minus)	= 0.50
The taxable value	= ₹ 500 (i.e. US$1000 x Re. 0.50)
Service Tax	= ₹ 72.50 (i.e. ₹ 500 x 14.5%)

Note: Service tax is subject to 2% and 1% Education and SAH Education Cess.

Example 46: INR70000 is changed into Great Britain Pound (GBP) and the exchange rate offered is ₹70, thereby giving GBP 1000.

RBI reference rate for that currency at that time for GBP is ₹ 69.

		₹
RBI reference rate for GBP at that time	=	69.00
Less: Buying rate by a customer	=	70.00
Difference (irrespective of Plus or Minus)	=	1.00
The taxable value	=	₹ 1000.00 (i.e. GBP1 000 x Re. 1.00)
Service Tax	=	₹ 145.00 (i.e. ₹ 1000 x 14.5%)

Note: Service tax is subject to 2% and 1% Education and SAH Education Cess.

(ii) In case where the RBI reference rate for a currency is not available, the value shall be 1% of the gross amount of Indian Rupees provided or received, by the person changing the money.

Example 47: INR 70,000 is changed into Great Britain Pound (GBP) and the exchange rate offered is ₹70, thereby giving GBP 1000.

RBI reference rate for that currency at that time for GBP is not available.

The taxable value	=	**₹ 700 (i.e. GBP1000 x ₹ 70 x 1%)**
Service Tax (Standard Rate)	=	₹ 102 (i.e. ₹ 700 x 14.5%)

Note: (i) Service tax is subject to 2% and 1% Education and SAH Education Cess.

(ii) In case both the currencies are not Indian rupees, @1% of the lesser of the amounts received if the two currencies are converted at RBI reference rate.

Example 48: US$ 1,000 is changed into UK £ 571.4286 (i.e. 1 UK POUND = US$ 1.75).

RBI reference rate for that currency at that time for 1 US$ is ₹ 45 and for 1 UK POUND = ₹ 85

Particulars	Value in ₹	Remarks
US Dollars converted into RBI reference rate at that time of exchange	45,000	USD 1000 x ₹ 45
UK Pounds converted into RBI reference rate at that time of exchange	48,571	UK £ 571.4286 x ₹ 85

The lower of the above two currencies at RBI reference rate is ₹ 45,000. Therefore, the taxable value is ₹ 450 (i.e. ₹ 45,000 x 1%)

Service Tax = ₹ 65 (i.e. ₹ 450 x 14.5%)

Note: Service tax is subject to 2% and 1% Education and SAH Education Cess

Example 49: Food King Pvt. Ltd. Supplies foods and beverages only.

(i) at a restaurant for ₹ 11,250 (inclusive of VAT ₹ 1,250) located at Mylapore, Chennai and

(ii) Supplied food to Infosys company for ₹ 22,500 (including of VAT ₹ 2,500). Find service tax liability?

Answer:

		₹
(i) Value of service = 10,000 x 40%	=	4,000 (i.e. restaurant services)
(ii) Value of service = 20,000 x 60%	=	12,000 (i.e. outdoor catering services)
Total value of services	=	16,000
Service Tax 14.5% on ₹ 16,000	=	2,320

Example 50: Reimbursement expenses can be viewed as

Octroi or entry tax paid by carriage and freight forwarding agent on behalf of owner of goods, Customs duty by customs house agent on behalf of client, Advertisement charges paid by an advertising agency to newspaper on behalf of clients, Ticket charges paid by Travel Agent and recovered from his customer.

Example 51: X contracts with Y, a real estate agent to sell his house and thereupon Y gives an advertisement on television. Y billed X including charges for Television advertisement and paid service tax on the total consideration billed. In such a case, consideration for the service provided is what X pays to Y. Y does not act as an agent on behalf of X when obtaining the television advertisement even if the cost of television advertisement is mentioned separately in the invoice issued by Y. Advertising service is an input service for the estate agent in order to enable or facilitate him to perform his services as an estate agent.

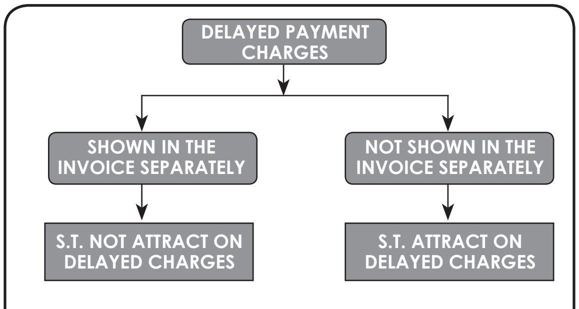
Example 52: In the course of providing a taxable service, a service provider incurs costs such as traveling expenses, postage, telephone, etc., and may indicate these items separately on the invoice issued to the recipient of service. In such a case, the service provider is not acting as an agent of the recipient of service but procures such inputs or input service on his own account for providing the taxable service. Such expenses do not become reimbursable expenditure merely because they are indicated separately in the invoice issued by the service provider to the recipient of service.

Example 53: A contract with B, an architect, for building a house. During the course of providing the taxable service, B incurs expenses such as telephone charges, air travel tickets, hotel accommodation, etc., to enable him to effectively perform the provision of services to A. In such a case, in whatever form B recovers such expenditure from A, whether as a separately itemized expense or as part of an inclusive overall fee, service tax is payable on the total amount charged by B. Value of the taxable service for charging service tax is what A pays to B.

Example 54: Company X provides a taxable service of rent-a-cab by providing chauffeur-driven cars for overseas visitors. The chauffeur is given a lump sum amount to cover his food and overnight accommodation and any other incidental expenses such as parking fees by the Company X during the tour. At the end of the tour, the chauffeur returns the balance of the amount with a statement of his expenses and the relevant bills. Company X charges these amounts from the recipients of service. The cost incurred by the chauffeur and billed to the recipient of service constitutes part of gross amount charged for the provision of services by the company X. This sum is subject to service tax.

Example 55: In respect of delay payment charges recovered by the service provider is includable in the value of taxable service?

Answer: vide CBEC LETTER 137/25/2011 dt.3.8.201 1, it is clarified in the following manner:



CB LETTER 137/25/2011 DT. 3.8.2011

“SECTION 67A: Date of determination of rate of tax, value of taxable service and rate of exchange —The rate of service tax, value of a taxable service and rate of exchange, if any, shall be the rate of service tax or value of a taxable service or rate of exchange, as the case may be, in force or as applicable at the time when the taxable service has been provided or agreed to be provided.

6.16 IMPORTANT ISSUES UNDER SERVICE TAX PROVISIONS

6.16.1 There is no Service Tax on free services. This is because there is no consideration involved in rendering the free service. However the service tax department is likely to verify whether the services were in fact rendered free.

6.16.2 If the service provider received an amount from service receiver indirectly in addition to receiving the value of services, such receipt is not subject to Service Tax.

Example 56: A mandap keeper lets out his premises to a contactor at market rates. The contractor then gave donation of ₹ 20 lakhs to the mandap keeper as contribution to corpus of the mandap. This amount was not in relation to service of mandap provided by mandap keeper and hence will not attract service tax. *CKP Mandal* v *CCE* (2006) (Bom. HC).

However, in the above instance if the market rate is say ₹ 5 lakhs and the service has been offered at ₹ 2 lakhs, the difference between ₹ 5 lakhs and ₹ 2 lakhs i.e. ₹ 3 lakhs will suffer service tax and the balance i.e. ₹ 20 lakhs less ₹ 3 lakhs will not suffer service tax. This is laid out in Service Tax (Determination of Value) Rules, 2006 which says that if any amount is received indirectly as part of consideration for the services rendered then such indirect consideration will form part of the value of taxable services.

6.16.3 Option to pay an amount in case of lottery service under section 65(105) (zzzzn):

The distributor or selling agent is liable to pay service tax for the taxable service of promotion, marketing, organizing or any other manner assisting in organizing lottery.

As per Rule 6(7C) of the Service Tax Rules, 1994 the distributor or selling agent shall have the option to pay an amount at the rate specified below instead of paying service tax w.e.f 01-06-2015 (vide 15/2015-ST, dt. 19.05.2015).

S.No.	Rate	Condition
i	₹ 8,200 on every ₹ 10 lakh (or part of ₹ 10 lakh) of aggregate face value of lottery tickets printed by the organizing State for a draw	If the lottery or lottery scheme is one where the guaranteed prize payout is more than 80%.
ii	₹ 12,800 on every ₹ 10 lakh (or part of ₹ 10 lakh) of aggregate face value of lottery tickets printed by the organizing State for a draw	If the lottery or lottery scheme is one where the guaranteed prize payout is less than 80%.

Provided that in case of online lottery, the aggregate face value of lottery tickets for the purpose of this sub-rule shall be taken as the aggregate value of tickets sold, and service tax shall be calculated in the manner specified in the said Table.

Provided further that the distributor or selling agent shall exercise such option within a period of one month of the beginning of each financial year and such option shall not be withdrawn during the remaining part of the financial year.

Provided also that the distributor or selling agent shall exercise such option for financial year 2010-11, within a period of one month of the publication of this sub-rule in the Official Gazette or, in the case of new service provider, within one month of providing of service under the said sub-clause and such option shall not be withdrawn during the remaining part of that financial year.

Terms	Meanings	Examples
Face value	The amount mentioned on the lottery ticket.	 Face value of ₹ 10 per ticket
Aggregate face value	For printed tickets: Face value of ticket x No. of lottery tickets printed. For online tickets: Face value of ticket x No. of lottery tickets sold	 2,50,000 tickets printed x ₹ 10 = ₹ 25 lacs 2,00,000 tickets sold x ₹ 10 = ₹ 20 lacs
Guaranteed prize payout	the aggregate prize money distributed to all winners	Let us say ₹ 15 lacs in case of printed tickets out of ₹ 25 lacs. (i.e. 60%)

Example 57: M/s Martin Pvt. Ltd. is a distributor or selling agent authorized by a State in India. Following is the details of lotteries of a distributor to be organized by the State.

Particulars	Lakhpati (Printed)	Crorepati (Online)
No. of tickets proposed	2,50,000	3,00,000
Face value of ticket	₹ 10 each	₹ 500 each
Guaranteed prize payout	@60%	@90%
No. of tickets sold	2,00,000	2,35,000

Calculate the service tax under composition scheme as per Rule 6(7C) of the Service Tax Rules, 1994.

Answer:

Lakhpati lottery tickets - Printed

No. of tickets proposed	2,50,000 tickets
Face value of ticket	₹ 10 each
Total face value	₹ 25,00,000
Guaranteed prize payout	@60%
Multiples of TEN lakhs or part of TEN lakhs	3 (i.e. ₹ 25,00,000/₹ 10,00,000)
Service tax payable for every ₹ 10 lakhs or part thereof	₹ 12,800
Total Service tax (subject to Cess)	38,400 (i.e. 3 x ₹ 12,800)

Crorepati lottery tickets –Online

No. of tickets sold	2,35,000 tickets
Face value of ticket	₹ 500 each
Total face value	₹ 11,75,00,000
Guaranteed prize payout	@90%
Multiples of TEN lakhs or part of TEN lakhs	118 (i.e. ₹ 11 ,75,00,000/₹ 10,00,000)
Service tax payable for every ₹ 10 lakhs or part thereof	₹ 8,200
Total Service tax (subject to Cess)	₹ 9,67,600 (i.e. 118 x ₹ 8,200)

Total service tax liability payable by M/s Martin Pvt. Ltd.

Particulars	(₹)
Lakhpati lottery tickets - Printed	38,400
Crorepati lottery tickets – Online	9,67,600
Total	10,06,000

6.16.4 Persons marking the lottery tickets are exempt from service tax (vide Notification No. 50/201 0-ST, dated. 08-10-2010):

The Central Government, exempts persons marketing the lottery tickets (hereinafter referred to as 'such person'), other than the distributors or selling agents appointed or authorized by the lottery organising State (hereinafter referred to as 'such distributor or selling agent'), from the whole of service tax leviable thereon on the value of taxable service of marketing of lottery, if the optional composition scheme under sub-rule (7C) of rule 6 of Service Tax (2nd Amendment) Rules, 2010 dated 8th October 2010 is availed of by such distributor or selling agent, in respect of such lottery during the financial year.

Provided that if such person also markets lottery tickets for distributors or selling agents who have not so opted, then nothing contained in this notification shall apply to the value of service provided to the distributors or selling agents who have not so opted.

6.16.5 Penalty for Non-Payment or Delayed Payment of Service Tax (Section 76 of the Finance Act, 1994) w.e.f. 14.05.2015:

(1) Where service tax has not been levied or paid, or has been short-levied or short-paid, or erroneously refunded, for any reason, other than the reason of fraud or collusion or wilful mis-statement or suppression of facts or contravention of any of the provisions of this Chapter or of the rules made thereunder with the intent to evade payment of service tax, the person who has been served notice under sub-section (1) of section 73 shall, in addition the service tax and interest specified in the notice, be also liable to pay a penalty not exceeding ten per cent of the amount of such service tax:

Provided that where service tax and interest is paid within a period of thirty days of –

(i) the date of service of notice under sub-section (1) of section 73, no penalty shall be payable and proceedings in respect of such service tax and interest shall be deemed to have been concluded;

(ii) the date of receipt of the order of the Central Excise Officer determining the amount of service tax under sub-section (2) of section 73, the penalty payable shall be twenty-five per cent of the penalty imposed in that order, only if such reduced penalty is also paid within such period.

(2) Where the amount of penalty is increased by the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be, over the above the amount as determined under sub-section (2) of section 73, the time within which the reduced penalty is payable under clause (ii) of the proviso to sub-section (1) in relation to such increased amount of penalty shall be counted from the date of the order of the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be.]

6.16.6 Service Tax Liability — In case of Tax Deducted at Source (TDS) under Income Tax Act, 1961 Service Tax is payable on the value of Service and Not on value net of TDS.

Service Tax is to be paid on the gross value of taxable service which is charged by a Service Tax assessee for providing a taxable service. Income tax deducted at source is includible in the charged amount. Therefore, service Tax is payable on the gross amount including the amount of Income Tax deducted at source also.

Example 59: Mr. X, an architect has received the fees of ₹ 4,48,500 after the deduction of Income Tax of ₹ 51,500. The Service Tax is payable on ₹ 4,48,500 whether the statement is correct?

Answer: No, the service tax can be payable on value of services. Hence, the value of services is ₹ 5,00,000 and the service tax @ 14.5% can be levied on ₹ 5,00,000.

Hence, the service tax liability is ₹ 63,319 (i.e. ₹ 5,00,000 x 14.5/114.5)

6.17 E-PAYMENT OF SERVICE TAX

Every assessee shall electronically pay the service tax payable by him, through internet banking. Provided that the Assistant Commissioner or the Deputy Commissioner of Central Excise, as the case may be, having jurisdiction, may for reasons to be recorded in writing, allow the assessee to deposit the service tax by any mode other than internet banking.

6.18 SELF ADJUSTMENT OF EXCESS TAX PAID

Tax paid in excess to the credit of Government for a month/quarter may be adjusted by the assessee against the tax payable for the succeeding month/quarter Rule 6(4A) of the Service Tax Rules, 1994.

6.18.1 Conditions for Self-Adjustment

As per the Rule 6(4B) of the Service Tax Rules, 1994, self adjustment of excess payment of service tax allowed under Rule 6(4A) is subject to the following conditions:

i. Excess payment since exact amount to be paid could not be calculated

ii. When tax is to be paid by 31st March and calculation of exact amount of service tax is difficult

iii. Any calculation mistakes

An assessee who have centralized registration (i.e. one RC) can adjust the excess service tax paid on their own without any monetary limit provided the excess amount paid is on account of delayed receipt of details of payments from branches.

> Self adjustment will not be applicable when excess payment relates to interpretation of law, taxability, classification, valuation or eligibility to exemption notification.

In case of an assessee with multiple registration certificates (RCs), excess service tax paid on their own without any monetary limit w.e.f. 1.4.2012 [NT3/201 2-ST dt 17-3-2012]. The monetary limit is ₹ 2,00,000 upto 31-3-2012 for a month/quarter as per Rule 6(4B) (iii) of the Service Tax Rules, 1994.

Such adjustment can be made only in the succeeding month or quarter.

The details of self-adjustment should be intimated to the Superintendent of Central Excise within a period of 15 days from the date of adjustment as per Rule 6(4B) (iv) of the Service Tax Rules, 1994. W.e.f. 1-4-2012 there is no need to intimate to the Department about such self-adjustment.

6.18.2 Advance payment of Services Tax

As per Rule 6(1A) of the Service Tax Rules, 1994

i. The assessee may, on his own, pay Service tax in advance and adjust the amount towards future liability.

ii. He shall intimate details of advance payment to the Jurisdiction Superintendent of Central Excise within 15 days of such payment.

iii. He shall indicate the details of adjustment of advance payment in the returns.

6.19 SPECIAL AUDIT

Section 72A

(1) If the Principal Commissioner of Central Excise or the Commissioner of Central Excise, has reasons to believe that any person liable to pay service tax (herein referred to as "such person"),-

(i) Has failed to declare or determine the value of a taxable service correctly; or

(ii) Has availed and utilized credit of duty or tax paid-

(a) Which is not within the normal limits having regard to the nature of taxable service provided, the extent of capital goods used or the type of inputs or input services used, or any other relevant factors as he may deem appropriate; or

(b) By means of fraud, collusion, or any willful misstatement or suppression of facts; or

(iii) Has operations spread out in multiple locations and it is not possible or practicable to obtain a true and complete picture of his accounts from the registered premises falling under 20 the jurisdiction of the said Commissioner,

He may direct such person to get his accounts audited by a chartered accountant or cost accountant nominated by him, to the extent and for the period as may be specified by the Commissioner.

(2) The chartered accountant or cost accountant referred to in sub-section (1) shall, within the period specified by the said Commissioner, submit a report duly signed and certified by him to the 25 said Commissioner mentioning therein such other particulars as may be specified by him.

(3) The provisions of sub-section (1) shall have effect notwithstanding that the accounts of such person have been audited under any other law for the time being in force.

(4) The person liable to pay tax shall be given an opportunity of being heard in respect of any material gathered on the basis of the audit under Sub-Section (1) and proposed to be utilized in any proceeding under the provisions of this Chapter or rules made thereunder.

Explanation – For the purposes of this section –

(i) "chartered accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Chartered Accountants Act, 1949;

(ii) "cost accountant" shall have the meaning assigned to it in clause (b) of sub-section (1) of section 2 of the Cost and Works Accountants Act, 1959.;

6.20 RETURN

6.20.1 Filing of Returns

Every assessee registered under Service tax provisions should file returns mandatorily electronically (w.e.f. 1-10-2011) as explained below:

Period	Due date (e-filing)	Return (must be filed in triplicate)	Person responsible to file	Remarks
1st April to 30th September	25th of October	ST-3 Every assessee shall submit the half-yearly return electronically w.e.f. 1-10 2011.	All assessees (provider or recipient of service as the case may be)	Due date is a public holiday, then next working day is the due date. One ST-3 can file for multiple services. 'Nil' return acceptable but no return will attract penalty.
1st October to 31st March	25th April	ST-3 Every assessee shall submit the half-yearly return electronically w.e.f. 1-10-2011.	All assessees (provider or recipient of service as the case may be)	Due date is a public holiday, then next working day is the due date. One ST-3 can file for multiple services. 'Nil' return acceptable but no return will attract penalty.
1st April to 30th September	25th of October	ST-3A Every assessee shall submit the half-yearly return electronically w.e.f. 1-10-2011.	All assessees to whom provisional assessment has been granted.	A statement giving details of the difference between the service tax deposited and the service tax liable to be paid for each month or quarter, as the case may be, in a memorandum accompanying the half-yearly return.
1st October to 31st March	25th April	ST-3A Every assessee has submit the half-yearly return electronically w.e.f. 1-10-2011.	All assessees to whom provisional assessment has been granted.	A statement giving details of the difference between the service tax deposited and the service tax liable to be paid for each month or quarter as the case may be in a memorandum accompanying the half-yearly return.

6.20.2 Service Tax Return Preparer (STRP)

With effect from Finance Act, 2008, dated 10-5-2008 a scheme of Service Tax Return Preparer being introduced in the service tax provisions.

A STRP shall assist the person or class of persons to prepare and furnish the return in such manner as may be specified in the Scheme.

Service Tax Return Preparer (STRP) being an individual, who has authorized to act as a service tax return preparer under the Scheme.

6.20.3 Preservation Period of Records and Documents

All records and documents concerning any taxable service, CENVAT transactions etc. must be preserved for a minimum period of 5 years immediately after the financial year to which such records pertain (Rule 5(3) of Service Tax Rules 1994.)

6.20.4 Revised Return

With effect from 1st March, 2008 (Rule 7B of the Service Tax Rules), an assessee is allowed to rectify mistakes and file Revised Return within 90 days from the date of filing of the original return. Revised return after 90 days not allowed. (w.e.f. 1.3.2007 to 29.2.2008 the time limit was 60 days).

This implies that Returns pertaining to the period prior to 1st March, 2007 can be revised without the time limit.

Example 60: X Ltd. filed the ST-3 return on 30th November 2015 for the period from 1st April 2015 to 30th September 2015. Subsequently on 1st February 2016, some mistakes were found in the ST-3 return which was originally submitted on 30th November 2015. Service tax authorities rejected the revised return filed by the X Ltd. on 5th February, 2016, since the revised return was filed by the assessee after 90 days from the due date of filing the return (i.e. 25th October, 2015). Is the action of the department correct?

Answer: No, the department action is not sustainable in the eyes of law. As per Rule 7B of the Service Tax Rules, 1 994, the time limit of 90 days for filing of revised return counts only from the date of filing of the original return and not from the due date for filing of original return as contained in the Explanatory Notes. Therefore, X Ltd. can file revised return by 5th February, 2016.

6.21 PENALTIES

Late fee (Penalty) in case of late filing of Form ST-3

Fee for Late filing of ST-3 (As per Rule 7C of Service Tax Rules, 1994)

If a person fails to furnish the ST-3 return within the due date [25th October and 25th April every year] he shall be liable to pay late fee (penalty) is as follows:

Delay upto 15 days ₹ 500

Delay upto 30 days ₹ 1,000

Delay beyond 30 days ₹ 1,000 + ₹ 100 per day subject to a maximum of ₹ 20,000 (w.e.f. 8-4-2011 ₹ 2,000 enhanced to ₹ 20,000)

Late fee should be paid at the time of filling the return without waiting for any communication or notice from the Department. However, filing of return cannot be refused for non-submission of evidence of payment of late fee along with the Return.

Other Penalties

Sl. No.	Types of penalty	Penalty (prior to 8-4-2011)	Penalty (w.e.f. 8-4-2011)
i.	Non-filing of Return Section 77 of the Finance Act, 1994)	Upto ₹ 5,000	Upto ₹ 10,000
ii.	Not obtaining registration (section 77 of the Finance Act, 1944)	₹ 200 per day for every day of default or ₹ 5,000 whichever is higher.	₹ 200 per day for every day of default or ₹ 10,000 whichever is higher, starting with the first day after the due date, till the date of actual compliance;
iii.	Non-maintenance of proper books of accounts (Section 77 of the Finance Act, 1994)	Upto ₹ 5,000	Upto ₹ 10,000
iv.	Non-appearance before Officers on issue of summons (Section 77 of the Finance Act, 1994)	₹ 200 per day for every day of default or ₹ 5,000 whichever is higher	₹ 200 per day for every day of default or ₹ 10,000 whichever is higher, starting with the first day after the due date, till the date of actual compliance;

Sl. No.	Types of penalty	Penalty (prior to 8-4-2011)	Penalty (w.e.f. 8-4-2011)
v.	Failure to pay tax electronically when so required to pay (Section 77 of the Finance Act, 1994)	Upto ₹ 5,000	Upto ₹ 10,000
vi.	Issuing incorrect invoice or not accounting invoices in books (Section 77 of the Finance Act, 1994)	Upto ₹ 5,000	Upto ₹ 10,000
vii.	Section 78A – Evasion of service tax, – Isuance of invoice without provision of service, – availment of Cenvat Credit without recipt of service of goods, or – Service tax collected remaining overdue for more than 6 months.		Section 78A is being introduced, to make provision for imposition of penalty on director, manager, secretary or other officer of the company, who is in any manner knowingly concerned with specified contraventions. Penalty upto ₹ 1 Lakh
viii.	Fraud or suppression of acts (Section 78 of the Finance Act, 1994): Wrongful utilization of Cenvat credit by reason of fraud, collusion or any willful mis-statement etc. with the intent to evade the payment of service tax, the provider of service shall be liable to pay penalty in terms of the provisions of Section 78 of the Finance Act, 1994.	A show cause notice has been issued under Section 73(1A) of the Finance Act, 1994 by demanding Minimum 100% of service tax. Maximum 200% of service tax. The penalty will be reduced to 25%, if tax, interest and penalty paid within 30 days from the date of receipt of order of Central Excise Officer.	100% of the service tax, where the true and complete details of the transactions are not recorded in the specified records. This penalty cannot be waived. Penalty reduced to 15% of tax, if tax, interest and reduced penalty also paid within 30 days of receipt of notice. Penalty reduced to 25% of tax, if tax, interest and reduced penalty also paid within 30 days of receipt of order. Penalty cannot exceed 50% of service tax in case transactions recorded in specified records between 08.04.2011 to 14.05.2015. Notices issued on or after 14.05.2015 or order passed on or after 14.05.2015, period of 30 days to be reckoned from 14.05.2015.
ix.	During the Department audit or verification of records of the assessee, they found short payment of service tax or sometimes, the amount erroneously refunded to the assessee. If all such transactions are completely recoded in the specified records (Section 73(4A) of the Finance Act, 1994 w.e.f. 8-4-2011). This provision is applicable to those assessees who have no intention to evade tax.		Omitted w.e.f 14.05.2015.

Clause (4B) inserted in Section 73 to prescribe time limit for determining the amount of Service Tax due in terms with Show Cause Notice

A time limit has been prescribed for completing the adjudication process and determining Service Tax dues in terms with Show Cause Notice issued under Section 73(1) of the Act. However, the proposed amendment comes in a rider stating 'where it is possible to do so', which allows authorities to by-pass the time limit. The following time limit has been prescribed for the adjudication process:

Sl. No.	Period of Limitation	Time Limit
1	Normal Period of Limitation i.e. up to 18 months	6 months from the date of notice
2	Extended Period of Limitation i.e. up to 5 years	12 months from the date of notice

6.22 ADJUDICATION & APPEALS

6.22.1 Adjudication

(i) Central Excise Officers have been empowered to adjudicate in following –

(*a*) Demand of service tax and its recovery - section 73.

(*b*) Rectification of mistake by amending own order - section 74.

(*c*) Imposition of penalty - section 83A

(*d*) Refund of service tax - section 11B of Central Excise Act made applicable to Service Tax.

(ii) **Time limit for issue of show cause notice -** If it is found that assessee has paid less tax, department will issue a show cause notice cum demand.

If any service tax is not levied or not paid or short levied or short paid or erroneously refunded, Central Excise Officer shall issue a show cause notice for demand can be made within 18 months from 'relevant date' [section 73(1)].

If such short payment etc. was by reason of fraud, collusion, wilful mis-statement, suppression of facts or contravention of any provision of Finance Act, 1994 or rules, show cause notice can be issued within five years [*proviso* to section 73(1)]. If notice is issued under 5 years, the demand for normal period would not Service — S.C. Decision in the case of Alcobex Metals. After considering the representation, Central Excise Officer will determine the service tax payable. Such tax cannot be more than the amount specified in show cause notice. Thereupon, the person shall pay the amount so determined [section 73(2)].

(iii) **Voluntary Payment before receipt of show cause notice -** Assessee may pay such tax on the basis of his own ascertainment or on the basis of tax ascertained by Central Excise Officer, before issue of show cause notice. After payment of tax, assessee should inform the Central Excise Officer in writing about such payment, and then the central excise officer shall not issue any show cause notice under section 73(1) in respect of service tax so paid [section 73(3)].

(iv) **Rectification -** The Central Excise Officer who has passed order (of assessment or demand or penalty) can rectify any mistake apparent from the record, within two years of the date in which the order was passed. The mistake must be 'apparent from the records'.

(v) **Revision -** The Commissioner of Central Excise can revise the orders passed by adjudicating authority subordinate to him. The revision order can be passed any time within two years of the original order, but not afterwards. No revision can be made if appeal against such order is pending with Commissioner (Appeals) [section 84]. Appeal against the order of Commissioner (after revision) lies with CESTAT under section 86.

In case of assessee appeal also, appellate tribunal can admit an appeal or permit the filing of memorandum of cross objections after the expiry of the relevant period.

6.22.2 APPEALS

(i) Appeal to Commissioner (Appeals) - Appeal to Commissioner (Appeals) can be made against order of any Central Excise Officer subordinate to Commissioner in respect of demand, interest or penalty or denial of refund of service tax. Appeal should be in prescribed form and duly verified. Appeal must be filed within three months from date of receipt of order. Delay upto three months can be condoned by Commissioner (Appeals). The procedures and powers will be similar to those under Central Excise. [section 85 of Finance Act, 1994].

(ii) Appeal to Tribunal - Appeal to CESTAT (Tribunal) can be made against order of Commissioner passed by him under section 73, 83A or order of Commissioner (Appeals) passed by him under section 85 [order in appeal from order of AC/DC] by assessee or the department. Appeal has to be filed within three months from date of receipt of order by assessee, Board or Commissioner as the case may be. [section 86 of Finance Act, 1994].

Tribunal can condone the delay in filing appeal on showing sufficient cause. Appeal has to be accompanied with prescribed fees, if appeal is by the assessee. Tribunal is final fact finding authority.

Where an order, relating to a service which is exported, has been passed under section 85 and the matter relates to grant of rebate of service tax on input services, or rebate of duty paid on inputs, used in providing such service, such order shall be dealt with in accordance with the provisions of section 35EE of the Central Excise Act.

(iii) Appeals to HC/SC – If issue involves classification or valuation, appeal lies with Supreme Court. If issue does not involve classification or valuation dispute, appeal lies with High Court only on substantial question of law.

PRACTICAL PROBLEMS

Point of Taxation:

Example 61: Sun Academy Pvt. Ltd., is providing commercial training services since, 2009. During the year 2014-15 service tax liability arises to pay was ₹ 12,00,000. However, service tax paid was paid ₹ 8 lacs after adjustment of CENVAT CREDIT of ₹ 4 lacs. In the month of April 2015, 60 students were joined for pursing Point of Taxation Rules (from 1st April'15 to 10th April'15). Fee per student is ₹ 3,000 (inclusive of Service tax) paid by all students the month of June 2015. Service Tax @14.5% paid on 5th july 2015. Calculate the following:

(a) Point of Taxation

(b) Due Date

(c) Service Tax liability

(d) Interest if any

Answer:

(a) Point of taxation = April 2015

(b) Due date = 6th May 2015

(c) Service tax = ₹ 22,795 (i.e. 3,000 x 60 x 14.5/114.5)

(d) Interest = ₹ 586 (i.e. 19,800 x 18/100 x 60/365)

Example 62: State briefly whether the following service under the Finance Act, 1994 relating to service tax are taxable service.

(a) Service provided in the State of Rajasthan by a person having a place of business in the State of Jammu and Kashmir.

(b) Service provided from India for use outside India

(c) Service provided from outside India and received in India by Individual otherwise than purpose of use in business or commerce.

(d) Service provided to an Export Oriented Unit

Answer:

(a) These are taxable services. Services rendered within India (except in the state of Jammu and Kashmir) are come under the service tax net, provided these services are taxable services.

(b) These services can be considered as export of services, which are exempted from the service tax liability.

(c) Services in the nature of import are taxable if these are imported for the purpose of business or commerce. Services imported for the purpose of personal use by individuals are exempted from service tax.

(d) Service provided to export oriented undertaking is liable to service tax. Service rendered to EOU or supplies of services by EOU in domestic market is not presently exempt from service tax.

Example 63: Answer the following with reference to the Finance Act, 1994 as amended relating to applicability of service tax:

Service provided by educational institutions like IIMs by charging a fee from prospective employers like corporate houses regarding recruiting candidates through campus interviews.

Answer:

Manpower recruitment or supply agency is defined as 'any person engaged in providing any service, directly or indirectly, in any manner for recruitment or supply of manpower, temporarily or otherwise, to a client.

Educational institutes like IITs, IIMs etc. fall within the above definition. Thus, service tax is liable to be paid on services provided by such institutes in relation to campus recruitment.

Example 64: Answer the following:

(a) A particular service has been brought into service tax net with effect from 1-5-2015. Mr. Vignesh has provided this service on 10-05-2015 and invoice has been issued on the same date. The payment for the same was received on 30-4-2015. Is service tax payable on the same?

(b) Mr. Saravanan has collected ₹ 15,000 as service tax from a client mistakenly, even though no service tax is chargeable for such service. Should the amount so collected be remitted to the credit of the Central Government?

(c) Briefly explain the nature of the service tax

Answer:

(a) As per Rule 5(b) of the Point of Taxation Rules, 2011, no tax shall be payable if the payment has been received before the service becomes taxable and invoice has been issued within the period referred to in rule 4A of the Service Tax Rules, 1994.

As per rule 4A of the Service Tax Rules, 1994, an invoice is required to be issued within 30 days from the date of completion of service or from the date of receipt of any payment of taxable service, whichever is earlier.

In the given case, Mr. Vignesh is not liable to pay service tax.

(b) Section 73A of the Finance Act, 1994 casts an obligation on every person who has collected service tax from any recipient of service in any manner as service tax, to remit the same to the credit of the Central Government. On account of this provision, where any person has collected any amount, which is not required to be collected from any other person, in any manner as representing service tax, he should also immediately pay the amount so collected to the credit of the Central Government.

Hence, Mr. Saravanan has to remit the service tax collected by him on the non taxable services to the credit of Central Government of India.

(c) Section 70 of the Finance Act, 1994 enjoins that every person liable to pay service tax shall himself assess the tax due on the services provided by him and shall furnish a return to the Superintendent of Central Excise.

Example 65: Ms. P rendered taxable services to a client. A bill of ₹ 40,000 were raised on 29-4-2015. ₹15,000 were received from the client on 1-5-2015 and the balance on 23-5-2015. No service tax was separately charged in the bill.

(a) Is Ms. P liable to pay service tax, even though the same has not been charged by her?

(b) If so, what is the value of taxable services and the service tax?

(c) Due date of payment of service tax?

Note: previous year turnover is ₹ 25 lakhs

Answer:

(a) Ms. P is liable to pay service tax even though she has not collected the service tax from his client, by considering the service tax is inclusive in the value of the bill. The point of taxation is 29-4-2015. It means she is liable to pay service tax for the month of April, 2015.

(b) Service tax liability is as follows:

Value of taxable services = 40,000 x 100/114.5	=	₹ 34,934
Service tax liability = 34,934 x 14.5/100	=	₹ 5,066

(c) Due date of payment of service tax is 6th July 2015.

Example 66: Mr. Vasudevan is a practicing Cost Accountant, has rendered freely, a service to a client which is taxable, but has not charged or received any fee from a client. Is service tax payable on such free services?

Answer:

Service tax is payable when services are provided for consideration as per Section 67 of the Finance Act, 1994. Moreover the charging section 66 provides that service tax is chargeable on the value of taxable service. Hence, if the value is Free no service tax is payable even though the service may be taxable. However, this principle applies only when there is really a 'free service' and not when its cost is recovered through different means.

Example 67: Mr. Harish, a consulting engineer raised a bill of ₹2,20,600 (including service tax @14.5%) on his client for consulting services rendered by him in the month of June, 2015. A partial payment of ₹ 1,65,450 was received by Mr. Harish in the month of September 2015 as full and final settlement. Compute the service tax amount payable by Mr. Harish and the due date by which service tax can be deposited. Previous year taxable services are ₹ 74 lakhs.

Answer:

Service tax is payable only on the basis of point of taxation rules. Hence, service tax is required to be paid on the entire bill value. The service tax is required to be paid on the value of service which is actually billed in the month of June 2015.

Value of taxable services (₹ 2,20,600 x 100/114.5)	=	₹ 1,92,664
Service tax payable on ₹ 1,92,664 @14.5%	=	₹ 27,936
Total	=	₹ 2,20,600

Therefore, service tax payable to the government ₹ 27,936.

Due dates of payment of service tax is quarterly for an individual. Therefore, due date is on or before 6th July 2015.

Tax Dedcuted at Source:

Example 68: A Ltd. provided Information Technology & Software services to B Ltd. in the month of July 2015. A bill inclusive of Service Tax issued in the month of July 2015. B Ltd paid ₹ 24,81,750 (after deducting TDS under sec 1 94J of the Income Tax Act, 1961 @10% towards TDS) in the month of August, 2015. You are required to calculate:

(a) Service tax liability

(b) Due date of payment of service tax.

Answer: **(Amount in ₹)**

(a)	Net payment received	=	24,81,750 = 90%
	TDS @ 10%	=	2,75,750 =10%
	Total bill value		27,57,500

Service tax liability = ₹ 27,57,500 x 14.5/114.5 = 3,49,203

(b) Due date of payment of service tax in case of electronically payment through interest banking is on or before 6th of August 2015.

Due date of payment of service tax in case of other than e-payment is on or before 5th August 2015.

Interest

Example 69: Mr. X practicing Chartered Accountant received ₹ 20,00,000 in the June 2015. He paid service tax on 26th July 2015 by way of e-payment. Gross receipts in the year 2014-15 were ₹ 25 lakhs.

You are required to calculate Interest on delay payment of service tax.

Answer :

Service tax @14.5% on ₹ 20,00,000 = ₹ 2,90,000.

Due date of payment of service tax- 6th July, 2012.

No. of days delay = 20 days

Interest = ₹ **2,384 (i.e.₹ 2,90,000 x 15/100 x 20/365)**

Example 70: What is the rate of interest for late filing of return (i.e. V Form ST-3)?

Answer :

No interest will be levied in case of late filing of return Form ST-3.

Interest for Delayed Payment of Service Tax.

Example 71: X Ltd. is liable to pay service tax of ₹ 1,00,000 on or before 6th July 2015 but he paid it on 16th July 2015. What is the penalty for non-payment or delayed payment of service tax? Can this penalty be waived or reduced?

Answer:

(1) Where service tax has not been levied or paid, or has been short-levied or short-paid, or erroneously refunded, for any reason, other than the reason of fraud or collusion or wilful mis-statement or suppression of facts or contravention of any of the provisions of this Chapter or of the rules made thereunder with the intent to evade payment of service tax, the person who has been served notice under sub-section (1) of section 73 shall, in addition the service tax and interest specified in the notice, be also liable to pay a penalty not exceeding ten per cent of the amount of such service tax:

Provided that where service tax and interest is paid within a period of thirty days of –

(i) the date of service of notice under sub-section (1) of section 73, no penalty shall be payable and proceedings in respect of such service tax and interest shall be deemed to have been concluded;

(ii) the date of receipt of the order of the Central Excise Officer determining the amount of service tax under sub-section (2) of section 73, the penalty payable shall be twenty-five per cent of the penalty imposed in that order, only if such reduced penalty is also paid within such period.

(2) Where the amount of penalty is increased by the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be, over the above the amount as determined under sub-section (2) of section 73, the time within which the reduced penalty is payable under clause (ii) of the proviso to sub-section (1) in relation to such increased amount of penalty shall be counted from the date of the order of the Commissioner (Appeals), the Appellate Tribunal or the court, as the case may be.]

Penalty for Late Filing of Return:

Example 72: SM Ltd. filed its service tax returns for the half years ending on September 2014 and March 2015 on 25-11-2014 and 31-7-2015. The two half yearly returns show a service tax liability of ₹ 2,00,000 and ₹ 1,00,000 respectively. Is any late fee/fine payable by SM Ltd.? If yes, what is the quantum of such fee in both the cases?

Will your answer be different if SM Ltd. files a nil return for the half year ending on September 2014?

Answer:

Form ST-3 half yearly – due dates

25th October for the first half year ending 30th September

25th April for the second half year ending 31st March

Actual No. of days delay for the first half year return = 31 days

(Oct 6 days + Nov 25 days)

Therefore, penalty is ₹ 1,100

Actual No. of days delay for the 2nd half year return = 97 days

(April 5 days + May 31 days + June 30 days + July 31 days)

Upto 30 days of delay ₹ 1,000 plus ₹ 100 per day of delay subject to maximum of ₹ 20,000 (w.e.f. 8-4-2011) Therefore, penalty is ₹ 7,700.

Penalty can be reduced or waived if the ST-3 return belongs to nil return.

Study Note - 7

ADJUDICATION, PENALTIES AND APPEALS IN INDIRECT TAXES

This Study Note includes

7.1 COMMON TOPICS IN INDIRECT TAXES

Three major indirect taxes, viz. Central Excise, Service Tax and Customs are being administered by single authority i.e. Central Board of Excise and Customs (CBE&C) under Ministry of Finance, Government of India. Final departmental appellate authority i.e. Tribunal is common. It is, therefore, natural that basic thinking and approach is same in all the legislations connected with these three taxes.

Many provisions of Central Excise are made applicable to service tax. Many provisions of customs law have been made applicable to Central Excise.

7.1.1 Provisions in respect of Demands, Refunds, Penalties, Appeals are Common or Similar

Provisions relating to demands, refunds, penalties and appeals are either common in all the three legislations or at least they are similar.

7.1.2 Assessee and Assessment

Assessment means determining the tax liability.

Duty is paid by the manufacturer on his own while clearing goods from the factory/warehouse, on 'self assessment'. The assessee himself has to determine classification and valuation of goods and pay duty accordingly.

Rule 2(b) of Central Excise Rules states that 'assessment' includes self-assessment of duty made by the assessee and provisional assessment made under Rule 7.

'Assessee' - Rule 2(c) of Central Excise Rules states that 'assessee' means any person who is liable for payment of duty assessed or a producer or manufacturer of excisable goods or a registered person of a private warehouse in which excisable goods are stored, and includes an authorized agent of such person.

Self Assessment - The assessment under Central Excise is basically an Invoice based self-assessment, except in case of cigarettes. Rule 6 of Central Excise Rules provides that the assessee shall himself assess the duty payable on excisable goods, except that that in case of cigarettes, the Superintendent or Inspector of Central Excise shall assess the duty payable before removal of goods.

The assessee has to submit monthly return in ER-1/ER-2/ER-3 form. The return has to be along with 'Self Assessment Memorandum', where Assessee declares that (a) the particulars in ER-1/ER-2/ER-3 return are correctly stated (b) Duty has been assessed as per provisions of Section 4 or 4A of CEA (c) TR-6 challans by which duty has been paid are genuine.

In case of service tax also, Section 70(1) of Finance Act, 1994 provides that every person liable to pay service tax shall himself assess the tax due and file return. The ST-3 return filed by assessee contains a 'Self-Assessment Memorandum'. Self assessed tax remaining unpaid to be recovered alongwith interest.

7.1.3 Scrutiny of Correctness of Duty

After submission of return by assessee, first stage dealer and second stage dealer, the 'proper officer' will scrutinise the return on the basis of information contained in the return and further enquiry as considered necessary. The manner of scrutiny will be prescribed by CBE&C [Rule 12(3) Central Excise Rules – inserted w.e.f. 1-4-2005].

Every assessee shall make available to 'proper officer' all documents and records for verification as and when required by such officer [Rule 12(4)].

7.1.4 Assessment Order in Customs but not in Excise and Service Tax

In case of customs, Bill of Entry (in case of imports) and Shipping Bill (in case of exports) is an assessment order. If the valuation shown by assessee is not accepted by department, order with reasons will have to be issued within 14 days. Appeal can be filed against the order. Mere filing of refund claim is not sufficient.

In case of excise and service tax, the assessee is required to file returns. Excise officers will not 'assess' the duty i.e. assessment order is not issued. If the officers are of opinion that there is short payment, show cause notice cum demand will have to be issued.

7.1.5 Provisional Assessment

Rule 7 of Central Excise Rules make provisions in respect of provisional assessment. Provisional assessment can be requested by the assessee. Department cannot itself order provisional assessment.

Final assessment will be made later by Assistant/Deputy Commissioner after getting the required details. In case of such provisional assessment, demand can be raised within one year after the provisional assessment is finalised.

Overview of Provisions of Provisional Assessment - An assessee can request for provisional assessment in following circumstances – (a) Assessee is unable to determine the value of excisable goods in terms of Section 4 of CEA on account of non-availability of any document or information *or* (b) Assessee is unable to determine rate of duty applicable.

In aforesaid cases, assessee may request Assistant/Deputy Commissioner in writing giving reasons for provisional assessment of duty. [Assessee should give reason why he wishes to have provisional assessment]. After such request, the Assistant/Deputy Commissioner may by order allow payment of duty on provisional basis. The Assistant/Deputy Commissioner shall also specify the rate or value at which the duty will be paid on provisional basis. [Rule 7(1)].

Payment of duty on provisional basis will be allowed subject to execution of bond for payment of differential duty [Rule 7(2)]. After that Assistant/Deputy Commissioner should pass order for final assessment within 6 months from date of order of provisional assessment. This period can be extended by further 6 months by Commissioner and further without any time limit by Chief Commissioner [Rule 7(3)]. If differential amount is payable, interest is payable [Rule 7(4)]. If excess amount was paid, it is refundable with interest [Rule 7(5)]. The refund is subject to provision of Unjust Enrichment [Rule 7(6)].

Finalisation of Provisional Assessment

AC/DC is required to pass order of final assessment after getting relevant information, within six months of date of communication of his order allowing provisional assessment. The period of 6 months can be extended by Commissioner of CE, on making a specific request, for reasons to be recorded in writing. Extension beyond one year for further period can be granted only by Chief Commissioner. [Rule 7(3) of Central Excise Rules].

No time limit for finalisation in case of customs – In *Shakti Beverages* v. *CC* 2003(153) ELT 445 (CEGAT 3 member bench), it was held that there is no time limit for finalising provisional assessment. The only question that can be considered by Tribunal is whether due to delay in finalising provisional assessment whether appellant has suffered any prejudice and whether there is violation of principles of natural justice. [The principle should apply to Central Excise also].

Interest payable/receivable - If differential duty is found to be payable, interest as specified in Section 11AA of the Central Excise Act will be payable by assessee from first day of the month succeeding the month *for which* such amount is determined till date of payment thereof. [Rule 7(4)].

Since the word used is '*for*', interest is payable from first day of next month after clearance of goods. For example, if goods were cleared on 15th October 2003 under provisional assessment and assessment was finalized on 25th March 2004, interest will be payable from 1st November, 2003 till date of payment.

If differential amount is found to be refundable to assessee, it shall be refunded with interest at rate as specified in Section 11BB. The period for payment of Interest will be same as per section 11BB. Thus, interest is payable by department is on the same basis as payable by assessee, i.e. not from date of finalisation of provisional assessment, but from month next to the month on which duty was provisionally paid. [Note that u/s 11BB, interest on delayed refund is payable only three months after filing of refund application. This provision does not apply to refund obtainable after finalization of Provisional Assessment].

Interest in case of customs - Section 18 of Customs Act (inserted w.e.f. 13-7-2006) makes provision for payment of interest after finalization of provisional assessment.

Refund after finalization of assessment

If duty is paid on provisional basis, refund claim can be filed within one year after duty is adjusted after final assessment. [*Explanation* B(eb) to Section 11B].

Refund subject to provision of Unjust Enrichment - Rule 7(6) of Central Excise Rules clarifies that refund is subject to provisions of 'Unjust Enrichment', i.e. refund will be granted to manufacturer if he has not passed on incidence of duty to another person – confirmed in *Hindustan Lever* v. *CCE* (2004) 171 ELT 12 (CESTAT).

In case of customs duty, there was no parallel provision in respect of provisional assessment. Section 18(5) of Customs Act inserted by Taxation Laws (Amendment) Act w.e.f. 13-7-2006, has made provision for unjust enrichment in case of customs duty refund when there was provisional assessment.

7.2 ADJUDICATION IN INDIRECT TAXES

Adjudicate means to hear or try and decide judicially and adjudication means giving a decision. As per Oxford Dictionary, 'adjudicate' means deciding judicially (regarding a claim etc.), pronounce.

Excise and Customs Authorities are empowered to determine classification, valuation, refund claims and the tax/duty payable. They are also empowered to grant various permissions under rules and impose fines, penalties, etc., and confiscate offending goods. Since the authorities are departmental officers, the process is called "departmental adjudication".

They are required to follow principles of natural justice. Their adjudicating powers are prescribed under Act and departmental circulars Their orders are appealable.

These are 'quasi judicial authorities' and they are not bound by any trade notice or instructions of superiors.

Uncontrolled authority may cause great damage to an assessee and hence opportunity of appeal against the order has been provided. The topmost authority of departmental appeal is "Tribunal" in Excise and Customs. The decision of the Tribunal is final as far as the departmental remedy of appeal is concerned. Provisions are available for appeal/reference to High Court/Supreme Court in limited cases. Needless to mention, writ jurisdiction of High Court and Supreme Court is independent of any provision/s of the Excise Act and Writ Petition can be filed in High Court/SLP in Supreme Court irrespective of any provision of Excise Act.

7.2.1 Principles of Natural Justice

Basic requirements of principle of natural justice are – (a) Full information about charges, (b) Allowing party to state his defence (Personal Hearing), (c) Unbiased authority & (d) Order with reasons.

7.2.2 Adjudicating Authority

(i) Any authority competent to pass any order or decision under Central Excise Act.

(ii) Commissioner (appeals) and CBEC are not adjudicating authority.

(iii) If amount of duty or Cenvat credit involved is up to ₹ 5,00,000, such demand can be made by Deputy/Assistant Commissioner of Central Excise.

(iv) If amount of duty or Cenvat credit involved is above ₹ 5,00,000 and upto ₹ 50,00,000 such demand can be made by Additional Commissioner of Central Excise.

(v) Demand of duty or demand of CENVAT credit of any amount (i.e. without any upper limit) can be made by Commissioner or Commissioner of Central Excise.

(vi) Gazetted officer rank starts from Superintendent of Central Excise.

7.2.3 Remission of Duty (Rule 21 of the Central Excise Rules, 2002)

Remission of Duty means duty levied but exempted from payment of duty with the permission of Adjudicating Authority. Where it is shown to the satisfaction of the Commissioner that goods have been lost or destroyed by natural causes or by unavoidable accident or are claimed by the manufacturer as unfit for consumption or for marketing, at any time before removal, he may remit the duty (i.e. no demand of duty) payable on such goods, subject to such conditions as may be imposed by him by order in writing (Rule 21 of the Central Excise Rules, 2002).

Note: Remission of duty is not allowed in case of theft, since the goods are available for consumption somewhere else.

Procedure for claiming Remission of Duty :

(i) A manufacturer has to make an application in duplicate to the Range Officer indicating complete details of the goods and reasons for destruction, along with the proof that the goods have become unfit for consumption or for marketing such as report of chemical test or any other test, conducted by a Government recognized laboratory.

(ii) The application will be quickly processed by the Range Office. In case the matter falls within the competency of superior officer, he will forward the application along with his recommendation to the Deputy/Assistant Commissioner within 15 days of receipt.

(iii) The Deputy/Assistant Commissioner will scrutinise the application and based upon the information given by the assessee, if found in order, allow destruction of goods and remission of duty, if the case relates to his competency. Otherwise, he will forward the application with his remarks to the superior authority competent to give permission for destruction and remission (Additional/Joint Commissioner or Commissioner, as the case may be) within 3 days.

(iv) Where only physical verification is required, the same may be conducted by the remission granting authority (proper officer), as specified above and upon his satisfaction, destruction of goods and remission of duty may be allowed.

(v) As far as possible, destruction should be made inside the factory.

(vi) The goods are rendered unfit for consumption or marketing should be accepted and necessary permission should be granted within a period of 21 days or earlier, if possible. Where samples are drawn, such permission should be granted within 45 days.

Example 1: B Ltd. was engaged in the manufacture of lead and zinc concentrates. At the time of carrying out the physical stock taking, some difference was found between the physically verified stock and the stock as per the books. According to B Ltd., this difference was due to de-bagging, shifting of concentrates, seepage of rain water and storage and loading on trucks. B Ltd. applied for the remission of duty under rule 21 of the Central Excise Rules, 2002. Revenue claimed that the shortage could have been avoided or minimized by the assessee, as they were neither due to natural causes, nor due to unavoidable accident. Thus, the prayer for remission was declined.

Answer:

In the case of UOI v Hindustan Zinc Limited 2009 (233) ELT 61 (Raj), *the High court said that* Revenue's claim is not valid in law. B Ltd can get benefit under Rule 21 of the Central Excise Rules 2002.

7.2.4 Rebate of Duty

Rebate of duty can be under stood as duty draw back. Where any goods are exported, the Central Government may, by notification, grant rebate of duty paid on such excisable goods or duty paid on materials used in the manufacture or processing of such goods and the rebate shall be subject to such conditions or limitations, if any, and fulfillment of such procedure, as may be specified in the notification.

7.2.5 Recovery of duties not levied or not paid or short levied or short paid or erroneously refunded [Section 11A of Central Excise Act, 1944/Section 28 of Customs Act / Section 73 of Finance Act, 1994]

Show Cause Notice under section 11A(1)(a) of Central Excise Act provides that a Central Excise authority can, within ONE year from *relevant date*, serve show cause notice on assessee chargeable to duty if—

(a) Central Excise duty has not been paid or short paid

(b) Central Excise duty erroneously refunded.

> The Apex Court held that the time-limit under section 11A of the Central Excise Act, 1944 is not applicable to recovery of dues under compounded levy scheme [Hans Steel Rolling Mill v. CCEx., Chandigarh 2011 (265) E.L.T. 321 (S.C.)].

Section 28 of the Customs Act,1962 also deals with recovery of duties not levied or short levied or erroneously refunded. In the case of *C.Cus.* v *Sayed Ali* 2011 (SC) the Apex Court held that—

- Director General of Revenue Intelligence or
- Director General of Central Excise Intelligence
- Are not eligible for issuing show cause notices. However, w.e.f 16.9.2011 the law amended retrospectively by providing validity to those show cause notices issued by the Director General of Revenue Intelligence or, Director General of Central Excise Intelligence.

Provided that the proper officer shall not serve such show cause notice, where the amount involved is less than rupee one hundred.

Duty and interest paid before issue of show cause notice Section 11A(1)(b)

As per section 11A(1)(b), the person chargeable with duty may, before service of notice under Section 11A(1)(a), pay on the basis of his own ascertainment of such duty or the duty ascertained by the Central Excise Officer, the amount of duty along with interest payable thereon under section 11AA.

Description	**Relevant section**	**Time period to issue notice**	**Excise duty**	**Interest @18%p.a**	**Penalty equal to the duty specified in the notice**
Duty paid along with interest before issue of show cause notice (other than fraud)	Section 11A(1) (b)	One year from the relevant date, if required	Liable to pay	Liable to pay	No penalty is required to pay

Intimation to the Central Excise Officer under section 11A(2): The person who has paid the duty under section 11A(1)(b), shall inform the Central Excise Officer of such payment in writing, who, on receipt of such information, shall not serve any notice under section 11A(1)(a) or any penalty leviable under the provisions of this Act or the rules made thereunder. It means penalty cannot be levied.

Show cause notice under section 11A(3): where the Central Excise Officer is of the opinion that the amount paid under section 11A(1)(b), falls short of the amount actually payable, then he shall proceed to issue the notice as provided under section 11A(1)(a) in respect of such amount which falls short of the amount actually payable in the manner specified under that sub-section and the period of ONE year shall be computed from the date of receipt of information under section 11A(2).

Show Cause Notice under section 11A(4) in case of fraud: the Central Excise Officer can also be issued a show cause notice within FIVE years from relevant date if Central Excise duty has not been paid by way of fraud, or collusion, or willful misstatement and suppression of facts, or contravention of any of the provisions of this Act or the rules made thereunder with intent to evade payment of duty. Show cause can be issued by demanding the amount of duty along with interest payable thereon under Section 11AA and a penalty equivalent to the duty specified in the notice.

Description	Relevant section	Time period to issue notice	Excise duty	Interest @18%p.a (1-4-2011)	Penalty (w.e.f. 8-4-2011)
Show Cause issued under on the grounds of fraud	Section 11A(4)	5 years from the relevant date	Liable to pay	Liable to pay	Liable to pay equal to the duty specified in the notice

Fraud noticed during the audit, investigation but the details are available in the specified records Section 11A(5): [Omitted w.e.f. 14.05.2015]

Fraud noticed during the audit, investigation but the details are available in the specified records, where as dues has been paid before issue of show cause notice Section 11(6): [Omitted w.e.f. 14.05.2015]

Section 11A is being amended to insert sub-section (7A) providing that service of a statement containing details of duty not paid, short levied or erroneously refunded shall be deemed to be service of notice under sub-section (1) or (3) or (4) of this section.

According to section 11A (8) while computing the period of ONE year or FIVE years the period during which there was any stay by an order of the court or tribunal in respect of payment of such duty shall be excluded.

As per section 11A(9) if the department has not been established against the person to whom notice was issued under section 11A(4) i.e. fraud or collusion or any willful mis-statement or suppression of facts or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, then any Appellate Authority or Tribunal or Court concludes that the notice issued by the Central Excise Officer shall determine the duty of excise payable by such person for the period of ONE year, deeming as if the notice were issued under Section 11A(1)(a).

As per section 11A(10) the Central Excise Officer shall determine the amount of duty of excise due from such person not being in excess of the amount specified in the show cause notice. The Central Excise Officer can do so after allowing the concerned person an opportunity of being heard.

Under section 11A(11) the Central Excise Officer shall determine the amount of duty of excise under section 11A(10) within SIX months from the date of notice where it is possible to do so, in respect of cases falling under section 11A(1). Cases falling under section 11A(4), within ONE year from the date of notice.

As per section 11A(12) where the Appellate Authority or Tribunal or Court modifies the amount of duty of excise determined by the Central Excise Officer under section 11(10), then the amount of penalties and interest under this section shall stand modified accordingly, taking into account the amount of duty of excise so modified.

As per section 11A(13) where the amount as modified by the Appellate Authority or Tribunal or Court is more than the amount determined under section 11A(10) by the Central Excise Officer, the time within which the interest or penalty is payable under this Act shall be counted from the date of the order of the appellate authority or tribunal or court in respect of such increased amount.

As per section 11A(14) where an order determining the duty of excise is passed by the Central Excise Officer under section 11A, the person liable to pay the said duty of excise shall pay the amount so determined along with the interest due on such amount whether or not the amount of interest is specified separately. It means section 11A and 11AA goes hand-in-hand.

As per section 11A(15) where interest alone is payable has not been paid or part paid or erroneously refunded, then section 11A(1) to (14) shall apply, mutatis mutandis.

Important points:

(i) If the Court has issued a Stay Order for recovery of amount, the period during which the stay order is in operation will be excluded for calculation of the time limit.

(ii) If demand has been raised without show cause, notice is invalid and unsustainable. At the same time penalty cannot be imposed if show cause notice does not contain proposal for penalty.

(iii) While interpreting section 32L(3), the Gujarat High Court held that for working out the time limit prescribed under section 11A for recovery of duties, the period commencing from the date of application to the Settlement Commission to the date of receipt of the order under section 32L by the adjudicating authority, shall be excluded Vishwa Traders Pvt. Ltd. v UOI 2009 (241) ELT 164 (Guj). Section 32L, deals with sending back a case to proper officer if applicant has not co-operated with the Settlement Commission.

(iv) *Relevant Date:* it means it may be any one of the following:

  (a) date of actual filling of monthly return, or

  (b) Date on which return should have been filed, when required to be filed but not filed, or

  (c) If no return is required to be filed under the Central Excise, then the date of payment of duty, or

  (d) In case of provisional assessment, relevant date is the date of adjustment of duty after final adjustment.

  (e) In case of erroneous refund, date of such refund.

  (f) In the case where only interest is to be recovered, the date of payment of duty to which such interest relates

7.2.6 Protective Demand

It means issue show-cause notice-cum-demand in time, so that it does not get time barred, specially in case of receipt of audit objections, protective demands should be issued in time.

7.3 ENFORCEMENT POWERS OF REVENUE OFFICERS

7.3.1 Powers of Central Excise Officers

i. Power to access registered premises: As per Rule 22(1) of Central Excise Rules, 2002, an officer empowered by the Commissioner in this behalf shall have access to any premises registered under these rules for the purpose of carrying out any scrutiny, verification and checks as may be necessary to safeguard the interest of revenue.

ii. Power to stop and search: As per Rule 23 of Central Excise Rules, 2002, any Central Excise Office, may search any conveyance carrying excisable goods in respect of which he has reason to believe that the goods are being carried with the intention of evading duty.

iii. **Power to detain or seize goods:** As per Rule 24 of Central Excise Rules, 2002, if a Central Excise Officer, has reason to believe that any goods, which are liable to excise duty but no duty has been paid thereon or the said goods were removed with the intention of evading the duty payable thereon, the Central Excise Officer may detain or seize such goods.

iv. **Power to delegate authority:** As per Section 12E(1) of Central Excise Act, 1944, a Central Excise Officer may exercise the powers and discharge the duties conferred or imposed under this Act on any other Central Excise Officer who is sub-ordinate to him.

Notwithstanding anything contained in sub-section (1), the Commissioner of Central Excise (Appeals) shall not exercise the powers and discharge the duties conferred or imposed on a Central Excise Officer other than those specified in section 14.

v. **Power to arrest:** As per the provisions of Section 13 of the Central Excise Act, 1944 the central excise officer not below the rank of inspector can arrest any person whom he has a reason to believe to be liable to punishment under the Central Excise Law. However, such an arrest can be only with the prior approval of Commissioner of Central Excise. The arrested person must be produced before the Magistrate within twenty four hours of the arrest.

According to Section 14 of the Central Excise Act, 1944, any Central Excise Officer not below the rank of Superintendent of Central Excise shall have power to summon any person whose attendance he considers necessary for gathering relevant evidence and documents. All persons so summoned shall be bound to attend, either in person or by an authorized agent. Every such inquiry as aforesaid shall be deemed to be a 'Judicial Proceeding' within the meaning of Section 193 and Section 228 of the Indian Penal Code, 1860.

Section 18 of the Central Excise Act, 1944 all arrests shall be carried out in accordance with the provisions of the Code of Criminal Procedure relating to arrest.

Note: provisions of arrest are not applicable to service tax matters.

vi. **Power to summon persons to give evidence and produce documents in inquiries under this Act:** As per Section 14 of the Central Excise Act, 1944,

(1) Any Central Excise Officer duly empowered by the Central Government in this behalf, shall have power to summon any person whose attendance he considers necessary either to give evidence or to produce a document or any other thing in any inquiry which such officer is making for any of the purposes of this Act. A summons to produce documents or other things may be for the production of certain specified documents or things or for the production of all documents or things of a certain description in the possession or under the control of the person summoned.

(2) All persons so summoned shall be bound to attend, either in person or by an authorised agent, as such officer may direct; and all persons so summoned shall be bound to state the truth upon any subject respecting which they are examined or make statements and to produce such documents and other things as may be required:

Provided that the exemptions under Sections 132 and 133 of the Code of Civil Procedure, 1908 (5 of 1908) shall be applicable to requisitions for attendance under this section.

(3) Every such inquiry as aforesaid shall be deemed to be a "judicial proceeding" within the meaning of Section 193 and Section 228 of the Indian Penal Code, 1860.

7.3.2 Show-Cause Notice Can be Issued by the Following Authority Under Section 11A

Authority	Demand of Duty/Cenvat Credit (applicable for Central Excise and Service Tax matters)
Superintendents	Upto ₹ 1,00,000 (Excluding cases involving determination of rate of duty or valuation and cases involving extended period of limitation). *[C.B.E. & C. Circular No. 922/12/2010-CX., dated 18.5.2010]*
Assistant/Deputy Comm. of C. Ex	₹ 5,00,000 (Except the cases where Superintendents are empowered to adjudicate). *[C.B.E. & C. Circular No. 922/12/2010-CX., dated 18.5.2010]*
Joint Comm. of C. Ex.	₹ 5,00,000 to ₹ 50,00,000
Additional Comm. of C. Ex.	₹ 5,00,000 to ₹ 50,00,000 (Circular No. 957/18/2011-CX-3 25th October, 2011)
Commissioner of Central Excise	Without any limit.

It means to say that the Superintendent of Central Excise now can issue the show cause notice.

Now, Superintendents are eligible to issue Show Cause Notices (SCN) involving duty and or CENVAT credit upto ₹ 1,00,000. It means to say that Superintendents are competent to issue SCN were cases involving wrong availment of CENVAT credit upto a monetary limit of ₹ 1,00,000 or duty calculated wrongly. They also eligible to decide Show Cause Notice proposing only imposition of penalty.

However, they would not be eligible to decide (i.e. settle) cases which involve excisability of a product, classification, eligibility of exemption, valuation and cases involving suppression of facts, frauds etc. [C.B.E. & C. Circular No. 922/12/2010-CX, dated 18.5.2010]

A show cause notice issued before the finalization of provisional assessment is not valid in law. In the case of *CCE & C* v *I.T.C. Ltd.* (2006) the Supreme Court of India observed that the power to issue a show cause notice under section 11A of the Central Excise Act, 1944 can be invoked only when duty is not levied or not paid or short-levied or short-paid. Such a proceeding can be initiated within one year from the relevant date. As per section 11A(3)(ii)(b), in case of provisional assessment the relevant date is the date of adjustment of duty after final assessment.

7.3.3 Joint Commissioner or Additional Commissioner of Central Excise is Empowered to Issue Show Cause Notices Without Upper Monetary Limit in Cases Relating to

(i) export under bond or

(ii) export under rebate or

(iii) loss of goods during transit to warehouse

7.3.4 Records Should be Returned Within 30 Days from the Date of Issue of Show Cause Notice (Rule 24A of Central Excise Rules, 2002)

A new rule has been inserted in the Central Excise Rules 2002 to provide that records seized by the department during an investigation but not relied upon in the Show Cause Notice should be returned to the party within 30 days of the issue of show cause notice or the completion of the period for issue of the show cause notice [Notification No. 17/2009-CE(NT), dated 7.7.2009].

7.3.5 Interest on Delayed Payment of Duty (Section 11AA of C.Ex. Act W.E.F. 1-4-2011 Similar Provision Under the Section 28AA(1) of the Customs Act.)

Interest on delay payment should not be less than 10% and nor more than 36%. The interest is payable from the next date after the due date in case of delay in payment. The interest rate is 18%p.a. w.e.f. 1-4-2011. (Prior to 1-4-2011 it was @13% p.a.).

No interest is shall be payable where, the duty payable arises subsequent to the issue of an order, instruction or direction by the Board under section 37B and such amount of duty is voluntarily paid in full, within 45 days from the date of issue of such order, instruction or direction, without reserving any right to appeal against the said payment at any subsequent stage of such payment.

Recovery of duty from successor: if the assessee transfers his business or trade to third party, any duty is due from predecessor (namely assessee) can be recovered from successor in trade or business. It is clear that only goods, plant etc transferred by predecessor can be attached and not goods or machinery acquired by the successor.

In case of liquidation of the company, the assets are transferred or disposed of by Court order and hence, recovery of duty from successor does not arise.

If non-payment or short payment of duty is due to oversight or by mistake but not intentional as per section 11A(2B), in such case it provides that the assessee in default may, before the notice issued under section 11A(1) is served on such assessee, make payment of the unpaid duty and inform to the Central Excise Officer in writing about the payment of differential amount. Hence, the person who has paid the duty under Section 11A(2B) shall, in addition to the duty be liable to pay the interest under section 11AA. However, no penalty is payable. [CCE v SKF India Ltd. 2009 (239) ELT 385 (SC)]

Example 2: Mr. X, paid the duty for the month of June 2015 on 15th July 2015. Hence, the interest @18% p.a. is calculated on the amount of duty for 10 days of delay (i.e. due date is 5th July 2015).

Example 3: Mr. Y, paid the duty for the month of June 2015 on 5th July for ₹ 10,300. It was found by the department officer, the actual amount of duty is ₹ 15,450 for the June 2015. Hence, the interest @18% p.a. is calculated on the amount of duty which is short paid from the 1st day of the month following the month in which the duty ought to have been paid, till the date of payment. It means delay number of days count start from 6th July 2015 upto the date of actual payment.

Interest @18% p.a. is payable from 6th July 2015 upto the date of payment.

7.4 PENALTIES IN INDIRECT TAX LAWS

7.4.1 Penalty [Section 11AC of Central Excise Act, 1944/Section 114A of Customs Act, 1962/Section 78 of Finance Act, 1994]

Penalty attracted if any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded by reasons of fraud, collusion or any willful miss-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made there under with intent to evade payment of duty.

7.4.2 Penalty Provisions W.E.F. 8-4-2011

Section 11AC(1)(a)

Where any duty of excise has not been levied or paid or short levied or short paid or erroneously refunded, by any reason other than the reason of fraud or collusion or any willful miss-statement or suppression of facts or contravention of any of the provisions of this Act or of the rules made there under with intent to evade payment of duty, the person who is liable to pay duty as determined under section 11A(10) shall also be liable to pay a penalty not exceeding 10% of the duty so determined or ₹5,000 whichevr is higher. Provisions are same even in the case of Customs Act, 1962 under section 114A.

Section 11AC (1)(b)

Where any duty as determined under sub-section (10) of section 11A and the interest payable thereon under section 11AA in respect of transactions referred to in clause (a) is paid within thirty days of the date of communication of the order of the Central Excise Officer who has determined such duty, the amount of penalty liable to be paid by such person shall be twenty-five per cent, of the penalty imposed, subject to the condition that such reduced penalty is also paid within the period so specified.

Section 11AC(1)(c)

Where any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, by reason of fraud or collusion or any willful mis-statement or suppression of facts, or contravention of any of the provisions of this Act or of the rules made thereunder with intent to evade payment of duty, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay a penalty equal to the duty so determined.

Section 11AC(1)(d)

Where any duty demanded in a show cause notice and the interest payable thereon under section 11AA, issued in respect of transactions referred to in clause (c), is paid within thirty days of the communication of show cause notice, the amount of penalty liable to be paid by such person shall be fifteen per cent, of the duty demanded, subject to the condition that such reduced penalty is also paid within the period so specified and all proceedings in respect of the said duty, interest and penalty shall be deemed to be concluded.

Section 11AC(2)

Where the appellate authority or tribunal or court modifies the amount of duty of excise determined by the Central Excise Officer under sub-section (10) of section 11 A, then, the amount of penalty payable under clause (c) of sub-section (1) and the interest payable under section 11AA shall stand modified accordingly and after taking into account the amount of duty of excise so modified, the person who is liable to pay duty as determined under sub-section (10) of section 11A shall also be liable to pay such amount of penalty and interest so modified.

7.4.3 'Unjust Enrichment'

It means the assessee gaining double benefits under the law out of one transaction.

Example 4: X Ltd. manufactured and sold goods to its buyer by collecting excise duty. Subsequently X Ltd. claimed refund of excise duty for the same transaction. Hence, such refund of duty to the manufacturer will amount to excess and un-deserved profit. This is called as 'Unjust Enrichment'

Example 5: Y Ltd. collected the excise duty and not remitted to the department of Excise. This is known as 'Unjust Enrichment'

Example 6: Z Ltd. claimed the Cenvat credit of excise duty and duty drawback. This is called as 'Unjust Enrichment'.

Where refund is due (i.e. Unjust Enrichment) it should be transferred to a Consumer Welfare Fund instead of paying it to the assessee. Thereby, provisions in respect of 'Unjust Enrichment' were incorporated under Central Excise Act, 1944 which will be applicable even for Service Tax and Customs duty.

Refund of Duty and interest (Section 11B of Central Excise Act, 1944)

a. The assessee can claim the refund of duty if due to him along with interest (w.e.f. 10.05.2008).

b. The refund should be filed in form 'R' in duplicate in the office of Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise.

c. Application for refund should be made within ONE year from the relevant date. Time limit not applicable in the following cases:—

   (i) duty paid by the assessee under protest

   (ii) in case of appeal, order is decided in favour of assessee then the time limit of one year not applicable.

d. The relevant date of one year count starts from the date of order.

Example 7: The assessee had paid excess amount of interest under section 11AA of Central Excise Act, 1944. Consequently, a refund claim for the said interest was filed by the assessee under section 11B. The Department objected to the refund claim on the ground that section 11B merely provides for refund of duty paid erroneously and not interest.

Answer:

As per the decision of the High Court, the payment of interest is automatic with payment of duty in case of delayed payment of duty and in case of delayed payment of refund of duty. Therefore payment of interest cannot be excluded from provisions of section 11B merely because it uses the expression of 'refund of duty' [*CCEx.* v *Northern Minerals Ltd*. 2007 (216) ELT 198 (P&H)]

Example 8: The assessee had never applied for revision of classification and once the classification is finalized and duty is paid accordingly, unless and until such classification is challenged and/or disturbed, it is not possible for the assessee to make refund claim based on some order passed by the Appellate authority in other case. Such order cannot universally be applied without going into facts of the case. Therefore, in the given case refund of duty is not allowed to the assessee- Wood Polymer Limited 2010 (H.C.).

7.4.4 Refund Under Section 11B of Central Excise Act, 1944/Section 27 of Customs Act, 1962/Section 83 of Finance Act, 1944 is applicable in the following Cases

(a) rebate of duty of excise on excisable goods exported out of India or on excisable materials used in the manufacture of goods which are exported out of India;

(b) unspent advance deposits lying in balance in the applicant's current account maintained with the Commissioner of Central Excise

(c) refund of credit of duty paid on excisable goods used as inputs in accordance with the rules made, or any notification issued, under this Act;

(d) the duty of excise paid by the manufacturer, if he had not passed on the incidence of such duty to any other person;

(e) the duty of excise borne by the buyer, if he had not passed on the incidence of such duty to any other person;

(f) the duty of excise borne by any other such class of applicants as the Central Government may, by notification in the Official Gazette, specify:

Example 9: Greenview Technologies Ltd. has paid excess amount of interest under section 11AA of Central Excise Act, 1944. Consequently, a refund claim for the said interest was filed by Greenview Technologies Ltd. under section 11B. The Department raised the objection to the refund claim on the ground that section 11B merely provides for refund of duty paid erroneously and not the interest. Do you think that the objection raised by the Department is valid in law?

Answer:

The provision applicable for refund of duty extended to refund of interest with effect from 10th May 2008. Hence, application for refund of duty has to be made by the assessee within one year from the relevant date to the Assistant or Deputy Commissioner of Central Excise.

Therefore Greenview Technologies Ltd is eligible to claim refund of interest along with duty. Department view is not valid.

7.4.5 Documents Required for Filing the Refund Applications

(i) Application form 'R'

(ii) ARE-1 (original copy)

(iii) Bill of lading or airway bill (duly attested)

(iv) Shipping bill copy duly attested

(v) Copy of invoice which shows clearly the value of goods and duty thereon.

7.4.6 Interest on Delayed Refunds (Section 11BB of Central Excise Act, 1944 Section 27A of Customs Act, 1962/Section 83 of Finance Act, 1994)

If the refund of duty along with interest has been granted to the assessee the same has to be paid within 3 months from the date of application made by him. If the amount is not paid within the time period of 3 months then interest @ 6% p.a. interest has to be paid.

While working out the time limit prescribed under section 11BB interest on delayed refunds, the period commencing from the date of application to the Settlement Commission under section 32E, to the date of receipt of the order under section 32L by the adjudicating authority, shall be excluded. Section 32L deals with sending back a case to proper officer if applicant has not co-operated with the Settlement Commission

7.4.7 Deposit of Duty Collected from the Buyer in Excess of Duty or Service Tax Assessed, into the Credit of Central Government. (Section 11D Of C. Ex Act, 1944 / Section 28B of Customs Act, 1962/Section 73A of Finance Act, 1994)

Interest on the amounts Collected in Excess of the Duty (Section 11DD of C. Ex. Act, 1944 / Section 73B of Finance Act, 1994)

Assessee is liable to make payment of interest on excess duty collected from any person or where a person has collected any amount as representing duty of excise on any excisable goods which are wholly exempt or are chargeable to nil rate of duty. Therefore, interest is payable @15% p.a. from the first day of the month succeeding the month in which the amount ought to have been paid till the date of payment of such amount Section 11DD of C.Ex. Act, 1944).

7.4.8 Provisional Attachment of Property (Section 11DDA of C.Ex. Act, 1944 Section 28BA of Customs Act, 1962 / Section 73C of Finance Act, 1994)

(1) Where during the pendency of any proceedings under section 11A or section 11D, the Central Excise Officer is of the opinion that for the purpose of protecting the interest of revenue, it is necessary so to do, he may, with the previous approval of the Principal Commissioner of Central Excise or Commissioner of Central Excise, by order in writing, attach provisionally any property belonging to the person on whom notice is served under section 11A or sub-section (2) of section 11D, as the case may be, in accordance with the rules made in this behalf under section 142 of the Customs Act.

(2) Every such provisional attachment shall cease to have effect after the expiry of a period of six months from the date of the order made under sub-section (1).

7.4.9 Liability Under Act to be First Charge

w.e.f. 8-4-2011, the Finance Act, 2011 has inserted a new section 11E of the Central Excise Act, 1944 so as to create first charge on the property of the defaulter for recovery of excise duty dues from such defaulter subject to provisions of section 326 of the Companies Act, 2013 and the Recovery of Debts Due to Bank and the Financial Institutions Act, 1993 and the Securitization and Reconstruction of Financial Assets and the Enforcement of Security Interest Act, 2002. Similar provisions in Customs Act, 1962 under section 131BA.

Deposit of duty demanded or penalty levied (Section 35F of C.Ex. Act, 1944 / Section 129E of Customs Act, 1962/Section 83 of Finance Act, 1994)

The person aggrieved with the decision of the adjudicating authority wants to go for appeal against the order shall, pending the appeal, deposit the duty demanded or penalty levied. Sometimes, the appellate authority in its discretion dispense with such deposit (i.e. no deposit of duty is required in such case). Such waiver of deposit is with the interest of revenue. These provisions are same in case of Section 129E of the Customs Act, 1962.

Interest on delayed refund of amount deposited (Section 35FF of C.Ex. Act, 1944 / Section 129EE of Customs Act, 1962/Section 83 of Finance Act, 1994)

If the appeal is decided in the favour of assessee, the pre-deposit is refundable within three months from the date of communication of the order to adjudicating authority. Delay in refund will attract interest @ 6% as per section 11BB of C.Ex. Act, 1944.

Publishing the name of any person and particulars of any proceedings (Section 37E)

Section 37E introduced by the Taxation Laws (Amendment) Act, 2006 provides for publishing the name of any person and particulars of any proceedings in relation to such person, in public interest. The provisions are as follows:

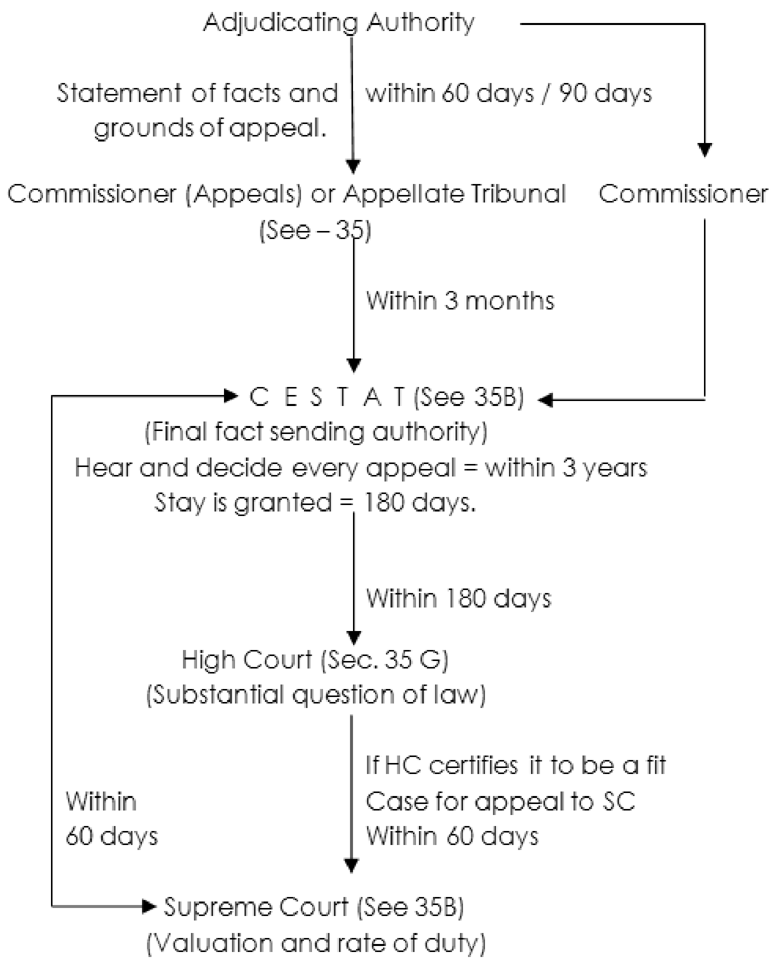
(i) The Central Government may publish name of any person and any other particulars relating to any proceedings or prosecutions in respect of such person if it is of the opinion that it is necessary or expedient in the public interest to do so. The Government can do the publication in such manner as it thinks fit.

(ii) The publication shall be made in relation to any penalty only after the time for presenting an appeal to the Commissioner (Appeals) or the Appellate Tribunal expires without an appeal being presented or the appeal, if presented, gets disposed off.

(iii) In the case of a firm, company or other association of persons, the names of the partners of the firm, directors, managing agents, secretaries and treasurers or managers of the company, or the members of the association, as the case may be, may also be published if, in the opinion of the Central Government, circumstances of the case justify it.

7.5 APPEAL PROVISIONS UNDER CENTRAL EXCISE, SERVICE TAX AND CUSTOMS

Assessment Procedure



7.5.1 Section 35: Appeals to Commissioner (Appeals) —

(1) Any person aggrieved by any decision or order passed under this Act by a Central Excise Officer, lower in rank than a Principal Commissioner of Central Excise or Commissioner of Central Excise, may appeal to the Commissioner of Central Excise (Appeals) hereafter in this Chapter referred to as the Commissioner (Appeals) within sixty days from the date of the communication to him of such decision or order:

Provided that the Commissioner (Appeals) may, if he is satisfied that the appellant was prevented by sufficient cause from presenting the appeal within the aforesaid period of sixty days, allow it to be presented within a further period of thirty days.

(1A) The Commissioner (Appeals) may, if sufficient cause is shown at any stage of hearing of an appeal, grant time, from time to time, to the parries or any of them and adjourn the hearing of the appeal for reasons to be recorded in writing:

Provided that no such adjournment shall be granted more than three times to a party during hearing of the appeal.

(2) Every appeal under this section shall be in the prescribed form and shall be verified in the prescribed manner.

SECTION 35A: Procedure in appeal -

(1) The Commissioner (Appeals) shall give an opportunity to the appellant to be heard, if he so desires.

(2) The Commissioner (Appeals) may, at the hearing of an appeal, allow an appellant to go into any ground of appeal not specified in the grounds of appeal, if the Commissioner (Appeals) is satisfied that the omission of that ground from the grounds of appeal was not wilful or unreasonable.

(3) The Commissioner (Appeals) shall, after making such further inquiry as may be necessary, pass such order, as he thinks just and proper, confirming, modifying or annulling the decision or order appealed against

Provided that an order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value or reducing the amount of refund shall not be passed unless the appellant has been given a reasonable opportunity of showing cause against the proposed order:

Provided further that where the Commissioner (Appeals) is of opinion that any duty of excise has not been levied or paid or has been short-levied or short-paid or erroneously refunded, no order requiring the appellant to pay any duty not levied or paid, short-levied or short-paid or erroneously refunded shall be passed unless' the appellant is given notice within the time-limit specified in section 11A to show cause against the proposed order.

(4) The order of the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reasons for the decision.

(4A) The Commissioner (Appeals) shall, where it is possible to do so, hear and decide every appeal within a period of six months from the date on which it is filed.

(5) On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the appellant, the adjudicating authority, the Principal Chief Commissioner of Central Excise or Chief Commissioner of Central Excise and Principal Commissioner or the Commissioner of Central Excise.

SECTION 35B: Appeals to the Appellate Tribunal -

(1) Any person aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order —

(a) a decision or order passed by the Principal Commissioner of Central Excise or the Commissioner of Central Excise as an adjudicating authority;

(b) an order passed by the Commissioner (Appeals) under section 35A;

(c) an order passed by the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 (hereafter in this Chapter referred to as the Board) or the Appellate Principal Commissioner of Central Excise or Commissioner of Central Excise under section 35, as it stood immediately before the appointed day;

(d) an order passed by the Board or Principal Commissioner of Central Excise or the Commissioner of Central Excise, either before or after the appointed day, under section 35A, as it stood immediately before that day:

Provided that no appeal shall lie to the Appellate Tribunal and the Appellate Tribunal shall not have jurisdiction to decide any appeal in respect of any order referred to in clause (b) if such order relates to, —

(a) a case of loss of goods, where the loss occurs in transit from a factory to a warehouse, or to another factory, or from one warehouse to another, or during the course of processing of the goods in a warehouse or in storage, whether in a factory or in a warehouse;

(b) a rebate of duty of excise on goods exported to any country or territory outside India or on excisable materials used in the manufacture of goods which are exported to any country or territory outside India;

(c) goods exported outside India (except to Nepal or Bhutan) without payment of duty;

(d) credit of any duty allowed to be utilised towards payment of excise duty on final products under the provisions of this Act or the rules made thereunder and such order is passed by the Commissioner (Appeals) on or after the date appointed under section 109 of the Finance (No. 2) Act, 1998;

Provided further that the Appellate Tribunal may, in its discretion, refuse to admit an appeal in respect of an order referred to in clause (b) or clause (c) or clause (d) where—

(i) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or

(ii) the amount of fine or penalty determined by such order,

does not exceed two lakh rupees.

(1A) Every appeal against any order of the nature referred to in the first proviso to sub-section (1), which is pending immediately before the commencement of section 47 of the Finance Act, 1984, before the Appellate Tribunal and any matter arising out of, or connected with, such appeal and which is so pending shall stand transferred on such commencement to the Central Government, and the Central Government shall deal with such appeal or matter under section 35EE as if such appeal or matter were an application or a matter arising out of an app" made to it under that section.

(IB) (i) The Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 may, by order, constitute such Committee as may be necessary for the purposes of this Act.

(ii)Every Committee constituted under clause (i) shall consist of two Chief Commissioners of Central Excise or two Commissioners Central Excise, as the case may be.

(2) The Committee of Commissioners of Central Excise may, if it is of opinion that an order passed by the Appellate Commissioner Excise under section 35, as it stood immediately before the appointed day, or the Commissioner (Appeals) under section 35A, is not proper, direct any Central Excise Officer authorised by him in this behalf to appeal on its behalf to the Appellate Tribunal against such order.

Provided that where the Committee of Commissioners of Central Excise differs in its opinion regarding the appeal against the order Commissioner (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Principal Chief Commissioner of Central Excise or Chief Commissioner of Central Excise who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner (Appeals) is not legal or proper, direct any Central Excise Officer to appeal to the Appellate Tribunal against such order.

Explanation — For the purposes of this sub-section, "jurisdictional Chief Commissioner;" means the Principal Chief Commissioner of Central Excise or the Chief Commissioner of Central Excise having jurisdiction over the adjudicating authority in the matter.

(3) Every appeal under this section shall be filed within three months from the date on which the order sought to be appealed against is communicated to the Principal Commissioner of Central Excise or the Commissioner of Central Excise, or, as the case may be, the other party preferring the appeal.

(4) On receipt of notice that an appeal has been preferred under this section, the party against whom the appeal has been preferred may, notwithstanding that he may not have appealed against such order or any part thereof, file, within forty-five days of the receipt of the notice, a memorandum of cross-objections verified in the prescribed manner against any part of the order appealed against and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in sub-section (3).

(5) The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period referred to in sub-section (3) or sub-section (4), if it is satisfied that there was sufficient cause for not presenting it within that period.

(6) An appeal to the Appellate Tribunal shall be in the prescribed form and shall be verified in the prescribed manner and shall, irrespective of the date of demand of duty and interest or of levy of penalty in relation to which the appeal is made, be accompanied by a fee of, —

(a) where the amount of duty and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is five lakh rupees or less, one thousand rupees;

(b) where the amount of duty and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is more than five lakh rupees but not exceeding fifty lakh rupees, five thousand rupees;

(c) where the amount of duty and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is more than fifty lakh rupees, ten thousand rupees:

Provided that no fee shall be payable in the case of an appeal referred to in sub-section (2) or a memorandum of cross-objections referred to sub-section (4).

(7) Every application made before the Appellate Tribunal, —

(a) in an appeal for rectification of mistake or for any other purpose; or

(b) for restoration of an appeal or an application,

shall be accompanied by a fee of five hundred rupees :

Provided that no such fee shall be payable in the case of an application filed by or on behalf of Principal Commissioner of Central Excise or the Commissioner of Central Excise under this sub-section.

7.5.2 Departmental Appeals not Allowed (W.E.F. 17-12-2015)

The Central Board of Excise and Customs (CBE&C) has issued instructions (vide F.No. 390/ Misc./ 163/2010- JC dated 17-8-2011) by fixing the following different minimum monetary limits for filing appeals to the Customs, Excise and Service Tax Appellate Tribunal (CESTAT) and High Court:

(i) Departmental appeals in the Tribunal (CESTAT) shall not be filed in cases where the duty involved is below ₹10,00,000.

(ii) Departmental appeals in the High Court should not be filed in cases where the duty involved is below ₹15,00,000.

(iii) Departmental appeals in the Supreme Court should not be filed in cases where the duty involved is below ₹25,00,000.

However, Departmental appeals in case of adverse judgments relating to the following disputes shall be allowed irrespective of the amount involved.

(a) Where the constitutional validity of the provisions of an Act or Rule is under challenge.

(b) Where notification/instruction/order or Circular has been held illegal or ultra virus.

Example 10: X Ltd. received a protective demand notice from the department on 18.12.2015 under Section 11A of the Central Excise Act, 1944 where the duty demanded is ₹ 5,00,000, in addition to interest of ₹ 10,000 and Penalty of ₹ 1,00,000. The assessee went for appeal and filed the case in the Commissioner (Appeals) on 18.01.2016. Subsequently on 30.03.2016, the Commissioner (Appeals) decided the case in favour of the assessee. The Committee of Commissioners can delegate the authority to the department officers to go for further appeal on its behalf to the Appellate Tribunal (CESTAT) against such order.

Answer:

As per the Central Board of Excise and Customs (CBE&C) instructions (vide F.No. 390/Misc./163/ 2010-JC dated 17-8-2011), in a case involving duty below ₹10,00,000, no appeal shall henceforth (i.e. w.e.f. 17-12-2015) be filed in the Tribunal (CESTAT).

Hence, in the given case, no appeal shall henceforth be filed in the Tribunal as the duty involved is below the monetary limit of ₹10,00,000.

SECTION 35C: Orders of Appellate Tribunal -

(1) The Appellate Tribunal may, after giving the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit, confirming, modifying or annulling the decision or order appealed against or may refer the case back to the authority which passed such decision or order with such directions as the Appellate Tribunal may think fit, for a fresh adjudication or decision, as the case may be, after taking additional evidence, if necessary.

(1A) The Appellate Tribunal may, if sufficient cause is shown, at any stage of hearing of an appeal, grant time, from time to time, to the parties or any of them and adjourn the hearing of the appeal for reasons to be recorded in writing:

Provided that no such adjournment shall be granted more than three times to a party during hearing of the appeal.

(2) The Appellate Tribunal may, at any time within six months from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it under sub-section (1) and shall make such amendments if the mistake is brought to its notice by the Principal Commissioner of Central Excise or the Commissioner of Central Excise or the other party to the appeal:

Provided that an amendment which has the effect of enhancing an assessment or reducing & refund or otherwise increasing the liability of the other party, shall not be made under this sub-section, unless the Appellate Tribunal has given notice to him of its intention to do so and has allowed him a reasonable opportunity of being heard.

(2A) The Appellate Tribunal shall, where it is possible to do so, hear and decide every appeal within a period of three year from the date on which such appeal is filed:

(3) The Appellate Tribunal shall send a copy of every order passed under this section to the Principal Commissioner of Central Excise or Commissioner of Central Excise and the other party to the appeal.

(4) Save as provided in Section 35G or 35L orders passed by the Appellate Tribunal on appeal shall be final.

Example 11: The CESTAT passed its order on 01.01.2015. The assessee filed the application for rectification of a mistake apparent from the record in the said order on 23.05.2015. However, the Tribunal could not dispose of the application till 30.06.2015. Thereafter, the Tribunal rejected the application on the ground that the six months period had lapsed. Do you think that the stand taken by the Tribunal is valid in law?

Answer:

The assessee has filed the application for rectification of mistake apparent from the record within six month from the date of passing the original order. Hence, it is apparent that Tribunal is not justified in rejecting the application on the ground that the six months period has lapsed as the application had been filed before the expiry of SIX months. *Sree Ayyangar Spg & Wvg Mills Ltd.* v *CIT* 2008 (229) ELT 164 (SC).

Example 12: The High Court held that in a case of confiscation of goods because of their under valuation, Tribunal could not cancel the confiscation order for want of evidence from the foreign supplier. *CCus.* v *Jaya Singh Vijaya Jhaveri* 2010 (251) ELT 38 (Ker).

An order passed by CESTAT based on consent and the matter was remanded at the instance of Revenue, then Revenue could not pursue an appeal against such order in a higher forum.

Example 13: The Tribunal had remanded the matter in order to re-compute the duty payable by the assessee on the basis of representation of Revenue. Thereafter, the Revenue filed an appeal against the said order. The assessee contended that the appeal filed by the Revenue was not maintainable since the order had been passed by the Tribunal on the submission of the representative of the Revenue. Further, since it is a consent order, no appeal would lie. Hence, the High Court held that an appeal against the consent order cannot be filed by the Revenue (*CCus* v *Trilux Electronics* 2010 (253) ELT 367 (Kar).

SECTION 35D: Procedure of Appellate Tribunal -

(1) The provisions of subsections (1), (2), (5) and (6) of section 129C of the Customs Act, 1962(52 of 1962), shall apply to the Appellate Tribunal in the discharge of its functions under this Act as they apply to it in the discharge of its functions under the Customs Act, 1962.

(2) Omitted

(3) The President or any other member of the Appellate Tribunal authorised in this behalf by the President may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member where—

(a) in any disputed case, other than a case where the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment is in issue or is one of the points in issue, the difference in duty involved or the duty involved; or

(b) the amount of fine or penalty involved,

does not exceed fifty lakh rupees.

SECTION 35E: Powers of Board or Commissioner of Central Excise to pass certain orders —

(1) The Committee of Chief Commissioners of Central Excise may, of its own motion, call for and examine the record of any proceeding in which Principal Commissioner of Central Excise or a Commissioner of Central Excise as an adjudicating authority has passed any decision or order under this Act for the purpose of satisfying itself as to the legality or propriety of any such decision or order and may, by order, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order as may be specified by the Committee of Chief Commissioners of Central Excise in its order.

Provided that where the Committee of Chief Commissioners of Central Excise differs in its opinion as to the legality or propriety of the decision or order of the Commissioner of Central Excise, it shall state the point or points on which it differs and make a reference to the Board which, after considering the facts of the decision or order, if is of the opinion that the decision or order passed by the Principal Commissioner of Central Excise or the Commissioner of Central Excise is not legal or proper, may, by order, direct such Commissioner or any other Commissioner to apply to the Appellate Tribunal for the determination of such points arising out of the decision or order, as may be specified in its order.

(2) The Principal Commissioner of Central Excise or Commissioner of Central Excise may, of his own motion, call for and examine the record of any proceeding in which an adjudicating authority subordinate to him has passed any decision or order under this Act for the purpose of satisfying himself as to the legality or propriety of any such decision or order and may, by order, direct such authority or any Central Excise Officer subordinate to him to apply to the Commissioner (Appeals) for the determination of such points arising out of the decision or order as may be specified by the Principal Commissioner of Central Excise or Commissioner of Central Excise in his order.

(3) Every order under sub-section (1) or sub-section (2), as the case may be, shall be made within a period of three months from the date of communication of the decision or order of the adjudicating authority.

Provided that the Board may, on sufficient cause being shown, extend the said period by another thirty days.

(4) Where in pursuance of an order under sub-section (1) or sub-section (2), the adjudicating authority or the authorised officer makes an application to the Appellate Tribunal or the Commissioner (Appeals) within a period of one month from the date of communication of the order under sub-section (1) or sub-section (2) to the adjudicating authority, such application shall be heard by the Appellate Tribunal or the Commissioner (Appeals), as the case may be, as if such application were an appeal made against the decision or order of the adjudicating authority and the provisions of this Act regarding appeals, including the provisions of sub-section (4) of section 35B shall, so far as may be, apply to such application.

SECTION 35EE: Revision by Central Government—

(1) The Central Government may, on the application of any person aggrieved by any order passed under section 35A, where the order is of the nature referred to in the first proviso to sub-section (1) of section 35B, annul or modify such order.

Provided that the Central Government may in its discretion, refuse to admit an application in respect of an order where the amount of duty or fine or penalty, determined by such order does not exceed five thousand rupees.

Explanation.— For the purposes of this sub-section, "order passed under section 35A" includes an order passed under that section before the commencement of section 47 of the Finance Act, 1984 against which an appeal has not been preferred before such commencement and could have been, if the said section had not come into force, preferred after such commencement, to the Appellate Tribunal.

(1A) The Principal Commissioner of Central Excise or Commissioner of Central Excise may, if he is of the opinion that an order passed by the Commissioner (Appeals) under section 35A is not legal or proper, direct the proper officer to make an application on his behalf to the Central Government for revision of such order.

(2) An application under sub-section (1) shall be made within three months from the date of the communication to the applicant of the order against which the application is being made:

Provided that the Central Government may, if it is satisfied that the applicant was prevented by sufficient cause from presenting the application within the aforesaid period of three months, allow it to be presented within a further period of three months.

(3) An application under sub-section (1) shall be in such form and shall be verified in such manner as may be specified by rules made in this behalf and shall be accompanied by a fee of,—

- **(a)** two hundred rupees, where the amount of duty and interest demanded, fine or penalty levied by any Central Excise Officer in the case to which the application relates is one lakh rupees or less;
- **(b)** one thousand rupees, where the amount of duty and interest demanded, fine or penalty levied by any Central Excise Officer in the case to which the application relates is more than one lakh rupees:

Provided that no such fee shall be payable in the case of an application referred to in sub-section (IA).

(4) The Central Government may, of its own motion, annul or modify any order referred to in sub-section (1).

(5) No order enhancing any penalty or fine in lieu of confiscation or confiscating goods of greater value shall be passed under this section,—

(a) in any case in which an order passed under section 35A has enhanced any penalty or fine in lieu of confiscation or has confiscated goods of greater value; and

(b) in any other case, unless the person affected by the proposed order has been given notice to show cause against it within one year from the date of the order sought to be annulled or modified.

(6) Where the Central Government is of opinion that any duty of excise has not been levied or has been short-levied, no order levying or enhancing the duty shall be made under this section unless the person affected by the proposed order is given notice to show cause against it within the time limit specified in section 11A.

SECTION 35F: Deposit of certain percentage of duty demanded or penalty imposed before filling appeal

The Tribunal or the Commissioner (Appeals), as the case may be, shall not entertain any appeal,—

(i) under sub-section (1) of section 35, unless the appellant has deposited seven and a half per cent, of the duty demanded or penalty imposed or both, in pursuance of a decision or an order passed by an officer of Central Excise lower in rank than Principal Commissioner of Central Excise or the Commissioner of Central Excise;

(ii) against the decision or order referred to in clause (a) of sub-section (1) of section 35B, unless the appellant has deposited seven and a half per cent, of the duty demanded or penalty imposed or both, in pursuance of the decision or order appealed against;

(iii) against the decision or order referred to in clause (b) of sub-section (1) of section 35B, unless the appellant has deposited ten per cent, of the duty demanded or penalty imposed or both, in pursuance of the decision or order appealed against.

Provided that the amount required to be deposited under this section shall not exceed rupees ten crores.

Provided further that the provisions of this section shall not apply to the stay applications and appeals pending before any appellate authority prior to the commencement of the Finance (No.2) Act, 2014.

Explanation.— For the purposes of this section "duty demanded" shall include,—

(i) amount determined under section 11D;

(ii) amount of erroneous Cenvat credit taken;

(iii) amount payable under rule 6 of the Cenvat Credit Rules, 2001 or the Cenvat Credit Rules, 2002 or the Cenvat Credit Rules, 2004.

SECTION 35FF: Interest on delayed refund of amount deposited under section 35F. — Where an amount deposited by the appellant u/s 35F is required to be refunded consequent upon the order of the appellate authority, there shall be paid to the appellant interest at such rate, not below five percent and not exceeding thirty six percent per annum as is for the time being fixed by the Central Government, by notification in the official Gazette, on such amount from the date of payment of the amount till the date of refund of such amount.

Provided that the amount deposited u/s 35F, prior to the commencement of the Finance Act, 2014, shall continue to be governed by the provisions of section 35FF as it stood before the commencement of the said Act.

SECTION 35G: Appeal to High Court -

(1) An appeal shall lie to the High Court from every order passed in appeal by the Appellate Tribunal on or after the 1st day of July, 2003 (not being an order relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment), if the High Court is satisfied that the case involves a substantial question of law.

(2) The Principal Commissioner of Central Excise or the Commissioner of Central Excise or the other party aggrieved by any order passed by the Appellate Tribunal may file an appeal to the High Court and such appeal under this sub-section shall be

(a) filed within one hundred and eighty days from the date on which the order appealed against is received by the Commissioner of Central Excise or the other party;

(b) accompanied by a fee of two hundred rupees where such appeal is filed by the other party;

(c) in the form of a memorandum of appeal precisely stating therein the substantial question of law involved.

(2A) The High Court may admit an appeal after the expiry of the period of one hundred and eighty days referred to in clause (a) of sub-section (2), if it is satisfied that there was sufficient cause for not filing the same within that period.

(3) Where the High Court is satisfied that a substantial question of law is involved in any case, it shall formulate that question.

(4) The appeal shall be heard only on the question so formulated, and the respondents shall, at the hearing of the appeal, be allowed to argue that the case does not involve such question:

Provided that nothing in this sub-section shall be deemed to take away or abridge the power of the court to hear, for reasons to be recorded, the appeal on any other substantial question of law not formulated by it, if it is satisfied that the case involves such question.

(5) The High Court shall decide the question of law so formulated and deliver such judgment thereon containing the grounds on which such decision is founded and may award such cost as it deems fit.

(6) The High Court may determine any issue which-

(a) has not been determined by the Appellate Tribunal; or

(b) has been wrongly determined by the Appellate Tribunal, by reason of a decision on such question of law as is referred to in subsection (1).

(7) When an appeal has been filed before the High Court, it shall be heard by a bench of not less than two judges of the High Court, and shall be decided in accordance with the opinion of such judges or of the majority, if any, of such judges.

(8) Where there is no such majority, the judges shall state the point of law upon which they differ and the case shall, then, be heard upon that point only by one or more of the other judges of the High Court and such point shall be decided according to the opinion of the majority of the judges who have heard the case including those who have first heard it.

(9) Save as otherwise provided in this Act, the provisions of the Code of Civil Procedure, 1908, relating to appeals to the High Court shall, as far as may be, apply in the case of appeals under this section.

SECTION 35-I: Power of High Court or Supreme Court to require statement to be amended — If the High Court or the Supreme Court is not satisfied that the statements in a case referred to it are sufficient to enable it to determine the questions raised thereby, the Court may refer the case back to the Appellate Tribunal for the purpose of making such additions thereto or alterations therein as it may direct in that behalf.

SECTION 35J: Case before High Court to be heard by not less than two judges —

(1) When any case has been referred to the High Court under section 35G or section 35H, it shall be heard by a Bench of not less than two judges of the High Court and shall be decided in accordance with the opinion of such judges or of the majority, if any, of such judges.

(2) Where there is no such majority, the judges shall state the point of law upon which they differ and the case shall then be heard upon that point only by one or more of the other judges of the High Court, and such point shall be decided according to the opinion of majority of the judges who have heard the case including those who first heard it.

SECTION 35K: Decision of High Court or Supreme Court on the case stated —

(1) The High Court or the Supreme Court hearing any such case shall decide the question of law raised therein and shall deliver its judgment thereon containing the grounds on which such decision is founded and a copy of the judgment shall be sent under the seal of the Court and the signature of the Registrar to the Appellate Tribunal which shall pass such orders as are necessary to dispose of the case in conformity with such judgment.

(1A) Where the High Court delivers a judgment in an appeal filed before it under section 35G, effect shall be given to the order passed on the appeal by the concerned Central Excise Officer on the basis of a certified copy of the judgment;

(2) The costs of any reference to the High Court or an appeal to the High Court or the Supreme Court, as the case may be, which shall hot include the fee for making the reference, shall be in the discretion of the Court.

SECTION 35L: Appeal to the Supreme Court - (1) An appeal shall lie to the Supreme Court from—

(a) any judgment of the High Court delivered-

(i) in an appeal made under section 35G; or

(ii) on a reference made under section 35G by the Appellate Tribunal before the 1st day of July, 2003; or

(iii) on a reference made under section 35H,

in any case which, on its own motion or on an oral application made by or on behalf of the party aggrieved, immediately after passing of the judgment the High Court certifies to be a fit one for appeal to the Supreme Court.

(b) any order passed before the establishment of the National Tax Tribunal by the Appellate Tribunal relating, among other things, to the determination of any question having a relation to the rate of duty of excise or to the value of goods for purposes of assessment.

For the purpose of this chapter the determination of any question having a relation to the rate of duty shall include the determination of taxability or excisability of goods for the purpose of assessment.

SECTION 35M: Hearing before Supreme Court -

(1) The provisions of the Code of Civil Procedure, 1908, relating to appeals to the Supreme Court shall, so far as may be, apply in the case of appeals under section 35L as they apply in the case of appeals from decrees of a High Court:

Provided that nothing in this sub-section shall be deemed to affect the provisions of sub-section (1) of section 35K or section 35N.

(2) The costs of the appeal shall be in the discretion of the Supreme Court.

(3) Where the judgment of the High Court is varied or reversed in the appeal, effect shall be given to the order of the Supreme Court in the manner provided in section 35K in the case of a judgment of the High Court.

SECTION 35N: Sums due to be paid notwithstanding reference, etc — Notwithstanding that a reference had been made to the High Court or the Supreme Court or an appeal has been preferred to the Supreme Court, under this Act before the commencement of the National Tax tribunal Act, 2005, sums due to the Government as a result of an order passed under sub-section (1) of section 35C shall be payable in accordance with the order so passed.

SECTION 35-O: Exclusion of time taken for copy — In computing the period of limitation prescribed for an appeal or application under this Chapter, the day on which the order complained of was served, and if the party preferring the appeal or making the application was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order shall be excluded.

SECTION 35Q: Appearance by authorised representative —

(1) Any person who is entitled or required to appear before a Central Excise Officer or the Appellate Tribunal in connection with any proceedings under this Act, otherwise than when required under this Act to appear personally for examination on oath or affirmation, may, subject to the other provisions of this section, appear by an authorised representative.

(2) For the purposes of this section, "authorised representative" means a person authorised by the person referred to in sub-section (1) to appear on his behalf, being—

(a) his relative or regular employee; or

(b) any legal practitioner who is entitled to practice in any civil court in India; or

(c) any person who has acquired such qualifications as the Central Government may prescribe for this purpose.

(3) Notwithstanding anything contained in this section, no person who was a member of the Indian Customs and Central Excise Service -Group A and has retired or resigned from such Service after having served for not less than three years in any capacity in that Service, shall be entitled to appear as an authorised representative in any proceedings before a Central Excise Officer for a period of two years from the date of his retirement or resignation, as the case may be.

(4) No person,—

(c) who has been dismissed or removed from Government service; or

(d) who is convicted of an offence connected with any proceeding under this Act, the Customs Act, 1962 or the Gold (Control) Act, 1968; or

(e) who has become an insolvent, shall be qualified to represent any person under sub-section (1),

for all times in the case of a person referred to in clause (a), and for such time as the Commissioner of Central Excise or the competent authority under the Customs Act, 1962 or the Gold (Control) Act, 1968, as the case may be, may, by order, determine in the case of a person referred to in clause (b), and for the period during which the insolvency continues in the case of a person referred to in clause (c).

(5) If any person, —

(a) who is a legal practitioner, is found guilty of misconduct in his professional capacity by any authority entitled to institute proceedings against him, an order passed by that authority shall have effect in relation to his right to appear before a Central Excise Officer or the Appellate Tribunal as it has in relation to his right to practice as a legal practitioner;

(b) who is not a legal practitioner, is found guilty of misconduct in connection with any proceedings under this Act by the prescribed authority, the prescribed authority may direct that he shall thenceforth be disqualified to represent any person under sub-section (1).

(6) Any order or direction under clause (b) of sub-section (4) or clause (b) of sub-section (5) shall be subject to the following conditions, namely: —

(a) no such order or direction shall be made in respect of any person unless he has been given a reasonable opportunity of being heard;

(b) any person against whom any such order or direction is made may, within one month of the making of the order or direction, appeal to the Board to have the order or direction cancelled; and

(c) no such order or direction shall take effect until the expiration of one month from the making thereof, or, where an appeal has been preferred, until the disposal of the appeal.

SECTION 35R: Appeal not to be filed in certain cases —

(1) The Central Board of Excise and Customs may, from time to time, issue orders or instructions or directions fixing such monetary limits, as it may deem fit, for the purposes of regulating the filing of appeal, application, revision or reference by the Central Excise Officer under the provisions of this Chapter.

(2) Where, in pursuance of the orders or instructions or directions, issued under sub-section (1), the Central Excise Officer has not filed an appeal, application, revision or reference against any decision or order passed under the provisions of this Act, it shall not preclude such Central Excise Officer from filing appeal, application, revision or reference in any other case involving the same or similar issues or questions of law.

(3) Notwithstanding the fact that no appeal, application, revision or reference has been filed by the Central Excise Officer pursuant to the orders or instructions or directions issued under sub-section (1), no person, being a party in appeal, application, revision or reference shall contend that the Central Excise Officer has acquiesced in the decision on the disputed issue by not filing appeal, application, revision or reference.

(4) The Commissioner (Appeals) or Appellate Tribunal or Court hearing such appeal, application, revision or reference shall have regard to the circumstances under which appeal, application, revision or reference was not filed by the Central Excise Officer in pursuance of the orders or instructions or directions issued under sub-section (1).

(5) Every order or instruction or direction issued by the Central Board of Excise and Customs on or after the 20th day of October, 2010, but before the date on which the Finance Bill, 2011 receives the assent of the President, fixing monetary limits for filing of appeal, application, revision or reference shall be deemed to have been issued under sub-section (1) and the provisions of sub-sections (2), (3) and (4) shall apply accordingly.

SECTION 36: Definitions - In this Chapter - **(b)** "High Court" means, -

(i) In relation to any State, the High Court for that State;

(ii) In relation to a Union Territory to which the jurisdiction of the High Court of a State has been extended by law, that High Court;

(iii) In relation to the Union Territories of Dadra and Nagar Haven' and Daman and Diu the High Court at Bombay;

(iv) In relation to any other Union Territory, the highest court of civil appeal for that territory other than the Supreme Court of India.

(c) "President" means the President of the Appellate Tribunal.

SECTION 36A: Presumption as to documents in certain cases — Where any document is produced by any person or has been seized from the custody or control of any person, in either case, under this Act or under any other law and such document is tendered by the prosecution in evidence against him or against him and any other person who is tried jointly with him, the Court shall, —

(a) unless the contrary is proved by such person, presume —

  (i) the truth of the contents of such document;

  (ii) that the signature and every other part of such document which purports to be in the handwriting of any particular person or which the Court may reasonably assume to have been signed by, or to be in the handwriting of, any particular person, is in that person's handwriting, and in the case of a document executed or attested, that it was executed or attested by the person by whom it purports to have been so executed or attested;

(b) admit the document in evidence, notwithstanding that it is not duly stamped, if such document is otherwise admissible in evidence.

SECTION 37C: Service of decisions, orders, summons, etc. —

(1) Any decision or order passed or any summons or notices issued under this Act or the rules made thereunder, shall be served, —

  (a) by tendering the decision, order, summons or notice, or sending it by registered post with acknowledgement due, or by sped post with proof of delivery or by courier approved by the Central Board of Excise and Customs constituted under the Central Boards of Revenue Act, 1963 to the person for whom it is intended or his authorised agent, if any;

  (b) if the decision, order, summons or notice cannot be served in the manner provided in clause (a), by affixing a copy thereof to some conspicuous part of the factory or warehouse or other place of business or usual place of residence of the person for whom such decision, order, summons or notice, as the case may be, is intended;

  (c) if the decision, order, summons or notice cannot be served in the manner provided in clauses (a) and (b), by affixing a copy thereof on the notice board of the officer or authority who or which passed such decision or order or issued such summons or notice.

(2) Every decision or order passed or any summons or notice issued under this Act or the rules made thereunder, shall be deemed to have been served on the date on which the decision, order, summons or notice is tendered or delivered by post or a copy thereof is affixed in the manner provided in sub-section (1).

SECTION 38A: Effect of amendments, etc., of rules, notifications or orders — Where any rule, notification or order made or issued under this Act or any notification or order issued under such rule, is amended, repealed, superseded or rescinded, then, unless a different intention appears, such amendment, repeal, supersession or rescinding shall not -

(a) revive anything not in force or existing at the time at which the amendment, repeal, supersession or rescinding takes effect; or

(b) affect the previous operation of any rule, notification or order so amended, repealed, superseded or rescinded or anything duly done or suffered thereunder; or

(c) affect any right, privilege, obligation or liability acquired, accrued or incurred under any rule, notification or order so amended, repealed, superseded or rescinded; or

(d) affect any penalty, forfeiture or punishment incurred in respect of any offence committed under or in violation of any rule, notification or order so amended, repealed, superseded or rescinded; or

(e) affect any investigation, legal proceeding or remedy in respect of any such right, privilege, obligation, liability, penalty, forfeiture or punishment as aforesaid,

and any such investigation, legal proceeding or remedy may be instituted, continued or enforced and any such penalty, forfeiture or punishment may be imposed as if the rule, notification or order, as the case may be, had not been amended, repealed, superseded or rescinded.

SECTION 84 of Finance Act 1994: Appeals to Commissioner of Central Excise (Appeals) —

(1) The Principal Commissioner of Central Excise or the Commissioner of Central Excise may, of his own motion, call for and examine the record of any proceedings in which an adjudicating authority subordinate to him has passed any decision or order under this Chapter for the purpose of satisfying himself as to the legality or propriety of any such decision or order and may, by order, direct such authority or any Central Excise Officer subordinate to him to apply to the Commissioner of Central Excise (Appeals) for the determination of such points arising out of the decision or order as may be specified by the Principal Commissioner of Central Excise or the Commissioner of Central Excise in his order.

(2) Every order under sub-section (1) shall be made within a period of three months from the date of communication of the decision or order of the adjudicating authority.

(3) Where in pursuance of an order under sub-section (1), the adjudicating authority or any other officer authorised in this behalf makes an application to the Commissioner of Central Excise (Appeals) within a period of one month from the date of communication of the order under sub-section (1) to the adjudicating authority, such application shall be heard by the Commissioner of Central Excise (Appeals), as if such application were an appeal made against the decision or order of the adjudicating authority and the provisions of this Chapter regarding appeals shall apply to such application.

Explanation. — For the removal of doubts, it is hereby declared that any order passed by an adjudicating officer subordinate to the Principal Commissioner of Central Excise or the Commissioner of Central Excise immediately before the commencement of clause (C) of section 113 of the Finance (No. 2) Act, 2009, shall continue to be dealt with by the Commissioner of Central Excise as if this section had not been substituted.

SECTION 85: Appeals to the Commissioner of Central Excise (Appeals) —

(1) Any person aggrieved by any decision or order passed by an adjudicating authority subordinate to the Principal Commissioner of Central Excise or the Commissioner of Central Excise may appeal to the Commissioner of Central Excise (Appeals).

(2) Every appeal shall be in the prescribed form and shall be verified in the prescribed manner.

(3) An appeal shall be presented within three months from the date of receipt of the decision or order of such adjudicating authority, relating to service tax, interest or penalty under this Chapter made before the date on which the Finance Bill, 2012 receives the assent of the President:

(3A) An appeal shall be presented within two months from the date of receipt of the decision or order of such adjudicating authority, made on and after the Finance Bill, 2012 receives the assent of the President, relating to service tax, interest or penalty under this Chapter:

Provided that the Commissioner of Central Excise (Appeals) may, if he is satisfied that the appellant was prevented by sufficient cause from presenting the appeal within the aforesaid period of two months, allow it to be presented within a further period of one month.

(4) The Commissioner of Central Excise (Appeals) shall hear and determine the appeal and, subject to the provisions of this Chapter, pass such orders as he thinks fit and such orders may include an order enhancing the service tax, interest or penalty:

Provided that an order enhancing the service tax, interest or penalty shall not be made unless the person affected thereby has been given a reasonable opportunity of showing cause against such enhancement.

(5) Subject to the provisions of this Chapter, in hearing the appeals and making orders under this section, the Commissioner of Central Excise (Appeals) shall exercise the same powers and follow the same procedure as he exercises and follows in hearing the appeals and making orders under the Central Excise Act, 1944.

SECTION 86: Appeals to Appellate Tribunal -

(1) Save as otherwise provided herein an assessee aggrieved by an order passed by a Commissioner of Central Excise under section 73 or section 83A, or an order passed by a Principal Commissioner of Central Excise or a Commissioner of Central Excise (Appeals) under section 85, may appeal to the Appellate Tribunal against such order within three months of the date of receipt of the order.

(1A) (i) The Board may, by order, constitute such Committees as may be necessary for the purposes of this Chapter.

(ii) Every Committee constituted under clause (i) shall consist of two Principal Chief Commissioners of Central Excise or Chief Commissioners of Central Excise or two Principal Commissioners of Central Excise or Commissioners of Central Excise, as the case may be.

(2) The Committee of Principal Chief Commissioner of Central Excise or Chief Commissioners of Central Excise may, if it objects to any order passed by the Principal Commissioner or 'Commissioner of Central Excise under section 73 or section 83A, direct the Commissioner of Central Excise to appeal to the Appellate Tribunal against the order.

Provided that where the Committee of Principal Chief Commissioners or Chief Commissioners of Central Excise differs in its opinion against the order of the Principal Commissioner or the Commissioner of Central Excise, it shall state the point or points on which it differs and make a reference to the Board which shall, after considering the facts of the order, if is of the opinion that the order passed by the Principal Commissioner or the Commissioner of Central Excise is not legal or proper, direct the Principal Commissioner or the Commissioner of Central Excise to appeal to the Appellate Tribunal against the order.

(2A) The Committee of Commissioners may, if it objects to any order passed by the Commissioner of Central Excise (Appeals) under section 85, direct any Central Excise Officer to appeal on its behalf to the Appellate Tribunal against the order.

Provided that where the Committee of Commissioners differs in its opinion against the order of the Commissioner of Central Excise (Appeals), it shall state the point or points on which it differs and make a reference to the jurisdictional Principal Chief Commissioner or Chief Commissioner who shall, after considering the facts of the order, if is of the opinion that the order passed by the Commissioner of Central Excise (Appeals) is not legal or proper, direct any Central Excise Officer to appeal to the Appellate Tribunal against the order.

Explanation.— For the purposes of this sub-section, "jurisdictional Principal Chief Commissioner or Chief Commissioner" means the Principal Chief Commissioner or the Chief Commissioner having jurisdiction over the concerned adjudicating authority in the matter.

(3) Every appeal under sub-section (2) or sub-section (2A) shall be filed within four months from the date on which the order sought to be appealed against is received by the Committee of Principal Chief Commissioner or Chief Commissioners or, as the case may be, the Committee of Commissioners.'

(4) The Principal Commissioners or the Commissioner of Central Excise or any Central Excise Officer subordinate to him or the assessee, as the case may be, on receipt of a notice that an appeal against the order of the Principal Commissioner or the Commissioner of Central Excise or the Commissioner of Central Excise (Appeals) has been preferred under sub-section (1) or sub-section

(2) or sub-section (2A) by the other party may, notwithstanding that he may not have appealed against such order or any part thereof, within forty-five days of the receipt of the notice, file a memorandum of cross-objections, verified in the prescribed manner, against any part of the order of the Principal Commissioner or the Commissioner of Central Excise or the Commissioner of Central Excise (Appeals), and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in sub section (3).

(5) The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period referred to in sub-section (3) or sub-section (4) if it is satisfied that there was sufficient cause for not presenting it within that period.

(6) An appeal to the Appellate Tribunal shall be in the prescribed form and shall be verified in the prescribed manner and shall, irrespective of the date of demand of service tax and interest or of levy of penalty in relation to which the appeal is made, be accompanied by a fee of, —

(a) where the amount of service tax and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is five lakh rupees or less, one thousand rupees;

(b) where the amount of service tax and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is more than five lakh rupees but not exceeding fifty lakh rupees, five thousand rupees;

(c) where the amount of service tax and interest demanded and penalty levied by any Central Excise Officer in the case to which the appeal relates is more than fifty lakh rupees, ten thousand rupees :

Provided that no fee shall be payable in the case of an appeal referred to in sub-section (2) or sub-section (2A) or a memorandum of cross-objections referred to in sub-section (4).

(6A) Every application made before the Appellate Tribunal, —

(a) in an appeal for rectification of mistake or for any other purpose; or

(b) for restoration of an appeal or an application,

shall be accompanied by a fee of five hundred rupees :

Provided that no such fee shall be payable in the case of an application filed by the Principal Commissioner of Central Excise or the Commissioner of Central Excise or Assistant Commissioner of Central Excise or Deputy Commissioner of Central Excise, as the case may be under this sub-section.

(7) Subject to the provisions of this Chapter, in hearing the appeals and making orders under this section, the Appellate Tribunal shall exercise the same powers and follow the same procedure as it exercises and follows in hearing the appeals and making orders under the Central Excise Act 1944.

7.6 SETTLEMENT COMMISSION

SECTION 31: Definitions — Unless the context otherwise requires,—

(a) "assessee" means any person who is liable for payment of excise duty assessed under this Act or any other Act and includes any producer or manufacturer of excisable goods or a registered person under the rules made under this Act, of a private warehouse in which excisable goods are stored;

(b) "Bench" means a Bench of the Settlement Commission;

(c) "case" means any proceeding under this Act or any other Act for the levy, assessment and collection of excise duty, pending before an adjudicating authority on the date on which an application under sub-section (1) of section 32E is made.

Provided that when any proceeding is referred back by any court, Appellate Tribunal or any other authority, to the adjudicating authority for a fresh adjudication or decision, as the case may be, then such proceeding shall not be deemed to be a proceeding pending within the meaning of this clause;

(d) "Chairman" means the Chairman of the Settlement Commission;

(e) "Commissioner (Investigation)" means an officer of the Customs or a Central Excise Officer appointed as such Commissioner to conduct enquiry or investigation for the purposes of this Chapter;

(f) "Member" means a Member of the Settlement Commission and includes the Chairman and the Vice-Chairman;

(g) "Settlement Commission" means the Customs, Central Excise and Service tax Settlement Commission constituted under section 32; and

(h) "Vice-Chairman" means a Vice-Chairman of the Settlement Commission.

7.6.1 Advantages of Settlement Commission

(i) Quick settlement of disputes to avoid prolonged litigation

(ii) Settlement commission provides chance to turn a new leaf.

(iii) Settlement commission can grant waiver/reduction of penalty, fine or interest.

(iv) Settlement commission can grant immunity from prosecution to an assessee, its directors and partners. (Immunity cannot be granted in respect of prosecution under Indian Penal Code or any other Central law w.e.f. 1-6-2007).

(v) Issues can be resolved within an outer limit of 9 months to 1 year.

7.6.2 Section 31(C) [Corresponding Customs Section 127A(B)] Defines "Case" to mean

- any proceeding under this Act or any other Act
- for the levy, assessment and collection of excise duty/ customs duty,
- ***pending before an adjudicating authority*** on the date on which an application for settlement is made.

Remanded proceedings-Not pending proceedings: However, when any proceeding is referred back by any court, Appellate Tribunal or any other authority, to the adjudicating authority for a fresh adjudication/ decision, then such proceeding shall not be deemed to be a 'Proceeding Pending' for the purposes of the above. Therefore, no settlement application can be filed in respect of cases remanded for fresh adjudication.

Pending appeals not 'case': Since Commissioner (Appeals) is not 'Adjudicating Authority', hence, proceedings pending before him will not be regarded as 'case' for the purposes of Settlement.

SECTION 32: Customs and Central Excise Settlement Commission.-

(1) The Central Government shall, by notification in the Official Gazette, constitute a Commission to be called the Customs, Central Excise and Service Tax Settlement Commission for the settlement of cases under this Chapter and Chapter XIVA of the Customs Act, 1962.

(2) The Settlement Commission shall consist of a Chairman and as many Vice-Chairmen and other Members as the Central Government thinks fit and shall function within the Department of the Central Government dealing with customs and central excise matters.

(3) The Chairman, Vice-Chairman and other Members of the Settlement Commission shall be appointed by the Central Government from amongst persons of integrity and outstanding ability, having special knowledge of, and experience in, administration of customs and central excise laws:

SECTION 32A: Jurisdiction and powers of Settlement Commission —

(1) Subject to the other provisions of this Chapter, the jurisdiction, powers and authority of the Settlement Commission may be exercised by Benches thereof.

(2) Subject to the other provisions of this section, a Bench shall be presided over by the Chairman or a Vice-Chairman and shall consist of two other Members.

(3) The Bench for which the Chairman is the presiding officer shall be the principal Bench and other Benches shall be known as additional Benches.

(4) Notwithstanding anything contained in sub-section (1) and sub-section (2), the Chairman may authorise the Vice-Chairman or other Member appointed to one Bench to discharge also the functions of the Vice-Chairman or, as the case may be, other Member of another Bench.

(5) The principal Bench shall sit at Delhi and the Central Government shall, by notification in the Official Gazette, establish additional Benches at such places as it considers necessary.

(6) Notwithstanding anything contained in the foregoing provisions of this section, and subject to any rules that may be made in this behalf, when one of the persons constituting a Bench (whether such person be the presiding officer or other Member of the Bench) is unable to discharge his functions owing to absence, illness or any other cause or in the event of the occurrence of any vacancy either in the office of the presiding officer or in the office of one or the other members of the Bench, the remaining Members may function as the Bench and if the presiding officer of the Bench is not one of the remaining Members, the senior among the remaining Members shall act as the presiding officer of the Bench:

Provided that if at any stage of the hearing of any such case or matter, it appears to the presiding officer that the case or matter is of such a nature that it ought to be heard of by a Bench consisting of three Members, the case or matter may be referred by the presiding officer of such bench to the Chairman for transfer to such Bench as the Chairman may deem fit.

Provided further that at any stage of the hearing of any such case or matter, referred to in the first proviso, the Chairman may, if he thinks that the case or matter is of such a nature that it ought to be heard by a Bench consisting of three Members, constitute such Bench and if Vice-Chairman is not one of the Members, the senior among the Members shall act as the presiding officer of such Bench.

(7) Notwithstanding anything contained in the foregoing provisions of this section, the Chairman may, for the disposal of any particular case, constitute a special Bench consisting of more than three Members.

(8) Subject to the other provisions of this Chapter, the special Bench shall sit at a place to be fixed by the Chairman.

SECTION 32B: Vice-Chairman to act as Chairman or to discharge his functions in certain circumstances—

(1) In the event of the occurrence of any vacancy in the office of the Chairman by reason of his death, resignation or otherwise, the Vice-Chairman or, as the case may be, such one of the Vice-Chairmen as the Central Government may, by notification in the Official Gazette, authorise in this behalf, shall act as the Chairman until the date on which a new Chairman, appointed in accordance with the provisions of this Chapter to fill such vacancy, enters upon his office.

(2) When the Chairman is unable to discharge his functions owing to absence, illness or any other cause, the Vice-Chairman or, as the case may be, such one of the Vice-Chairmen as the Central

Government may, by notification in the Official Gazette, authorise in this behalf, shall discharge the functions of the Chairman until the date on which the Chairman resumes his duties.

SECTION 32C: Power of Chairman to transfer cases from one Bench to another.—On the application of the assessee or the Principal Chief Commissioner the Chief Commissioner or Commissioner of Central Excise and after giving notice to them, and after hearing such of them as he may desire to be heard, or on his own motion without such notice, the Chairman may transfer any case pending before one Bench, for disposal, to another Bench.

7.6.3 Section 32E (Corresponding Customs Section 127B) are as Follows :

(I) Conditions to be fulfilled before a settlement application is filed to Settlement Commission:

The following conditions must be fulfilled before a settlement application can be filed-

(a) In case of Central Excise, the applicant must be an assessee. "Assessee" means any person who is liable for payment of excise duty assessed under this Act or any other Act and includes any producer or manufacturer of excisable goods or a registered person under the rules made under this Act, of a private warehouse in which excisable goods are stored.

In case of Customs, the applicant may be an importer or exporter or any other person;

(b) the case must have not been adjudicated i.e. settlement application can be made only before adjudication;

(c) the application should contain-

(i) a full and true disclosure of his duty liability which has not been disclosed before the Central Excise/ proper Officer having jurisdiction,

(ii) the manner in which such liability has been derived,

(iii) the additional amount of excise/customs duty accepted to be payable by him, and

(iv) such other particulars as may be prescribed,

(v) including the particulars of such excisable/ dutiable goods in respect of which he admits short levy on account of -

- misclassification,

- under-valuation,

- inapplicability of exemption notification or

- CENVAT credit or

- otherwise (Amendment by the Finance Act, 2010 w.e.f 8-5-2010)

[Before amendment it was provided that the following shall not be eligible for settlement:

(i) the goods in respect of which no proper record has been maintained by the assessee in his daily stock register (in case of central excise); or

(ii) the goods not included in the entry made under this Act (in case of customs)].

(d) the applicant has filed returns showing production, clearance and central excise duty paid in the prescribed manner; (in case of customs, the applicant has filed a bill of entry, or a shipping bill, in respect of import or export of such goods, as the case may be);

(e) a show cause notice for recovery of duty issued by the Central Excise Officer has been received by the applicant; (in relation to such bill of entry or shipping bill, a show cause notice has been issued to him by the proper officer applicable to Custom);

(f) the additional amount of duty accepted by the applicant in his application exceeds3 lakh;

(g) the applicant has paid the additional amount of excise duty accepted by him along with interest under section 11AA;

(h) if any excisable/ dutiable goods, books of accounts or other documents or any sale proceeds of goods have been seized, application for settlement has been made only after 180 days from the date of seizure.

(II) Cases for which no settlement application can be made : The Settlement Commission cannot entertain the following cases -

(a) cases pending with the Appellate Tribunal or any Court;

(b) cases involving the interpretation of the classification goods under the Customs/Excise Tariff;

(c) every application shall be accompanied by such fees as may be prescribed.

(d) An application made under this section shall not be allowed to be withdrawn by the applicant.

(III) Fees for filing an application : An application to Settlement Commission shall be made in prescribed form with a fee of ₹ 1,000 and cannot withdrawn by the applicant.

7.6.4 SECTION 32F (corresponding Customs section 127C) provides for the following procedure to be followed by the Settlement Commission for disposal of a case -

(i) Acceptance or Rejection of Application: On receipt of an application for settlement, the Settlement Commission shall, within 7 days from the date of receipt of the application, issue a notice to the applicant to explain in writing as to why the application made by him should be allowed to be proceeded with. After taking into consideration the explanation provided by the applicant, the Settlement Commission, shall, within a period of 14 days from the date of the notice, pass an order either allowing the application to be proceeded with, or rejecting the application. In case of rejection, the proceedings before the Settlement Commission shall abate on the date of rejection.

However, where no notice has been issued or no order has been passed within the aforesaid period by the Settlement Commission, the application shall be deemed to have been allowed to be proceeded with.

A copy of every such order shall be sent to applicant and to the Principal Commissioner or the Commissioner having jurisdiction.

(ii) Calling of Report from Principal Commissioner or Commissioner when Application Allowed: Where an application is allowed or deemed to have been allowed to be proceeded with, the Settlement Commission shall, within seven days from the date of order allowing the application, call for a report along with relevant records from the Principal Commissioner or the Commissioner having jurisdiction and the Commissioner shall furnish the report within 30 days of receipt of communication from the Settlement Commission.

However, if the Commissioner does not furnish the report within 30 days as aforesaid, the Settlement Commission shall proceed further in the matter without the report of the Commissioner.

(iii) Further investigation by Commissioner (Investigation) : Where a report of the Commissioner has been furnished within 30 days as aforesaid, the Settlement Commission may, after examination of such report, if it is of the opinion that any further enquiry or investigation in the matter is necessary, direct the Commissioner (Investigation) within 15 days of the receipt of the report, to make or cause to be made such further enquiry or investigation and furnish a report within a period of 90 days of the receipt of the communication from the Settlement Commission, on the matters covered by the application and any other matter relating to the case.

However, if the Commissioner (Investigation) does not furnish the report within the aforesaid period, the Settlement Commission shall proceed to pass an order without such report.

(iv) Passing of Final Order: After examination of the records and the report the Principal Commissioner or the Commissioner of Central Excise/Customs including the report of the Commissioner (Investigation) if any, and after giving an opportunity of being heard both to the applicant and to the Principal Commissioner or the Commissioner and examining such other evidence as may be placed before it, the Settlement Commission shall pass final order as it thinks fit in accordance with the provisions of the Act.

The order shall be passed only on the matters covered by the application and any other matter relating to the case not covered by the application, but referred to in the report of the Principal Commissioner or the Commissioner or Commissioner (Investigation).

(v) Time limit for Passing of Final Order: The final order on settlement shall be passed -

- within 9 months from the last day of the month in which the application was made,

- failing which

(a) the settlement proceedings shall abate, and

(b) the adjudicating authority before whom the proceeding at the time of making the application was pending, shall dispose of the case in accordance with the provisions of this Act as if no application for settlement had been made.

Extension of time by 3 months : The aforesaid period of 9 months may, for reasons to be recorded in writing, be extended by the Settlement Commission for a further period not exceeding 3 months.

(vi) Terms of Final Order: Such an order shall provide for the terms of settlement including any demand by way of duty, penalty or interest, the manner in which any sum due under the settlement shall be paid and all other matters to make the settlement effective. In case of rejection, such order shall contain reasons thereof. Further, the amount of settlement ordered by the Settlement Commission shall not be less than the duty liability admitted by the applicant in the settlement application.

(vii) Recovery : Where any duty, interest, fine and penalty payable in pursuance of a final order is not paid by the assessee within 30 days of receipt of a copy of the order by him, the amount which remains unpaid, shall be recovered along with interest due thereon, as the sums due to the Central Government by the Central Excise Officer having jurisdiction over the assessee in accordance with the provisions of section11.

(viii) Consequences of Settlement obtained by Fraud: The orders passed by the Settlement Commission are conclusive and can only be reopened by the Settlement Commission. Any such order obtained by way of fraud or misrepresentation of facts shall be void. In case the Settlement has become void because it has been obtained by fraud and misrepresentation of facts, then the matters in respect of settlement shall be deemed to have been revived from the stage when the application was made to the Settlement Commission and the Central Excise/proper officer shall decide such case within a period of 2 years from the date of receipt of communication that the settlement has become void.

7.6.5 SECTION 32D

The decision of Settlement Commission will be according to the opinion of the majority. However, in case the members are equally divided on any point(s), then-

(a) the point(s) of difference shall be referred to Chairman or one or more additional members, and

(b) such point or points will be decided according to the opinion of the majority of the total members (i.e. additional members and the members who first heard it).

7.6.6 Power Of The Settlement Commission

(i) Power to order Provisional Attachment to Protect Revenue [Section 32G (Customs section 127D)]: The Settlement Commission has the power to order provisional attachment of any property belonging to the applicant in the prescribed manner. Such order can be made by the Settlement Commission during the pendency of any proceedings before it where it is of the opinion that such attachment is necessary for the purpose of protecting the interests of the revenue.

Cessation of attachment : Any such provisional attachment shall cease to have effect from the date the sums due to the Central Government in respect of such attachment are discharged by the applicant and the evidence in respect of such discharge is submitted to the Settlement Commission.

(ii) Power to Grant Immunity from Prosecution or Imposition of Penalty or Fine (Section 32K (Customs section 127H)] : If the Settlement Commission is satisfied that applicant has cooperated with it in the proceedings before it and has made a full and true disclosure of his duty liability, then the Commission may grant to an applicant immunity from-

(a) prosecution for any offence under this Act, and

(b) also wholly or partly from imposition of any penalty and fine under this Act.

Exception : The Settlement Commission cannot grant any immunity if the proceedings for the prosecution of the applicant were instituted before the date of receipt of the settlement application.

Immunity Withdrawn: The immunity so granted will be withdrawn in any of the following cases -

(a) If the applicant fails to pay any sum specified in the settlement order within the time specified in such order or fails to comply with any other condition subject to which the immunity was granted; or

(b) If the Settlement Commission is satisfied that the applicant had in the course of the proceedings concealed any particulars material to the settlement or had given false evidence.

(iii) Power to send case back to Central Excise/Customs Officer [Section 32L (Customs section 127I)]: If the applicant does not cooperate with the Settlement Commission in the proceeding before it, the Settlement Commission may send the case back to the Central Excise/Customs officer for further action as per law. If the application is sent back, then, all submissions made and all the information giver by the applicant before the Settlement Commission can be used by the Excise/ Customs officer while deciding the case.

In that case, the period commencing from the date of the application to the Settlement Commission and ending with the date of receipt by the Central Excise/Customs officer of the order sending case back to him, shall be excluded for the purposes of time limit u/s 11A and interest u/s 11BB

(iv) Other Powers: The Settlement Commission shall have the following other powers -

(a) all the powers which are vested in a Central Excise/Customs Officer under this. Act or the rules made there under;

(b) power to regulate its own procedure;

(c) exclusive jurisdiction over the case where application is allowed to be proceeded with and until the settlement order has been passed.

SECTION 32H: Power of Settlement Commission to reopen completed proceedings — [Omitted w.e.f. 14.05.2015]

SECTION 32-I: Powers and procedure of Settlement Commission —

(1) In addition to the powers conferred on the Settlement Commission under this Chapter, it shall have all the powers which are vested in a Central Excise Officer under this Act or the rules made thereunder.

(2) Where an application made under section 32E has been allowed to be proceeded with under section 32F, the Settlement Commission shall, until an order is passed under sub-section (5) of section 32F, have, subject to the provisions of sub-section (4) of that section, exclusive jurisdiction to exercise the powers and perform the functions of any Central Excise Officer, under this Act in relation to the case.

(3) In the absence of any express direction by the Settlement Commission to the contrary, nothing in this Chapter shall affect the operation of the provisions of this Act in so far as they relate to any matters other than those before the Settlement Commission.

(4) The Settlement Commission shall, subject to the provisions of this Chapter, have power to regulate its own procedure and the procedure of Benches thereof in all matters arising out of the exercise of its powers, or of the discharge of its functions, including the places at which the Benches shall hold their sittings.

SECTION 32J: Inspection, etc., of reports — No person shall be entitled to inspect, or obtain copies of, any report made by any Central Excise Officer to the Settlement Commission; but the Settlement Commission may, in its discretion furnish copies thereof to any such person on an application made to it in this behalf and on payment of the prescribed fee:

Provided that, for the purpose of enabling any person whose case is under consideration to rebut any evidence brought on record against him in any such report, the Settlement Commission shall, on an application made in this behalf, and on payment of the prescribed fee by such person, furnish him with a certified copy of any such report or part thereof relevant for the purpose.

SECTION 32M: **Order of settlement to be conclusive —** Every order of settlement passed under sub-section (5) of section 32F shall be conclusive as to the matters stated therein and no matter covered by such order shall, save as otherwise provided in this Chapter, be reopened in any proceeding under this Act or under any other law for the time being in force.

SECTION 32N: **Recovery of sums due under order of settlement —** Any sum specified in an order of settlement passed under sub-section (5) of section 32F may, subject to such conditions if any, as may be specified therein, be recovered, and any penalty for default in making payment of such sum may be imposed and recovered as sums due to the Central Government in accordance with the provisions under section 11 by the Central Excise Officer having jurisdiction over the person who made the application for settlement under section 32E.

7.6.7 Bar on subsequent application for settlement in certain cases [Section 32-O (Customs Section 127L), Amendment by the Finance Act, 2010 w.e.f. 8-5-2010]

(i) an order of settlement provides for the imposition of a penalty on the person who made the application for settlement, on the ground of concealment of particulars of his duty liability; or

(ii) after the passing of an order of settlement in relation to a case, as aforesaid, such person is convicted of any offence under this Act in relation to that case; or

Explanation.— In this clause, the concealment of particulars of duty liability relates to any such concealment made from the Central Excise Officer.

(iii) the case of such person is sent back to the Central Excise Officer having jurisdiction by the Settlement Commission under section 32L then, applicant shall not be entitled to apply for settlement in relation to any other matter.

7.6.8 Adjudicating Authority Can Track Information Submitted in the Office of Settlement Commission

Cases which are sent back to the adjudication authority, all submissions or disclosures and information furnished by applicant before Settlement Commission can be made use of by the adjudicating authority while finalizing demand of duties, interest and imposing penalties.

7.6.9 Entire Amount of Duty Should be Disclosed Under Section 127B of The Customs Act

Application u/s 127B is maintainable only if the duty liability is disclosed. The disclosure contemplated is in the nature of voluntary disclosure of concealed additional customs duty. Hence, having opted to get their customs duty liability settled by the Settlement Commission, the appellant could not be permitted to dissect the Settlement Commission's order with a view to accept what is favourable to them and reject what is not [*Sanghvi Reconditioners Pvt. Ltd.* v *UOI* 2010 (251) ELT 3 (SC)]

7.6.10 Recovery of Duty Drawback Erroneously Paid by The Revenue

As per section 127A of the Customs Act, 1962, the Settlement Commission have jurisdiction to settle cases relating to the recovery of drawback erroneously paid by the revenue as the claim for duty drawback is nothing but a claim for refund of duty as per the statutory scheme framed by the Government of India or in exercise of statutory powers under the provisions of the Act.

The contention that recovery of duty drawback does not involve levy, assessment and collection of customs duty as envisaged under section 127A(b) was not accepted .

Therefore, the Settlement Commission had jurisdiction to deal with the question relating to the recovery of drawback erroneously paid by the Revenue [*UOI* v *Customs & Excise Settlement Commission* 2010].

SECTION 32P: Proceedings before Settlement Commission to be judicial proceedings — Any proceedings under this Chapter before the Settlement Commission shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purposes of section 196 of the Indian Penal Code.

SECTION 96A of Finance Act, 1994: Definitions — In this Chapter, unless the context otherwise requires,—

(a) "advance ruling" means the determination, by the Authority, of a question of law or fact specified in the application regarding the liability to pay service tax in relation to a service proposed to be provided, by the applicant;

(b) "applicant" means —

(i) (a) a non-resident setting up a joint venture in India in collaboration with a non- resident or a resident; or

(b) a resident setting up a joint venture in India in collaboration with a non-resident; or

(c) a wholly owned subsidiary Indian company, of which the holding company is a foreign company,

who or which, as the case may be, proposes to undertake any business activity in India;

(ii) a joint venture in India; or

(iii) resident falling within any such class or category of persons, as the Central Government may, by notification in the Official Gazette, specify in this behalf,

and which or who, as the case may be, makes application for advance ruling under sub-section (1) of section 96C;

Explanation. — For the purposes of this clause, "joint venture in India" means a contractual arrangement whereby two or more persons undertake an economic activity which is subject to joint control and one or more of the participants or partners or equity holders is a nonresident having substantial interest in such arrangement;

(c) "application" means an application made to the Authority under sub-section (1) of section 96C;

(d) "Authority" means the Authority for Advance Rulings, constituted under sub-section (1), or authorised by the Central Government under subsection *(2A),* of section 28F of the Customs Act, 1962.

(e) "non-resident", "Indian company" and "foreign company" have the meanings respectively assigned to them in clauses (30), (26) and (23A) of section 2 of the Income-tax Act, 1961;

(f) words and expressions used but not defined in this Chapter and defined in the Central Excise Act, 1944 or the rules made thereunder shall apply, so far as may be, in relation to service tax as they apply in relation to duty of excise.

SECTION 96B: **Vacancies, etc., not to invalidate proceedings** — No proceeding before, or pronouncement of advance ruling by, the Authority under this Chapter shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the Authority.

SECTION 96C: Application for advance ruling —

(1) An applicant desirous of obtaining an advance ruling under this Chapter may make an application in such form and in such manner as may be prescribed, stating the question on which the advance ruling is sought.

(2) The question on which the advance ruling is sought shall be in respect of, -

(a) classification of any service as a taxable service under Chapter V;

(b) the valuation of taxable services for charging service tax;

(c) the principles to be adopted for the purposes of determination of value of the taxable service under the provisions of Chapter V;

(d) applicability of notifications issued under Chapter V;

(e) admissibility of credit of duty or tax in terms of the rules made in this regard.

(f) determination of the liability to pay service tax on a taxable service under the provisions of Chapter V.

(3) The application shall be made in quadruplicate and be accompanied by a fee of two thousand five hundred rupees.

(4) An applicant may withdraw an application within thirty days from the date of the application.

SECTION 96D: Procedure on receipt of application —

(1) On receipt of an application, the Authority shall cause a copy thereof to be forwarded to the Principal Commissioner of Central Excise or the Commissioner of Central Excise and, if necessary, call upon him to furnish the relevant records :

Provided that where any records have been called for by the Authority in any case, such records shall, as soon as possible, be returned to the Principal Commissioner of Central Excise or the Commissioner of Central Excise.

(2) The Authority may, after examining the application and the records called for, by order, either allow or reject the application:

Provided that the Authority shall not allow the application where the question raised in the application is, -

(a) already pending in the applicant's case before any Central Excise Officer, the Appellate Tribunal or any Court;

(b) the same as in a matter already decided by the Appellate Tribunal or any Court:

Provided further that no application shall be rejected under this sub-section unless an opportunity has been given to the applicant of being heard:

Provided also that where the application is rejected, reasons for such rejection shall be given in the order.

(3) A copy of every order made under sub-section (2) shall be sent to the applicant and to the Principal Commissioner or the Commissioner of Central Excise.

(4) Where an application is allowed under sub-section (2), the Authority shall, after examining such further material as may be placed before it by the applicant or obtained by the Authority, pronounce its advance ruling on the question specified in the application.

(5) On a request received from the applicant, the Authority shall, before pronouncing its advance ruling, provide an opportunity to the applicant of being heard, either in person or through a duly authorised representative.

Explanation - For the purposes of this sub-section, "authorised representative" has the meaning assigned to it in sub-section (2) of section 35Q of the Central Excise Act, 1944.

(6) The Authority shall pronounce its advance ruling in writing within ninety days of the receipt of application.

(7) A copy of the advance ruling pronounced by the Authority, duly signed by the Members and certified in the prescribed manner shall be sent to the applicant and to the Principal Commissioner or the Commissioner of Central Excise, as soon as may be, after such pronouncement.

SECTION 96E: Applicability of advance ruling —

(1) The advance ruling pronounced by the Authority under section 96D shall be binding only-

(a) on the applicant who had sought it;

(b) in respect of any matter referred to in sub-section (2) of section 96C;

(c) on the Principal Commissioner or the Commissioner of Central Excise, and the Central Excise authorities subordinate to him, in respect of the applicant.

(2) The advance ruling referred to in sub-section (1) shall be binding as aforesaid unless there is a change in law or facts on the basis of which the advance ruling has been pronounced.

SECTION 96F: Advance ruling to be void in certain circumstances –

(1) Where the Authority finds, on a representation made to it by the Principal Commissioner or the Commissioner of Central Excise or otherwise, that an advance ruling pronounced by it under sub-section (4) of section 96D has been obtained by the applicant by fraud or misrepresentation of facts, it may, by order, declare such ruling to be void ab initio and thereupon all the provisions of this Chapter shall apply (after excluding the period beginning with the date of such advance ruling and ending with the date of order under this sub-section) to the applicant as if such advance ruling had never been made.

(2) A copy of the order made under sub-section (1) shall be sent to the applicant and the Principal Commissioner or the Commissioner of Central Excise.

SECTION 96G: Powers of Authority –

(1) The Authority shall, for the purpose of exercising its powers regarding discovery and inspection, enforcing the attendance of any person and examining him on oath, issuing commissions and compelling production of books of account and other records, have all the powers of a civil court under the Code of Civil Procedure, 1908.

(2) The Authority shall be deemed to be a civil court for the purposes of section 195, but not for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973, and every proceeding before the Authority shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purpose of section 196 of the Indian Penal Code.

SECTION 96H: Procedure of Authority - The Authority shall, subject to the provisions of this Chapter, have power to regulate its own procedure in all matters arising out of the exercise of its powers under this Act.

SECTION 96-I : **Power of Central Government to make rules** —

(1) The Central Government may, by notification in the Official Gazette, make rules for carrying out the provisions of this Chapter.

(2) In particular, and without prejudice to the generality of the foregoing power, such rules may provide for all or any of the following matters, namely:-

(a) the form and manner for making application under sub-section (1) of section 96C;

(b) the manner of certifying a copy of advance ruling pronounced by the Authority under sub-section (7) of section 96D;

(c) any other matter which, by this Chapter, is to be or may be prescribed.

(3) Every rule made under this Chapter shall be laid, as soon as may be, after it is made, before each House of Parliament, while it is in session for a total period of thirty days which may be comprised in one session or in two or more successive sessions, and if, before the expiry of the session immediately following the session or the successive sessions aforesaid, both Houses agree in making any modification in the rule or both Houses agree that the rule should not be made, the rule shall thereafter have effect only in such modified form or be of no effect, as the case may be; so, however, that any such modification or annulment shall be without prejudice to the validity of anything previously done under that rule.

7.7 AUTHORITY FOR ADVANCE RULING

Advance Ruling means, determination of a question of law or fact specified in the application submitted by applicant regarding the liability to pay duty in relation to activity of manufacture or import or export proposed to be undertaken by the applicant.

Scope of advance ruling is being extended to cover resident public limited companies; a notification is being issued for this purpose, under section 96A(b)(iii) of the Finance Act, 1994 as amended by Finance Act 2013.

Advance Ruling helps the assessee to be clear about legal aspects in advance (i.e. before starting the business or venture). The Authority for Advance Ruling will give a decision on question raised before it. Such ruling will be binding on the applicant as well as on the department. Every procedure before the Authority for Advance Ruling deemed to be a judicial proceeding.

SECTION 23A: **Definitions —** Unless the context otherwise requires,—

(a) "activity" means production or manufacture of goods; and includes any new business of production or manufacturer proposed to be undertaken by the existing producer or manufacturer, as the case may be.

(b) "advance ruling" means the determination, by the authority of a question of law or fact specified in the application regarding the liability to pay duty in relation to an activity proposed to be undertaken, by the applicant;

(c) "applicant" means —

(i) (a) a non-resident setting up a joint venture in India in collaboration with a non-resident or a resident; or

(b) a resident setting up a joint venture in India in collaboration with a non-resident; or

(c) a wholly owned subsidiary Indian company, of which the holding company is a foreign company,

who or which, as the case may be, proposes to undertake any business activity in India;

(ii) a joint venture in India; or

(iii) a resident falling within any such class or category of persons, as the Central Government may, by notification in the Official Gazette, specify in this behalf,

and which or who, as the case may be, makes application for advance ruling under sub-section (1) of section 23C;

Explanation.— For the purposes of this clause, "joint venture in India" means a contractual arrangement whereby two or more persons undertake an economic activity which is subject to joint control and one or more of the participants or partners or equity holders are a non-resident having substantial interest in such arrangement;

(d) "application" means an application made to the Authority under sub-section (1) of section 23C;

(e) "Authority" means the Authority for Advance Rulings, constituted under sub-section (1), or authorised by the Central Government under sub-section (2A), of section 28F of the Customs Act, 1962.

(f) "Non-resident", "Indian company" and "foreign company" shall have the meanings respectively assigned to them in clause (30), (26) and (23A) of section 2 of the Income Tax Act, 1961.

7.7.1 As Per Section 23A(C) of the Central Excise Act, an Application for Advance Ruling can be Made by any of the following if they Propose to Undertake any business activity in India

(i) A Non-resident setting up a joint venture in India in collaboration with a non-resident or a resident.

(ii) A resident setting up a joint venture in India in collaboration with a non-resident.

(iii) A wholly owned subsidiary Indian company, of which the holding company is a foreign company, such holding company proposes to undertake any business activity in India.

(iv) A joint venture in India in which at least one of the participants, partners, or equity share holders is a non-resident having substantial interest in the joint venture.

(v) As may be specified by the Central Government of India by issuing a notification.

7.7.2 Section 23C(2) provides for the admissibility of application for advance ruling, inter alia, for credit of excise duty paid or deemed to have been paid. The scope of admissibility has been expanded to include credit of service tax paid or deemed to have been paid on Input Services.

7.7.3 Application for Advance Ruling can be made in respect of following questions under Central Excise, Customs and Service Tax

i. Classification of goods or services

ii. Applicable of any exemption notification

iii. Admissibility of CENVAT credit

iv. Determination of Assessable value

v. Determination of origin of goods in case of Customs

vi. Determination of liability to pay duties of excise on any goods

On receipt of application Authority may admit or reject the application. In general in the following cases the application can be rejected in the following cases:

(a) If the question raised is already pending before an officer of Excise or Tribunal or any Court.

(b) If the matter has already been decided by CESTAT or any Court.

Application can be withdrawn within 30 days from the date of filing the application.

Authority for Advance Ruling once accepted the application can decide the case within 90 days from receipt of application.

Authority for Advance Ruling is common in Income Tax, Customs and Central Excise;

As per section 28F(2A) of Customs Act (w.e.f. 19.8.2009), Central Government can authorize Authority of Advance Ruling appointed under section 245-O of the Income Tax Act, 1961 to act as authority for advance for advance rulings under Central excise and customs. Therefore, Authority for Advance Ruling under income tax will also be Authority for excise, customs and service tax matters (Notification No. 143/2009 Cus.(NT) dated 15.9.2009).

SECTION 23B: **Vacancies, etc., not to invalidate proceedings—** No proceeding before, or pronouncement of advance ruling by, the Authority under this Chapter shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the Authority.

SECTION 23C: Application for advance ruling -

(1) An applicant desirous of obtaining an advance ruling under this Chapter may make an application in such form and in such manner as may be prescribed, stating the question on which the advance ruling is sought

(2) The question on which the advance ruling is sought shall be in respect of, —

(a) classification of any goods under the Central Excise Tariff Act, 1985 (5 of 1986);

(b) applicability of a notification issued under sub-section (1) of section 5A having a bearing on the rate of duty;

(c) the principles to be adopted for the purposes of determination of value of the goods under the provisions of this Act.

(d) notifications issued, in respect of duties of excise under this Act, the Central Excise Tariff Act, 1985 and any duty chargeable under any other law for the time being in force in the same manner as duty of excise leviable under this Act;

(e) admissibility of credit of excise duty paid or deemed to have been paid on the goods used in or in relation to the manufacture of the excisable goods.

(f) determination of the liability to pay duties of excise on any goods under this Act.

(3) The Application shall be made in quadruplicate and be accompanied by a fee of two thousand five hundred rupees.

(4) An applicant may withdraw an application within thirty days from the date of the application.

SECTION 23D: Procedure on receipt of application.—

(1) On receipt of an application, the Authority shall cause a copy thereof to be forwarded to the Principal Commissioner of Central Excise or the Commissioner of Central Excise and, if necessary, call upon him to furnish the relevant records:

Provided that where any records have been called for by the Authority in any case, such records shall, as soon as possible, be returned to the Principal Commissioner of Central Excise or the Commissioner of Central Excise.

(2) The Authority may, after examining the application and the records called for, by order, either allow or reject the application:

Provided that the Authority shall not allow the application where the question raised in the application is,—

(a) already pending in the applicant's case before any Central Excise Officer, the Appellate Tribunal or any Court;

(b) the same as in a matter already decided by the Appellate Tribunal or any Court

Provided further that no application shall be rejected under this sub-section unless an opportunity has been given to the applicant of being heard:

Provided also that where the application is rejected, reasons for such rejection shall be given in the order.

(3) A copy of every order made under sub-section (2) shall be sent to the applicant and to the Commissioner of Central Excise.

(4) Where an application is allowed under sub-section (2), the Authority shall, after examining such further material as may be placed before it by the applicant or obtained by the Authority, pronounce its advance ruling on the question specified in the application.

(5) On a request received from the applicant, the Authority shall, before pronouncing its advance ruling, provide an opportunity to the applicant of being heard, either in person or through a duly authorised representative.

Explanation - For the purposes of this sub-section, "authorised representative" shall have the meaning assigned to it in sub-section (2) of section 35Q.

(6) The Authority shall pronounce its advance ruling in writing within ninety days of the receipt of application.

(7) A copy of the advance ruling pronounced by the Authority, duly signed by the Members and certified in the prescribed manner shall be sent to the applicant and to Principal Commissioner or the Commissioner of Central Excise, as soon as may be, after such pronouncement.

SECTION 23E: Applicability of advance ruling —

(1) The advance ruling pronounced by the Authority under section 23D shall be binding only—

(a) on the applicant who had sought it;

(b) in respect of any matter referred to in sub-section (2) of section 23C;

(c) on the Principal Commissioner or the Commissioner of Central Excise, and the Central Excise authorities subordinate to him, in respect of the applicant.

(2) The advance ruling referred to in sub-section (1) shall be binding as aforesaid unless there is a change in law or facts on the basis of which the advance ruling has been pronounced.

SECTION 23F: Advance ruling to be void in certain circumstances.—

(1) Where the Authority finds, on a representation made to it by the Commissioner of Central Excise or otherwise, that an advance ruling pronounced by it under sub-section (6) of section 23D has been obtained by the applicant by fraud or misrepresentation of facts, it may, by order, declare such ruling to be void *ab initio* and thereupon all the provisions of this Act shall apply (after excluding the period beginning with the date of such advance ruling and ending with the date of order under this sub-section) to the applicant as if such advance ruling had never been made.

(2) A copy of the order made under sub-section (1) shall be sent to the applicant and the Principal Commissioner or the Commissioner of Central Excise.

SECTION 23G: Powers of Authority -

(1) The Authority shall, for the purpose of exercising its powers regarding discovery and inspection, enforcing the attendance of any person and examining him on oath, issuing commissions and compelling production of books of account and other records, have all the powers of a civil court under the Code of Civil Procedure, 1908 (5 of 1908).

(2) The Authority shall be deemed to be a civil court for the purposes of section 195, but not for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974), and every proceeding before the Authority shall be deemed to be judicial proceeding within the meaning of section 193 and 228, and for the purpose of section 196, of the Indian Penal Code (45 of 1860).

SECTION 23H: Procedure of Authority — The Authority shall, subject to the provisions of this Chapter, have power to regulate its own procedure in all matters arising out of the exercise of its powers under this Act.

WTO:

The World Trade Organization (WTO) is the only global international organization dealing with the rules of trade between nations. At its heart are the WTO agreements, negotiated and signed by the bulk of the world's trading nations and ratified in their parliaments. The goal is to help producers of goods and services, exporters, and importers conduct their business.

The WTO is an organization for trade opening. It is a forum for governments to negotiate trade agreements. It is a place for them to settle trade disputes. It operates a system of trade rules. Essentially, the WTO is a place where member governments try to sort out the trade problems they face with each other. The goal of the WTO is to improve the welfare of the peoples of the member countries.

GATT 94:

The term "GATT" stands for the "General Agreement on Tariffs and Trade". It is an agreement between States aiming at eliminating discrimination and reducing tariffs and other trade barriers with respect to trade in goods. The GATT 1994 is one of the multilateral agreements annexed to the WTO Agreement. It is an international treaty binding upon all WTO Members.

Impact of tax on GATT 94:

The Most Favoured Nation (MFN) principle, as has been noted, requires Members not to discriminate among countries. The national treatment principle, which complements the MFN principle, requires that an imported product which has crossed the border after payment of customs duties and other charges should not receive treatment that is less favourable than that extended to the like product produced domestically. In other words, the principle requires member countries to treat imported products on the same footing as similar domestically produced goods.

Thus it is not open to a country to levy on an imported product, after it has entered the country on payment of customs duties at the border, internal taxes (such as a sales tax) at rates that are higher than those applied to comparable domestic products. Likewise, regulations affecting the sale and purchase of products in the domestic market cannot be applied more rigorously to imported products.

Study Note - 8

CENTRAL SALES TAX AND VAT ACT

This Study Note includes

8.1 INDIAN VALUE ADDED TAX SYSTEM

The Government of India has excogitated "Value Added Tax (VAT)" on the sale of goods to provide a set-off for the tax already paid through a mechanism of input tax credit. This input tax credit in relation to any period means setting off the input tax by a registered dealer against the amount of his output tax.

In conceptualization of the VAT system the Government aims at the tax is to be paid on value addition at each point of sales to the goods.

DEALER

The dealer is the person who is liable to pay the Tax under the system. Therefore, before delving into the topic of VAT it is necessary to know the term dealer. As defined in the Central Sales Tax Act, 1956 the term 'Dealer' means any person who carries on the business of buying, selling, supplying or distributing goods, directly or otherwise, whether for cash or for deferred payment, or for commission, remuneration or other valuable consideration.

The term dealer explicitly encompasses but not limited to the following having a variation from state to state:

1. an industrial, commercial or trading undertaking of the Government, the Central Government, a State Government, a statutory body, a local authority, company, a Hindu undivided family, a partnership firm, a society, a club or an association which carries on such business;
2. a casual trader, a person who has, whether as principal, agent or in any other capacity, carries on occasional transactions of a business nature involving the buying, selling, supply or distribution of goods in the State, whether for cash or for deferred payment, or for commission, remuneration or other valuable consideration;
3. a commission agent, a broker or del credere agent or an auctioneer or any other mercantile agent by whatever name called, who carries on the business of buying, selling , supplying or distributing goods on behalf of any principal;
4. a non-resident dealer or an agent of a non-resident dealer, a local branch of a firm or company or association situated outside the State;
5. a person who sells goods produced by him by manufacture or otherwise;
6. a person engaged in the business of transfer otherwise than in pursuance of a contract of property in any goods for cash deferred payment or other valuable consideration;
7. a person engaged in the business of transfer of property in goods (whether as goods or in some other form) involved in the execution of a works contract;

8. a person engaged in the business of delivery of goods on hire purchase or any system of payment by installments;
9. a person engaged in the business of transfer of the right to use any goods for any purpose (whether or not for a specified period) for cash, deferred payment or other valuable consideration.

GOODS COVERED UNDER VAT

All the goods including declared goods as mentioned in the Central Sales Tax Act, 1956 are covered under VAT and will get the benefit of input tax credit.

Only few goods which has been kept outside VAT is liquor, lottery tickets, petrol, diesel, aviation turbine fuel and other motor spirit since their prices are not fully market determined. These will continue to be taxed under the Sales Tax Act or any other State Act or even by making special provisions in the VAT Act itself, and with uniform floor rates decided by the Empowered Committee.

REGISTRATION UNDER VAT

Persons Require Registration under the Vat Act

All dealer prior to commencement of the VAT Act in the States, having a Registration Certificate either under Local Sales Tax Act or under Central Sales Tax Act are deemed to be the Registered Dealer. A new dealer will be given a 30 days time from the date of applicability of the Act in the State.

As per the White Paper on Value Added Tax published by the Ministry of Finance, the registration of dealers with gross annual turnover above ₹ 5 lakh will be compulsory. However every States is flexible to fix the threshold limit within ₹ 5 lakh for the small dealers.

No need of compulsory registration for small dealers whose gross annual turnover is less than ₹ 5 lakh. Also, the Empowered Committee of State Finance Minister subsequently allowed the States to increase the threshold limit for the small dealers to ₹ 10 lakh with the condition that the concerned State would bear the revenue loss, on account of increase in limit beyond ₹ 5 lakh.

Example 1 : Mr. X commenced business with effect from 1st July, 2008 for buying and selling automobile parts within the state of Tamil Nadu. His turnover exceeds ₹ 10 lakhs in the month of 1st of December, 2008 then he has to get register within 30 days from the date of crossing the threshold limit of ₹ 10 lakhs.

Every State shall make the provision for voluntary registration of dealers who are not otherwise liable to pay tax. However the voluntary registration process are same as applicable to other dealers who are liable to pay tax under VAT.

Dealers with annual gross turnover not exceeding ₹ 50 lakh who are otherwise liable to pay VAT, shall however have the option for a composition scheme with payment of tax at a small percentage of gross turnover. The dealers opting for this composition scheme will not be entitled to input tax credit.

REGISTRATION PROCESS

The form of application to register and manner of making application, and the fee payable is prescribed by the State VAT Act in each State.

A properly filled application may be filed with the Commercial Tax Officer or Assistant Commissioner of Commercial Taxes or any other authority prescribed by the State VAT Act, who is having a jurisdiction over the principal place of business of the Applicant. On receipt of an application to register the prescribed authority shall register any such dealer and grant him a certificate of registration, if he is satisfied that the applicant is a bona fide dealer and that he complies with the requirements of the Act.

The certificate of registration will be issued with effect from the first day of the month following the month in which such application is made or from such earlier date as may be mutually agreed.

The prescribed authority may refuse to grant a certificate of registration to the applicant for any good and sufficient reasons to be recorded in writing, after allowing the applicant to show cause in writing against such refusal.

The Act may contains provision relating to suo-moto Registration of dealer. The competent authority may after conducting such survey, inspection or enquiry as may be prescribed, finds a dealer liable to be registered has failed to inform the competent authority of his liability to be registered, proceed to register such person under the Act.

SECURITY FOR REGISTRATION

The act may prescribe the authority for the proper payment of the tax, from time to time demand from a registered dealer or from a dealer who has applied for registration under this Act, reasonable security not exceeding an amount to be paid in a manner suggested in the Act.

The prescribed authority as per the state VAT Act may by order forfeit the whole or any portion of the security furnished by a dealer:

1. for collecting any amount of tax, interest or penalty that is payable by such dealer, or
2. if such dealer is found to have misused any prescribed certificate or declaration or has failed to keep or retain them in the prescribed manner. -
3. No order shall be passed under sub-section (2), without giving the dealer an opportunity of showing cause in writing against such forfeiture.

VAT RATES AND THE COMMODITIES

The VAT covers about 550 goods and only two basic VAT rates of 4% and 12.5%, plus a specific category of tax-exempted goods and a special VAT rate of 1% only for gold and silver ornaments, etc. are applicable.

The uniform VAT rate will abolish the multiplicity of rates in the existing structure. Under the exempted category, there will be about 46 commodities comprising of natural and unprocessed products in unorganised sector, items which are legally barred from taxation and items which have social implications. Included in this exempted category is a set of maximum of 10 commodities flexibly chosen by individual States from a list of goods (finalised by the Empowered Committee) which are of local social importance for the individual States without having any inter-state implication. The rest of the commodities in the list will be common for all the States.

A VAT rate of 4% is applicable to the largest number of goods (about 270), common for all the States, comprising of items of basic necessities such as medicines and drugs, all agricultural and industrial inputs, capital goods and declared goods.

The remaining commodities, common for all the States, will fall under the general VAT rate of 12.5%. In terms of decision of the Empowered Committee, items relating to sugar, textile and tobacco, because of initial organisational difficulties, will not be imposed for one year after the introduction of VAT, and till then the existing arrangement will continue.

RETURNS AND FILING

A simplified form of returns may be used and such form is to be notified by each State. Returns are to be filed monthly/quarterly as specified in the State Acts/Rules, and will be accompanied with payment challans.

Every return furnished by dealers will be scrutinised expeditiously within prescribed time limit from the date of filing the return. If any technical mistake is detected on scrutiny, the dealer will be required to pay the deficit appropriately.

Every return shall be signed and verified-

1. In the case of an individual, by the individual himself, and where the individual is absent from India, either by the individual or by some person duly authorised by him in this behalf and where the individual is mentally incapacitated from attending to his affairs, by his guardian or by any other person competent to act on his behalf;
2. 'In the case of a Hindu Undivided Family, by a Karta and where the Karta is absent from India or is mentally incapacitated from attending to his affairs, by any other adult member of such family;
3. In the case of a company or local authority, by the principal officer thereof;
4. In the case of a firm, by any partner thereof, not being a minor;
5. in the case of any other association, by any member of the association or persons;
6. in the case of a trust, by the trustee or any trustee; and
7. in the case of any other person, by some person competent to act on his behalf.

SELF-ASSESSMENT

The basic simplification in VAT is that VAT liability will be self-assessed by the dealers themselves in terms of submission of returns upon setting off the tax credit.

Return forms as well as other procedures will be simple in all States. There will no longer be compulsory assessment at the end of each year as is existing now. If no specific notice is issued proposing departmental audit of the books of accounts of the dealer within the time limit specified in the Act, the dealer will be deemed to have been self-assessed on the basis of returns submitted by him.

APPELLATE AUTHORITIES

1. An appeal from every original order under the VAT Act or the rules made thereunder shall lie,-
   i. if the order is made by a an Assistant Commissioner or Sales Tax Officer, or any other officer subordinate thereto, to the Deputy Commissioner;
   ii. if the order is made by an Deputy Commissioner, to the Joint Commissioner;
   iii. if the order is made by a Joint Commissioner, Additional Commissioner, or Commissioner, to the Tribunal.
2. In the case of an order passed in appeal by an Deputy Commissioner or, as the case may be, by a Joint Commissioner, a second appeal shall lie to the Tribunal.
3. The Commissioner on receipt of notice that an appeal against the order passed in appeal by the Deputy Commissioner or, as the case may be, by the Joint Commissioner has been preferred by the other party to the Tribunal may, within thirty days of receipt of the notice, file a memorandum of cross objection against any part of the order passed in appeal by the Deputy Commissioner or, as the case may be, by the Joint Commissioner and such memorandum shall be disposed of by the Tribunal as if it were an appeal.

A person/Commissioner of Commercial Taxes not satisfied by the order of the Tribunal may approach the High court of the State either in appeal or revision within Ninety-days from the date of communication of the order, the decision of which will be final.

PENALTY & OTHER MEASURES

The penalties prescribed in the VAT Act are different in for different Offences and it still differs from state to State.

REFUNDS

Where any amount is refundable to a dealer after having duly verified the fact of deposit of such amount, the assessing authority shall in the prescribed manner refund to such dealer the amount to be refunded either by cash payment or by adjustment against the tax or other sum due in respect of any other period. Such refundable amount shall carry interest at the rate as may be notified by the State Government from time to time, with effect from the date of its deposit.

Where an amount or tax is collected at any check-post from any person who is not registered under the Act and such amount or tax is not found payable by him, or where an amount in lieu of tax for any work is deducted in any manner by an awarder from any bill of payment to a contractor, who is not liable to get registration under the Act, the amount so collected or deducted shall be refunded in the prescribed manner by the Assistant Commissioner or the Commercial Taxes Officer, as the case may be, in whose territorial jurisdiction such person or contractor ordinarily resides.

Any tax levied and collected under this Act, in respect of the sale or purchase inside the State of any declared goods which are subsequently sold in the course of inter-State trade or commerce and on which tax has been paid under the Central Sales Tax Act, 1956 (Central Act 74 of 1956), shall be refunded to the person making such sale or purchase in the course of inter-State trade or commerce.

A refund can be claimed only by the dealer or the person, who has actually suffered the incidence of tax; and the burden of proving the incidence of tax so suffered shall be on the dealer or the person claiming the refund.

8.2 CENTRAL SALES TAX ACT, 1956

Purpose/Scope

(i) This Act is applicable to sales/purchases taking place in course of interstate trade and commerce.

(ii) The interstate nature of transaction is to be determined as defined in Section 3(a)/(b). If sale/purchase occasions movement of goods from one State to another State, it is an interstate sale. A sale, effected by transfer of documents of title to goods when goods are in inter-state movement, is also an inter-state sale.

(iii) Section 4 of the CST Act determines situs of sale: i.e. State in which the sale takes place. Accordingly the situs is to be decided on the location of the goods at the time of sale.

(iv) Section 5 defines the sale/purchase taking place in course of import/export and such transactions are immune from levy of any tax by State Government or Central Government. [(Sections 5(1), 5(2) and 5(3)].

The sale of goods to any exporter for the purpose of complying with the pre-existing order and covered by Section 5(3) is also exempt as deemed export. These sales are to be supported by Form H along with export order details and copy of bill of lading etc. as evidence of actual export.

EXEMPTIONS

(i) Section 6 is charging Section. As per Section 6(2) subsequent inter-state sale transaction taking place by transfer of documents of title to goods, when the goods are in course of movement, are exempt. For this purpose the claimant dealer has to obtain Form E-1 from his vendor (if such vendor is first seller otherwise, E-II) and Form 'C' from the buyer.

(ii) Sale to notified foreign diplomat authorities is also exempt u/s. 6(3) against Form 'J'.

(iii) The interstate sale to units situated in Special Economic Zone (SEZ) or developers of SEZ against Form 'I' are exempt as per Sections 8(6) read with Section 8(8).

BRANCH/CONSIGNMENT TRANSFER

Under Section 6A, branch/consignment transfer is allowed only if Form 'F' is produced, else it will be deemed to be a sale. Form 'F' is required to be obtained from transferee branch/agent. One Form 'F' can cover transfers effected in one calendar month.

RATES OF TAX

As per Section 8 of CST Act, the rates of taxes are to be decided as per rates under Local Act. The rates can be as under:

(From 1-6-2008 onwards)

Local Rate of Tax	Rate of Tax under C.S.T. Act	
	Supported by 'C' Form (Form D is abolished)	**Without 'C' Form**
Declared goods	2%	4%
If the goods are generally exempt under Local Act	Exempt	Exempt
1%	1% (C form not required)	1%
4%	2%	4%
5%	2%	5%
12.5%	2%	12.5%

REGISTRATION, FORM 'C' PURCHASES AND OTHER PROVISIONS

(i) There is no threshold limit for registration under CST Act and hence even on the basis of single transaction a dealer will be liable for registration under Section 7(1). The dealer can also obtain registration voluntarily along with registration under VAT Act as per Section 7(2) of CST Act. Application for registration should be in Form A. Registration certificate will be in Form B.

(ii) As per Section 9(2), the interest/penalty/return/assessment provisions applicable under Local Act are also applicable to CST Act. In addition there are provisions for levy of penalty u/s. 10 like contravention of the conditions of declaration forms, wrong issue of form etc.

(iii) Purchases to be effected against Form 'C' are subject to conditions. The compliance is to be checked before using Form 'C'. In nutshell, it can be mentioned that Form 'C' can be used for effecting purchases which are meant for:

a) Resale by him
b) Use in manufacturing/ processing of goods for sale
c) Use in mining
d) Use in generation/ distribution of power
e) Use in packing of goods for sale/resale
f) Use in telecommunication network.

(iv) One 'C' form can be issued for one quarter of a financial year. Similarly EI/EII can also be issued on quarterly basis.

The Central Government has substituted second and third proviso to Rule 12(1) vide Notification No. 588(E) dated 16th September, 2005. According to these provisos, with effect from 1st October, 2005, Form C will have to be collected separately for each quarter of the year. Form D was required to be obtained transaction wise. However, Form D has been abolished with effect from 1st April, 2007.

Central Government has also substituted sub rule (7) to rule 12 with effect from 1st October, 2005. Form C or certificate in Form E-I or E-II will have to be submitted to sales tax department within three months from the end of the quarter in which sale is effected. In case of Form F, it is to be obtained on monthly basis and it is to be submitted to the sales tax department within three months from the end of the month in which goods are transferred to the interstate branch or agent. In Maharashtra State, the Commissioner of Sales Tax has exempted the dealer from submission of Form C, D, F, H, E-I or E-II. Instead of that, dealers are required to submit the list of missing forms on quarterly basis as per the format specified in Trade Circular No. 28T of 2005 dated 24.10.2005.

(v) From 11-5-2002 the six deemed transactions of sale, including works contracts and leases are taxable under the CST Act if they are effected in the course of inter-state trade.

(vi) Chapter VI-A provides for filing of appeals before Central Sales Tax Appellate Authority in case of disputes involving more than one state.

(vii) In addition, there are other provisions for declared goods, liability in case of companies, offences and prosecution, etc.

Levy and collection of tax and penalties [Section 9]

(1) The tax payable by any dealer under this Act on sales of goods effected by him in the course of interstate trade or commerce, whether such sales fall within clause (a) or clause (b) of section 3, shall be levied by the Government of India and the tax so levied shall be collected by that Government in accordance with the provision of sub-section (2) in the State from which the movement of the goods commenced.

Provided that, in the case of a sale of goods during their movement from one State to another, being a sale subsequent to the first sale in respect of the same goods and being also a sale which does not fall within sub-section (2) of section 6, the tax shall be levied and collected–

(a) Where such subsequent sale has been effected by a registered dealer, in the State from which the registered dealer obtained or, as the case may be, could have obtained, the form prescribed for the purposes of clause (a) of sub-section (4) of section 8 in connection with the purchase of such goods, and

(b) Where such subsequent sale has been effected by all unregistered dealer in the State from which such subsequent sale has been effected.

(2) Subject to the other provisions of this Act and the rules made thereunder, the authorities for the time being empowered to assess, re-assess, collect and enforce payment of any tax under general sales tax law of the appropriate State shall, on behalf of the Government of India, assess, re-assess, collect and enforce payment of tax, including any penalty, payable by a dealer under this Act as if the tax or penalty payable by such a dealer under this Act is a tax or penalty payable under the general sales tax law of the State and for this purpose they may exercise all or any of the powers they have under the general sales tax law of the State and the provisions of such law, including provisions relating to returns, provisional assessment, advance payment of tax, registration of the transferee of any business, imposition of the tax liability of a person carrying on business on the transferee of, or successor to, such business, transfer of liability of any firm or Hindu undivided family to pay tax in the event of the dissolution of such firm or partition of such family, recovery of tax from third parties, appeals, reviews, revisions, references, refunds, rebates, penalties, Charging or payment of interest, compounding of offences and treatment of documents furnished by a dealer as confidential, shall apply accordingly.

Provided that if in any State or part thereof there is no general sales tax law in force, the Central Government may, by rules made in this behalf make necessary provision for all or any of the matter specified in this sub-section.

(2A) All the provisions relating to offences and penalties (including provisions relating to penalties in lieu of prosecution for all offence or in addition to the penalties or punishment for all offence but excluding the provisions relating to matters provided for in section 10 and 10A) of the general sales tax law of each State shall, with necessary modifications, apply in relation to the assessment, reassessment, collection and the enforcement of payment of any tax required to be collected under this Act in such State or in relation to any process connected with such assessment, reassessment, collection or enforcement of payment as if the tax under this Act were a tax under such sales tax law.

(3) The proceeds in any financial year of any tax, including any penalty levied and collected under this Act in any State (other than a Union Territory) on behalf of the Government of India shall be assigned to that State and shall be retained by it and the proceeds attributable to Union Territories shall form part of the Consolidated Fund of India.

TRANSACTION RELATING TO STOCK TRANSFER & BRANCH TRANSFER

To constitute interstate sales, one of the basic requirements is that there should be sale. If a person sends goods outside from its state to its branch office in another state then it is not sale because you cannot sell goods to yourself. Similarly if a dealer sends goods to its agent in another state who stocks and sells goods on behalf of the dealer, such agent is called consignment agent and such stock transfer is also not considered as interstate sales since there is no sales involved in it, sales will take place when such agent will sell goods. But to prove such stock/branch transfer, F form is required to be produced as proof.

F form required for stock transfer- F form is required to be produced as proof of stock transfer. As per section 6A (1) submission of F form is mandatory to prove stock transfer. Otherwise, the transaction will be treated as sale for all purposes of CST Act.

F Form is issued by the branch office/consignment agent receiving goods as branch/stock transfer to its head office/ principal who is sending the goods by way of stock/ branch transfer. The H.O./ Principal produces such F forms to its assessing authority to prove such stock/branch transfer.

One F Form for one month- First Proviso to Rule 5 of CST Rules 1957 provides that one F form covering receipts during the month can be issued. If space in F form is not adequate, a separate list may be attached as annexure to form F giving details, provided that the annexure is firmly attached to the form. The blank form has to be obtained from sales tax authority in which the transferee is situated, i.e. State where goods were received. If the form is lost, indemnity bond has to be given and duplicate form clearly marked as Duplicate can be issued.

When Stock transfer is treated as Interstate sales- When goods are dispatched to Branch office or consignment agent in other state and thereafter these goods are sold from the branch office or by the consignment agent then it is not a sales and is stock or branch transfer hence no CST liability arises.

However, if the movement of goods is occasioned on account of sales, the movement will be treated as interstate sales. It can be explained with an example Suppose the dealer A registered in Punjab who manufactures some goods and send these goods after manufacturing to its branch office situated at Delhi wherefrom the goods are sold in Delhi. Now the movement of goods from Punjab to Delhi will be treated as stock transfer or branch transfer and for which no CST liability arises and F form will be issued by Delhi Branch to Punjab dealer.

But if a person B in Delhi wants to purchase some goods of special description which is not normally manufactured by A and Mr B places order with A in Punjab for manufacturing special description goods. Now if A manufactures such ordered goods and send them to its branch at Delhi then such movement will be an interstate sales and not a branch transfer since the movement of goods was due to a predetermined contract of sales.

Thus where goods were sold through branch, but buyer was known and identified before goods were dispatched from factory. Obviously this was held as interstate sales and not a stock transfer- Electric Construction and Equipment Co. Ltd. Vs. State of Haryana- (1990) 77 STC 424 (P&H HC DB).

In South India Viscose Ltd. vs. State of Tamilnadu -(1981) 48 STC 232 (SC)= AIR 1981 SC 1604 it was held that if there is a conceivable link between contract of sale and the movement of goods from one state to another in order to discharge the obligation under the contract of sale, the interposition of the agent of seller who may temporarily intercept the movement will not alter the interstate character of the sale.

F form is not a conclusive evidence but it is conclusive after assessing officer passes an order, Submitting F form is not a conclusive evidence per se to prove beyond doubt any stock or branch transfer. The assessing officer may make enquiry as to whether declaration furnished by dealer are true or not. The sales tax authorties can investigate if they are of the opinion that the movement of goods is an interstate sale and not stock transfer.

Section 6A (1) provides that the dealer may submit form F, along with evidence of dispatch of goods. If Dealer fails to furnish such declaration, the movement shall be deemed for all purposes of the Act to have been occasioned as a result of sale. Section 6A (2) provides that if assessing authority is satisfied after making enquiry that the declaration furnished by dealer are true, he shall make an order to that effect and thereupon, the movement of goods to which the declaration relates shall be deemed for the purpose of the CST Act to have been occasioned other than as a result of sale.

In Assam Company (India) Ltd. vs. CT, Assam (1997) 107 STC 154 (Gau HC DB), it was held that F form is not conclusive. Sales Tax Officer can make enquiry whether the declaration is true and can reject the F form, if the transaction is found not to be genuine.

In D Dhandapani vs. State of Tamilnadu-(1995) 96 STC 98(Mad HC DB), it was held that section 6A(2) of CST Act authorizes Assessing officer to make enquiry that particulars contained in the declaration furnished by the dealer are true and for this purpose other evidence produced by dealer is also to be considered. Authority can call for other information to verify the truth of particulars contained in form F. The dealer has to prove that details in form F are true. If he is unable to do so, transfer of goods can be taken as on account of interstate sales.

It has been held that by production of form F and providing proof of dispatch of goods, the initial burden of proof on the dealer is discharged- State of AP vs. Dairy Development Corporation Ltd- (1994) 95 STC 478 (AP HC).

Once assessing officer had made enquiry and passed order that the particulars stated are correct, the presumption that the movement has occasioned otherwise that as a result of sale is conclusive. Reopening of assessment under State Sales Tax would not be permissible only on limited grounds of fraud, collusion, misrepresentation or suppression of material facts- Ashok Leyland Ltd vs. State of Tamilnadu 2004 AIR SCW 1001.

ASSESSMENT ORDERS [SECTIONS 6A (1), 6A (2) AND 6A (3)]

There is confusion in the minds of dealers/ assessees as to the appellate forum to be approached in case of assessment orders passed under Sections 6A(1), 6A(2) and 6A(3) of the Central Sales Tax Act, 1956.

(i) Introduction

(a) CST Act deals with taxation of inter-state sales made by the dealers. A sale which occasions movement of goods from one State to another or is effected by transfer of documents of title to the goods during the movement from one State to another falls within the ambit of inter-state sale and liable for tax under the CST Act.

(b) If the movement of the goods does not takes place as a result of sale, but effected by a dealer to his own place of business or to his agent or principal in another State, then there is no tax liability on the dealer, since there is no sale of goods, subject to establishment of movement of goods otherwise than as a result of sale. CST Act stipulates the conditions to be fulfilled by the dealer, to prove that the material movement has taken place not as a result of sale, but on account of stock transfer to his place of business or to his agent or principal in another State(s).

(ii) Conditions for granting exemption to stock transfers

(a) The dealer effecting stock transfer of goods from one State to his place of business or to his agent or principal in another State, shall obtain a declaration in Form 'F' signed by the authorised signatory in other State(s), issued by the VAT department in those State(s), indicating the details of stock transfers made on the declaration Form, such as stock transfer challan no., date, value of the materials, vehicle no., LR No., date etc. The dealer is also required provide proof evidencing dispatch of goods to his place of business or to his agent or principal in other State(s). If the dealer fails to furnish the Form 'F' declarations and prove movement of goods to another State other than by way of sale, then the stock transfers shall be treated as sales.

(b) Rule 6A of the CST Act is reproduced hereunder for ready reference:

"6A (1) Where any dealer claims that he is not liable to pay tax under this Act, in respect of any goods, on the ground that the movement of such goods from one State to another was occasioned by reason of transfer of such goods by him to any other place of his business or to his agent or principal, as the case may be, and not by reason of sale, the burden of proving that the movement of those goods was so occasioned shall be on that dealer and for this purpose he may furnish to the assessing authority, within the prescribed time or within such further time as that authority may, for sufficient cause, permit, a declaration, duly filled and signed by the principal officer of the other place of business, or his agent or principal, as the case may be, containing the prescribed particulars in the prescribed form obtained from the prescribed authority, along with the evidence of despatch of such goods and if the dealer fails to furnish such declaration, then the movement of such goods shall be deemed for all purposes of this Act to have been occasioned as a result of sale".

(c) Rule 12(5) of the Central Sales Tax (Registration and Turnover) Rules, 1957 (hereinafter referred to as "CST Rules") stipulates that the declaration referred to in sub-section (1) of Section 6A shall be in Form 'F'.

(d) A single declaration form shall cover the stock transfers effected by the dealer during one calendar month.

(e) In effect, a dealer, who effected stock transfer of goods to his place of business or agent or principal in another State shall obtain one Form 'F' for each of the months during the year. If there are stock transfers during all the twelve months in a year, the dealer is required to obtain twelve (12) 'F' Forms from his place of business or agent or principal in another State and submit to his assessing authority along with proof of dispatch of goods to get exemption.

(f) The dealer has to submit forms obtained from his branch or agent or principal outside the State, within three months from the end of the month in which stock transfers took place.

(g) In case the dealer fails to submit the 'F' Forms, the movement of goods shall be treated as a result of sale and CST shall be levied, as per Section 6A(1) of the CST Act.

(iii) Assessment of stock transfers

(a) The assessing authority is required to verify the Form 'F' declarations furnished by the dealer and proof of dispatch of goods other than by way of sale and if he is satisfied that the movement of the goods from one State to another State is not as a result of sale, he may pass assessment order, admitting the stock transfers and grant exemption from taxable turnover, since the movement of the goods has been occasioned otherwise than as a result of sale. Rule 6A(2) of the CST Act dealing with assessment is reproduced hereunder for ready reference.

(b) If the assessing authority is satisfied that after making such inquiry as he may deem necessary that the particulars contained in the declaration furnished by a dealer under sub-section (1) are true, he may, at the time of, or at any time before, the assessment of the tax payable by the dealer under this Act, make an order to that effect and thereupon the movement of goods to which the declaration relates shall, subject to provisions of sub-section (3), be deemed for the purpose of this Act to have been occasioned otherwise than as a result of sale".

(c) The rule stipulates that the assessing authority required to pass assessment order, treating the movement of goods otherwise than as a result of sale and exempt the transaction from CST, in case the assessing authority is satisfied that declarations and documentary evidence furnished by the dealer, in support of claim that goods are moved from one State to another State otherwise than as a result of sale, are true.

(d) If the assessing authority after verification of the declaration forms and documentary evidence submitted by the dealer, in support of claim for stock transfers otherwise than as a result of sale, the assessing authority shall pass an order, rejecting the claim for stock transfers. In such a case, the movement of goods shall be treated as a result of sales and CST shall be levied on such transfers from one State to another.

(iv) Difference between orders under Section 6A(1) and 6A(2):

(a) Order under Section 6A(1): The assessing authorities are required to pass orders under Section 6A(1) of the CST Act, in case the dealer failed to submit Form 'F' declarations. In this case, the claim for stock transfers is rejected for non-submission of 'F' Forms. Genuineness of the movement of goods otherwise than by way of sale is not decided in the orders passed under this Section. The order is purely on account of non-submission of 'F' Forms. Since 'F' Forms are not submitted, the claim from stock transfers otherwise by way of sale is rejected and tax is levied.

(b) Forms and documents in support of claim for inter-state movement of goods otherwise than by way of sale submitted by the dealer. The assessing authority may reject the claim of the dealer for exemption on stock transfers and levy CST on the such inter-state transfers treating the same as inter-state sales, if he is not satisfied about the movement of goods otherwise than by way of sale.

(c) The basic difference between order under Section 6A(1) and 6A(2) is that in case of order under Section 6A(1) the demand is due to non-submission of 'F' Forms, while in case of order under Section 6A(2) the demand is due to levy of CST treating the movement of goods as a result of sale, rejecting the claim of the dealers that movement is otherwise than as a result of sale.

(v) Appellate forum to be approached in case of orders under Section 6A(1) and 6A(2):

(a) Orders passed for non-submission of 'F' Forms – Section 6A(1):

In case the order is passed under Section 6A(1) of the CST Act, rejecting the dealer's claim for stock transfers, for non-submission of the 'F' Forms, then the appeal lies before the next higher forum in the hierarchy of appellate forums. For ex., if the assessment order is passed by the Commercial/Sales Tax Officer/Asst. Commissioner, the appeal lies before the 1st appellate authority, who is generally Dy. Commissioner/Jt. Commissioner/Addl. Commissioner (Appeals) depending upon the designation of the 1st appellate authority. If the 1st appellate authority rejects the appeal, then the dealer has to file 2nd appeal before the 2nd appellate authority which is called Sales Tax Appellate Tribunal/Board or Tax Board etc., which is the highest appellate authority in the State.

(b) The important point to be noted here is that once the assessment order is passed for non-submission of 'F' Forms, denying the claim for stock transfers, the appeal lies before the 1st appellate authority, whether the assessing authority clearly indicates that the order is passed under Section 6A(1) or not.

(c) It is understood there is confusion or mis-conception as to the appellate authority to be approached in case of order under Section 6A (1) or order passed for non-submission of 'F' Forms. It is understood that VAT/Sales Tax authorities in some of the States have also advised the dealers that appeal lies before the highest appellate forum in the State i.e., Sales Tax Appellate Tribunal/Board, in case of orders passed for non-submission of 'F' Forms, citing the provisions of Section 18A of the CST Act.

Relevant provisions of Section 18A of the CST are reproduced hereunder for ready reference:

Appeals to highest appellate authority of State [Section 18A]

(1) Notwithstanding anything contained in a State Act, any person aggrieved by an order made by the assessing authority under sub-section (2) of section 6A, or an order made under the provisions of sub-section (3) of that section, may, notwithstanding anything contained in the general sales tax law of the appropriate State, prefer an appeal to the highest appellate authority of the State against such order.

Provided that any incidental issues including the rate of tax, computation of assessable turnover and penalty may be raised in such appeal.

(2) An appeal under sub-section (1) shall be filed within sixty days from the date on which the order referred to in that sub-section is communicated to the aggrieved person.

Provided that any appeal forwarded by the highest appellate authority of a State to the first appellate authority under the proviso to sub-section (2) of section 25 and pending before such authority immediately before the appointed day shall be transferred, on such appointed day, to the highest appellate authority of the State and the same shall be treated as an appeal filed under sub-section (1) and dealt with accordingly.

Explanation.— For the purposes of this sub-section, "appointed day" means such date as the Central Government may, by notification in the Official Gazette, appoint.

(3) The highest appellate authority of a State may, after giving both the parties an opportunity of being heard, pass appropriate order.

(4) The highest appellate authority of the State may, as far as practicable, hear and decide such appeal within a period of six months from the date of filling of the appeal.

(5) Notwithstanding anything contained in a State Act, the highest appellate authority of a State may, on the application of the appellant and after considering relevant facts, including the deposit of any amount towards local or central sales tax in other States on the same goods, pass an order of stay subject to such terms and conditions as it thinks fit, and such order may, inter alia, indicate the portion of tax as assessed, to be deposited prior to admission of the appeal.

Explanation.— For the purposes of this section and sections 20, 21, 22 and 25 highest appellate authority of a State, with its grammatical variations, means any authority or tribunal or court, except the High Court, established or constituted under the general sales tax law of a State, by whatever name called."

Summary of the above provisions

(i) It is very much clear from the provisions of Section 18 of CST Act that appeals to highest appellate authority of the State shall be preferred in case of orders passed under Section 6A (2) and 6A (3) of the CST Act.

(ii) Orders under Section 6A (2) are required to be passed by the assessing authority after verification of the Form 'F' declaration forms and documentary evidence in support of movement of goods otherwise than as a result of sale submitted by the dealer. Therefore, orders Section 6A (2) cannot be passed, if the declaration forms are not submitted by the dealer. In such a case, orders under Section 6A (1) can be passed.

(iii) Section 6A (3) deals with re-assessments by the assessing authority on discovery of new facts or by a higher authority on the ground that the findings of the assessing authority are contrary to the law. Evidently, Section 6A(3) covers re-assessments but not assessments. Therefore, original assessment orders passed by the assessing authorities are not covered by this Section.

(iv) In effect, Section 18A contemplates appeals to the highest appellate forum in the State in two cases:

   (a) Original assessment orders passed by the assessing authority, wherein CST is charged on the materials moved from one State to another State, rejecting the claim of the assessee towards stock transfer of materials, after verification of the 'F' form declarations and documentary evidence submitted by the dealer in support of movement of goods.

   (b) Re-assessment orders passed by either the assessing authority or any higher authority.

(v) The Section does not cover original assessment orders passed by the assessing authority for non-submission of 'F' forms, which are required to be passed under Section 6A (1) of the CST Act.

(vi) The ambiguity in the matter has been succinctly cleared by the judgment of the Hon'ble Karnataka High Court in the case of Tropican Beverages Vs. State of Karnataka and Others [(2012) 54 VST 472 (Kar)]. It has been held by the Hon'ble High Court that where the assessee could not produce Form 'F' to substantiate the exemption, then the question of conducting inquiry under Section 6A (2) does not arise at all. Consequently, the provisions of the Section 18A (1) of the CST Act do not get attracted in this case. Therefore, the appeal lies before the 1st appellate authority, but not before the highest appellate authority i.e., Appellate Tribunal. Dismissal of the appeals by the 1st appellate authority, on the ground that provisions of Section 18A (1) get attracted in this case and therefore appeal lies before the Karnataka Appellate Tribunal, is held to be invalid. The appellate authority is directed to decide the appeals as per the directions given by the High Court.

Conclusion:

(i) Dealers are advised to file appeals against the assessment orders passed for non-submission of 'F' forms before the 1st appellate authority, but not before the highest appellate forum in the State.

   The assessment order is supposed to mention that the order is passed under Section 6A (1) of the CST Act. Even if the assessment order fails to mention that the order is passed under Section 6A (1) of the CST Act, the dealer is required to prefer appeal before the 1st appellate authority, but not before the highest appellate forum in the State.

(ii) Dealers are advised to file appeals before the highest appellate forum in the State i.e., Sales Tax Appellate Tribunal/ Board or Tax Board, in case the order is passed either under Section 6A(2) or 6A(3) of the CST Act.

   Order under Section 6A (2) relates to rejection of the claim for stock transfers after verifying the genuineness of the transactions. Re-assessment order is passed under Section 6A(3) by the assessing authority on discovery of new facts or by a higher authority on the ground that the findings of the assessing authority are contrary to the law.

Central Sales Tax Appellate Authority [Section 19]

(I) The Central Government shall constitute, by notification in the Official Gazette, an Authority to settle inter- State disputes falling under section 6A read with section 9" of this Act, to be known as "the Central Sales Tax Appellate Authority (hereinafter referred to as the Authority)".

(2) The Authority shall consist of the following Members appointed by the Central Government, namely:-

(a) a Chairman, who is a retired Judge of the Supreme Court, or a retired Chief Justice of a High Court;

(b) an officer of the Indian Legal Service who is, or is qualified to be, an Additional Secretary to the Government of India; and

(c) an officer of a State Government not below the rank of Secretary or an officer of the Central Government not below the rank of Additional Secretary, who is an expert in sales tax matters.

(2A) Notwithstanding anything contained in sub-section (2), the Chairman or a Member holding a post as such in the Authority for Advance Rulings appointed under clause (a) or clause (c), as the case may be, of sub-section (2) of section 245-O of the Income-tax Act, 1961 (43 of 1961) may, in addition to his being the Chairman or a Member of that Authority, be appointed as the Chairman or a Member, as the case may be, of the Authority under this Act.

(3) The salaries and allowances payable to, and the terms and conditions of service of, the Chairman and Members shall be such as may be prescribed.

(4) The Central Government shall provide the Authority with such officers and staff as may be necessary for the efficient exercise of the powers of the Authority under this Act.

Vacancies, etc., not to invalidate proceedings [Section 19A]

No proceeding before the Authority shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the constitution of the Authority.]

Appeals [Section 20]

(1) An appeal shall lie to the Authority against any order passed by the highest appellate authority of a State under this Act determining issues relating to stock transfers or consignments of goods, in so far as they involve a dispute of inter-State nature."

(2) Notwithstanding anything contained in the general sales tax law of a State, the Authority shall adjudicate an appeal filed under sub-section (1).

(3) An appeal under sub-section (1) may be filed within ninety days from the date on which the order referred to in that sub-section is served on any aggrieved person.

Provided that the Authority may entertain any appeal after the expiry of the said period of ninety days, but not later than one hundred and fifty days from the date of such service, if it is satisfied that the appellant was prevented by sufficient cause from filing the appeal in time.

Provided further that the Authority may entertain any appeal from an aggrieved person within sixty days from the commencement of the Central Sales Tax (Amendment) Act, 2005, where such aggrieved person had the right to file an appeal against the order of the highest appellate authority of the State under sub-section (1) as it stood immediately before the commencement of the said Act, but has not availed of the right to file the appeal during the period commencing on and from the 3rd day of December, 2001 and ending with the 16th day of March, 2005.

(4) The application shall be made in quadruplicate and be accompanied by a fee of five thousand rupees.]

Procedure on receipt of application [Section 21]

(1) On receipt of an appeal, the Authority shall cause a copy thereof to be forwarded to the assessing authority concerned as well as to each State Government concerned with the appeal and to call upon them to furnish the relevant records:

Provided that such records shall, as soon as possible, be returned to the "assessing authority or such State Government concerned, as the case may be."

(2) The Authority shall adjudicate and decide upon the appeal filed against an order of the "highest appellate authority".

Explanation. For the purposes of this section and sections 21, 22 and 25 "highest appellate authority of a State" means any authority or tribunal or court (except the High Court) established or constituted under the general sales tax law of a State, by whatever name called.

(3) The Authority, after examining the appeal and the records called for, by order, either allow or reject the appeal.

Provided that no appeal shall be rejected unless an opportunity has been given to the appellant of being heard in person or through a duly authorised representative, and "also to each State Government" concerned with the appeal of being heard.

Provided further that whether an appeal is rejected or accepted, reasons for such rejection or acceptance shall be given in the order.

(4) The Authority shall make an endeavour to pronounce its order in writing within six month of the receipt of the appeal.

(5) A copy of every order made under sub-section (3) shall be sent to the "appellant, assessing authority, respondent and highest appellate authority of the State Government concerned".

Powers of the Authority [Section 22]

(1) The Authority shall have the same powers as are vested in a court under the Code of Civil Procedure, 1908 (5 of 1908) while trying a suit in respect of the following matters, namely:—

(a) enforcing the attendance of any person, examining him on oath or affirmation;

(b) compelling the production of accounts and documents;

(c) issuing commission for the examination of witnesses;

(d) the reception of evidence on affidavits;

(e) any other matter which may be prescribed.

(1A) The Authority may grant stay of the operation of the order of the highest appellate authority against which the appeal is filed before it or order the Pre-deposit of the tax before entertaining the appeal and while granting such stay or making such order for the Pre-deposit of the tax, the Authority shall have regard, if the assessee has made Pre-deposit of the tax under the general sales tax law of the State concerned, to such "Pre-deposit" or pass such appropriate order as it may deem fit.

(1B) The Authority may issue direction for refund of tax collected by a State which has been held by the Authority to be not due to that State, or alternatively, direct that State to transfer the refundable amount to the State to which central sales tax is due on the same transaction:

Provided that the amount of tax directed to be refunded by a State shall not exceed the amount of central sales tax payable by the appellant on the same transaction.

(2) Every proceeding before the Authority shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228 of the Indian Penal Code (45 of 1860) and the Authority shall be deemed to be a civil court for the purposes of section 195 and Chapter XXVI of the Code of Criminal Procedure, 1973 (2 of 1974).

Procedure of Authority [Section 23]

The Authority shall, subject to the provisions of this Chapter, have power to regulate its own procedure "in all matters including stay of recovery of any demand" arising out of the exercise of powers under this Act.

Authority for Advance Rulings to function as Authority under this Act [Section 24]

(1) Notwithstanding anything contained in any other law for the time being in force and in section 19 of this Act, the Authority for Advance Rulings constituted under section 245-O of the Income-tax Act, 1961 (43 of 1961), shall be notified by the Central Government in the Official Gazette, with such modifications as may be necessary, to make its composition in conformity with section 19 of this Act, as the Authority under this Act till such time an Authority is constituted under that section.

(2) On and from the date of the constitution of the Authority in accordance with the provisions of section 19 of this Act, the proceedings pending with the Authority for Advance Rulings shall stand transferred to the Authority constituted under that section from the stage at which such proceedings stood before the date of constitution of the said Authority.

Transfer of pending proceedings [Section 25]

(1) On and from the commencement of the Central Sales Tax (Amendment) Act, 2005, all appeals (except appeals against orders of the highest appellate authority of the State) pending before the Authority notified under subsection of section 24 shall stand transferred together with the records thereof to the highest appellate authority of the concerned State.

(2) Such highest appellate authority of the State to which such appeal has been transferred under sub-section (1) on receipt of such records shall proceed to deal with such appeal so far as may be in the same manner as in the case of an appeal filed before such highest appellate authority of the State according to the general sales tax law of the appropriate State, from the stage which was reached before such transfer or from any earlier stage or de novo as such highest appellate authority of the State may deem fit.

Applicability of order passed [Section 26]

An order passed by the Authority under this Chapter shall be binding on "each state Government concerned, the assessing authorities" and other authorities created by or under any law relating to general sales tax, in force for the time being in any State.

8.3 FORMS UNDER CST

Form A	This form is prescribed for application to get registered u/s 7 of CST Act. Details such as name, status, place of business, warehouses, nature of business, nature and purpose of goods to be dealt, goods to be bought from outside the state etc., are required to be furnished.
Form B	Certificate of registration shall be issued by the authority in this form. The certificate of registration should be kept in the principal place of business an copies thereof in the branches inside the appropriate state
Form C	Registered dealers are entitled to certain exemptions under CST Act, 1956 Form C is used by a purchasing dealer to get the goods at confessional rate of duty and is issued in favour of the dealer who effects interstate sale. It is obtained from the sales tax authorities in the state in which the purchasing dealer is registered. It contains particulars such as name of purchasing dealer, sales tax registration no., its validity, details of goods obtained (whether for resale, manufacture, processing or as packing material), name and address of the seller etc.

Form D	Abolished w.e.f. 1.4.2007
Form EI & E II	In case of subsequent sale in the course of Interstate sale, the dealer effecting subsequent sale can avail exemption by submitting Form C issued by his customer and by submitting Form E-1, issued by his seller. Form, E-I & E-II etc. are printed by the Sales Tax department and are supplied to the registered dealer for their use. Form E-II will have to be issued, in case there are more than one subsequent sale. Thus, it should be noted that Form E-I can be issued by the first seller alone. Form E-II & E-III will have to be submitted by those selling dealer (other than the first dealer) to their purchaser, who can avail of the exemption under section 6(2), subject to the condition that Form C is submitted as well.
Form F	Form by branch / consignment agent for goods received on stock transfer
Form G	Indemnity bond when C form lost
Form H	Certificate of Export
Form I	Certificate by SEZ unit

Study Note - 9

ASSESSMENT OF VARIOUS ENTITIES & TAX PLANNING

This Study Note includes

9.1 ASSESSMENT OF INDIVIDUALS

Tax incidence on Individuals

While computing taxable Income of an Individual following points should be considered.

Nature of Income	Tax Treatment
Income earned by the taxpayer	Except the following all other incomes shall be included (a) Income exempt under sections 10 to 13A (b) Incomes to be included in income of others by virtue of section 60 to 64.
Share of Profit from Hindu Undivided Family	It is exempt under section 10(2)
Share of Profit from a firm assessed as firm	It is exempt under section 10(2A)
Salary and Interest from the aforesaid firm	These are taxable as business Income
Share of profit from an Association of Persons/Body of Individuals	If the association/body is taxable at the maximum marginal rate (or at higher rate), then share of profit is not taxable in hands of recipient.
Income earned by others and included in the income of the taxpayer by virtue of section 60 to 64	Such income shall be included in the income of the taxpayer.

Special Provisions for persons governed by Portuguese Civil Law (Section 5A)

This Section is applicable for the appropriation of income between spouses governed by the Portuguese Civil Code which is in force in the state of Goa and Union territories of Dadra and Nagar Haveli and Daman and Diu. By virtue of this section, income from all other sources, except from salary, should be apportioned equally between husband and wife. The income so apportioned will be included separately in the total income of the husband and of the wife and the remaining provisions of act shall apply accordingly. Salary Income is, however, taxable in the hands of the spouse who has actually earned it.

Even the income from profession will be apportioned equally between the husband and the wife- CIT vs. Datta vs. Gaitonde [2002] 241 ITR 241/108/ taxman 533(Bom).

Taxable income shall be computed as follows :

Step 1- Income under the different heads of income -First find out income under the five heads of income

Step 2- Adjustment of losses of the current year and earlier years- Losses should be set off according to the provisions of sections 70 to 78. The income after adjustment of losses is the gross total income.

Step 3- Deduction from gross total income- Deductions specified under Chapter VI A should be considered while calculating the gross total income.

Step 4- Rounding off- The balance should be rounded off to the nearest ₹ 10. It is called as net income or taxable income or total income.

Tax Liability :

Normal Rates of Income Tax

I. In the case of every Individual (including Non Resident) or Hindu Undivided Family or AOP/BOI (other than a co-operative society) whether incorporated or not, or every Artificial Judicial Person

Upto ₹ 2,50,000	Nil
₹ 2,50,001 to ₹ 5,00,000	10%
₹ 5,00,001 to ₹ 10,00,000	20%
Above ₹ 10,00,000	30%

II. In the case of every individual, being a resident in India, who is of the age of 60 years or more at any time during the Previous Year. [Senior Citizen]

Upto ₹ 3,00,000	Nil
₹ 3,00,001 to ₹ 5,00,000	10%
₹ 5,00,001 to ₹ 10,00,000	20%
Above ₹ 10,00,000	30%

III. In the case of every individual, being a resident in India, who is of the age of 80 years or more at any time during the Previous Year. [Super Senior Citizen]

Upto ₹ 5,00,000	Nil
₹ 5,00,001 to ₹ 10,00,000	20%
Above ₹ 10,00,000	30%

Note : The amount of income tax computed applying the above rates and special rates u/s 111A and 112 shall be increased by a surcharge at the rate of 12% of such income tax incase the total income exceeds ₹1 crore.

'Education Cess' @ 2%, and 'Secondary and Higher Education Cess (SHEC)' @ 1% on income tax shall be chargeable.

Calculation of Tax Liability:

Step 1 – Determine Net Income and tax payable thereon at the slab rate.

Step 2 – Add surcharge @12% incase the total income exceeds ₹1 crore.

Step 3 – Add education cess and secondary and higher secondary education cess

Step 4 – Deduct rebate u/s 86, 87A, 89, 90,90A and 91

Step 5 – Add interest payable (if any)

Step 6 – Deduct amount of prepaid taxes paid (Advance Tax, Tax Deducted at Source, etc.)

The Balance so arrived is the amount of tax to be paid.

Note: (1) From the Assessment Year 2013-14, tax payable (i.e. amount arrived at Step 3) cannot be less than 18.5 percent of "Adjusted Total Income" in some Specified Cases.

(2) The total amount payable as income tax and surcharge on total income exceeding ₹1 crore shall not exceed the total amount payable as income tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹1 crore.

If an individual receives any portion of his salary in arrears or in advance or receives profit in lieu of salary, he can claim relief in terms of section 89 read with rule 21A as under:

Computation of relief when salary has been received in arrears or in advance [Rule 21A(2)]

The relief on salary received in arrears or in advance (hereinafter to be referred as additional salary) is computed in the manner laid down in rule 21A (2) as under:

1. Calculate the tax payable on the total income, including the additional salary, of the relevant Previous Year in which the same is received.
2. Calculate the tax payable on the total income, excluding the additional salary, of the relevant Previous Year in which the additional salary is received.
3. Find out the difference between the tax at (1) and (2).
4. Compute the tax on the total income after including the additional salary in the Previous Year to which such salary relates.
5. Compute the tax on the total income after excluding the additional salary in the Previous Year to which such salary relates.
6. Find out the difference between the tax at (3) and (4).
7. The excess of tax computed at (3) over tax computed at (6) is the amount of relief admissible under section 89. No relief is, however, admissible if tax computed at (3) is less than tax computed at (6). In such a case, the assessee-employee need not apply for relief.

If the additional salary relates to more than one Previous Year, salary would be spread over the Previous Years to which it pertains in the manner explained above.

Special Provisions relating to non-residents [Section 115C to 115-I]

The benefit of special provisions can be claimed by non-resident Indians. The following are non-resident Indians for the purpose:

a. citizen of India who is a non-resident ;
b. a person of Indian origin who is a non-residen

A person shall be deemed to be of Indian origin if he or either of his parents or any of his grandparents, was born in an undivided India.

The Provisions of Section 115C to 115-I are applicable only in respect of the following incomes derived by a non resident Indian:

a. Investment income derived from a "foreign exchange assets"; and
b. Long Term Capital Gains on sale or transfer of "foreign exchange assets".

Foreign Exchange Asset - It means those "specified asset" which the assessee has acquired or purchased with, or subscribed to in, convertible foreign exchange;

The following are the "specified assets":

a. shares in an Indian Company (public or private)

b. debentures issued by an Indian Company which is not a Private Company ;

c. deposits with an Indian Company which is not a Private Company, it may be even deposit with SBI or any other Banking Company;

d. any security of the Central Government ; and

e. such other asset as the Central Government may specify in this behalf by notification in the Official Gazette.

Investment Income

In computing the Investment income of a non-resident Indian, no deduction in respect of any expenditure or allowance shall be allowed under any provision of the Act. Moreover, no deduction under Sections 80C to 80U shall be allowed in respect of investment income of non–resident Indians.

Long Term Capital Gain

Long Term Capital Gain on sale or transfer of foreign exchange assets shall be calculated subject to:

1. The benefit of Indexation is not available for the sale or transfer of foreign exchange assets.
2. The non-resident Indian can claim exemption under section 115F by investing sale consideration in another asset.
3. No deduction is permissible under section 80C to 80U in respect of Long Term Capital Gain.

Tax treatment on Investment and Long Term Capital Gain:

Non-resident Indians are chargeable to tax on investment and Long Term Capital Gain at the rate of 20 percent and 10 percent respectively. (plus surcharge, education cess and secondary and higher secondary education cess)

General Provisions —

Rate of Tax — Similar to resident assessees.

Special rates of tax on Dividends, interest income from units of Mutual Fund and UTI, bonds or shares purchased in foreign currency and Capital Gains arising from their transfer :

- 20% of the dividends [which have not been subjected to additional Income Tax u/s 115-O] [other than dividends mentioned in clause (iv)];
- 5% of interest received from an infrastructure debt fund referred to in Section 10(47) or interest of the nature and extent referred to in Section 194LC/194LD;
- 20% of the interest received from Government or an Indian concern on monies borrowed or debt incurred in foreign currency;
- 20% of the income received in respect of units purchased in foreign currency, of a Mutual Fund specified u/s 10(23D) or of the Unit Trust India;
- 10% of the interest or dividends [which have not been subjected to additional income tax u./s 115-O], in respect of bonds or Global Depository Receipts in an Indian company purchased in foreign currency and issued under the Foreign Currency Convertible Bonds and Ordinary shares (Through Depository Receipt Mechanism) Scheme, 1993 (commonly known as Euro Issues/Euro Bonds) or in respect of bonds or Global Depository Receipts issued against shares of a public sector company sold by the Government to the non-resident in foreign currency; and
- 10% of the income by way of royalty or fees for technical services, if any, included in the total income;
- 10% of the Long-term Capital Gains arising from the transfer of the aforesaid bonds or Global Depository receipts.

Filing of return — Similar to resident assessees :

However, a non-resident shall not be required to file a return of income u/s 139(1), if his total income consists only of income subject to special rates of tax as mentioned in rate of tax under clauses (iv) supra and the tax has been deducted there from at source.

Return of Income not to be filled in certain cases:

Where a non-resident Indian has income only from a foreign exchange asset or income by way of Long Term Capital Gains arising on transfer of a foreign exchange asset, or both, and tax deductible at source from such income has been deducted, he is not required to file the return of income under section 139(1).

The income from foreign exchange assets and Long Term Capital Gains arising on transfer of such assets would be treated as separate block and charged to tax at a flat rate as explained above.

If the non-resident Indian has other Income in India, such other income is treated as an altogether separate block and charged to tax in accordance with other provisions of the Act.

Benefit available even after the assessee becomes resident – These provisions are as follows:

1. A non-resident Indian in any Previous Year becomes assessable as resident in India in any subsequent year.
2. He may furnish to the Assessing Officer a declaration in writing(along with his return of income under section 139 for the Assessment Year for which he is so assessable)to the effect that the special provisions shall continue to apply to him in relation to the investment income derived from any foreign exchange asset.
3. The foreign exchange assets for this purpose are debentures and deposit with an Indian public limited company and Central Government securities.

The special provisions shall continue to apply for that Assessment Year and for every subsequent Assessment Year till the transfer or conversion (otherwise than by transfer) into money of such assets.

Special Provisions not to apply if the assessee so chooses (Section 115-I)

A non-resident Indian may opt that the special provisions should not apply to him by making a declaration to that effect in his return of income for the relevant Assessment Year. In such case the whole of his Income (including income from foreign exchange assets and Long Term Capital Gains arising on transfer of a foreign exchange asset) is chargeable to tax under the general provisions of the Act.

Conversion of Proprietorship into Partnership

The first step that is usually taken by a proprietor sooner or later is to take the other members of the family as partners. Under the present scheme of taxation of firms, reasonable return for capital and salary for working partners can be deducted from the firm's profits, the balance being taxed at maximum marginal rate. In case of most big firms, the new system has given a significant advantage when compared to the earlier system of double taxation, once by way of firm's tax on firms and again on respective shares in the hands of partners. Such partnership can help to create wealth for the members of the family. Admission of minor children to the benefits of partnership would also help to ensure that the wealth of such minor children grows fast so that when they attain majority, they are assessable in their own hands. Where the parent is liable at maximum marginal rate at top slab, the fact that the minor's share would suffer maximum rate need not discourage such admission of minors. Prior to A.Y. 1993-94, it was possible for the Assessing Officer not to recognise a firm, where other members of the family do not bring in capital or skill in circumstances, where one suspects non-genuineness, a ground on which registration could be refused on the ground that such firms are not genuine. In that case, such firm may be treated as Association of Persons (AOP) with the consequential disallowance of salary and interest to partners. From A.Y.1993-94 onwards a firm is taxed as an entity with deductions permissible for salary and interest subject to certain limits while an AOP or BOI do not get this benefit.

Incoming partners have necessarily to justify their inclusion as a partner. Where they do not pay for their share of goodwill, there should be some justification for it. It is better that in such cases goodwill is evaluated and the individual (or existing partners) is/are credited prior to induction so that inference of lack of consideration cannot be lightly made. If the intention is to avoid the contingency of charging for goodwill, it is possible to have a clause in the partnership deed that the goodwill will always belong to the founders, and that, no retiring partner or the legal heirs of the deceased partner other than the founder partners would be entitled to a share of such goodwill. Similarly, real estate, if any, belonging to the individual but treated as that of the firm, would require to be brought in at market rate. If it is brought into the firm's books at book value, which very often is either the cost or the written down value after depreciation, the share of difference between the book value and the market value is lacking in consideration and was treated as deemed gift when gift tax was in vogue.

The Supreme Court's decision in the case of CGT vs. Chhotalal Mohanlal (1987) 166 ITR 124 (SC) should serve as a warning in this regard, though, in the facts of that case, the benefit of the reduction in share of the father went to the minor children, a situation, where lack of consideration can be more easily presumed. There are a number of High Court decisions where such attempt on the part of the Assessing Officers to presume gift have failed for one reason or the other. It is possible to resist the presumption of gift on the ground that partnership being a contract, there can be no inference of gift, a plea which is rather weak in the light of the Supreme Court decision or it can be argued that the incoming partners have brought in other intangible advantages for the business, which cannot be measured by what is given up by the individual. In CGT vs. Smt. Lalita B. Shah (1979) 118 ITR 794 (Bom.); CGT vs. Nagji Dulabhji (1979) 118 ITR 804 (Bom.); CGT vs. Shravenkumar P.Patel (1987) 167 ITR 496 (MP); CGT vs. Sardar Wazir Singh(1975) 99 ITR 104 (All.); and Addl. CGT vs. A. A. Annamalai Nadar (1978) 113 ITR 574 (Mad.) courts have taken a more liberal view on the ground that the promise of service or the agreement to share loss made up for any immediate benefit, which might otherwise be discernible. However, gift was inferred in a number of cases, as for example in N. K. Krishna Iyer Sreeman Motors vs. CGT (1973) 89 ITR 228 (Ker.); CGT vs. A. M. Abdul Rahman Rowther (1973) 89 ITR 219 (Mad); CGT vs. Smt. Rukrnani [Amma (1973) 87 ITR 549(Mad.) and CGT vs. Ganapathy Moothan (1972) 84 ITR 758 (Ker.).

No doubt, Supreme Court in *CGT* vs. *P. Gheevarghese Travancore Timbers & Products Kottayam* (1972) 83 ITR 403 (SC) chose not to infer gift in conversion of proprietary business into partnership; but it was not because there was no element of gift but only because the Assessing Officer had picked out goodwill as one of the assets of the proprietary business as the subject matter of the gift. It was pointed out that such an approach is "wholly incomprehensible" and that, therefore, the levy of gift-tax was illegal. On the other hand, if the Assessing Officer had evaluated the net asset value of the business, the issue would have still been open. In other words, the objection was more to the mode of computation of gift than on the principle as to whether there could be a gift at all in a contract of partnership. Relevance of such law after deletion of gift tax is to avoid inference of lack of genuineness on grounds of lack of consideration.

Where proprietary business becomes family partnership, there may be a tendency to regard the whole exercise as a mere tax routine. It cannot really be so. Partnership confers certain legal rights to the partners. A partnership deed in writing is necessary. If salary and interest are provided for and intended to be claimed as a deduction, such deed should be available even at the beginning of the accounting year. There is still the need for establishing that each partner is a genuine partner even under the new scheme of taxation of firms. A firm which is not genuine is not a firm at all. In order that a firm may be genuine, the partners must be real partners and not benamidars of someone else, whether of any other partner or outsider. It is quite likely that a son may be treated as benamidar of father, if he neither brought in capital nor is he able to participate in the firm and contribute his skill and labour. A more liberal view is, however, that even agreement to share loss, relieves the proprietor of his pressure and may be enough consideration. If the son has no asset of his own, his agreement to share the loss would have no meaning. It is, therefore, necessary that the admission of a partner, though a family member, is capable of being supported by objective considerations, though not in the strictest sense that there must be a quid pro quo as would be normal in the case of transactions with strangers.

The risk in the firm being found non-genuine is that it cannot be treated as a firm even if all the formalities are fulfilled. If it is not treated as a firm, deduction of interest and salary to partners will not be permissible. As an Association of Persons (AOP), it may be taxed at the maximum rate if the shares are not specified or if any one of the members has taxable income. Where the firm is not considered genuine, the maximum rate will be automatically applied as it will be treated as an AOP.

It may be taken note of that the Supreme Court in *ITO* vs. *Ch. Atchaiah* (1996) 218 ITR 239 (SC) has ruled that an AOP has only to be assessed directly as an AOP and there is no option either for revenue or taxpayer to have any option for assessment of each member on his respective share.

Where the proprietary business is converted into partnership, the advantage lies in not having to register the immovable property, even if such immovable property has to be treated as that of the firm. It is well-established that no registered instrument of transfer is required when a partner brings his asset as capital contribution. In most cases where the property is used for business, depreciation will be admissible and will lighten the burden of the firm especially since any deduction for depreciation will have the effect of reducing the tax at maximum rate. The fact that partner's capital account will be enlarged by the value of the asset so brought in will entitle him to larger interest deductible under section 40(b) and thereby reducing the incidence of maximum rate still further. It is, therefore, necessary that there should be enough documentation to suggest that the property belongs to the firm and does not continue to be that of the erstwhile proprietor. This is best done by mentioning the fact of the property being brought in by the individual partner as his capital contribution in the preamble to the partnership deed itself with the narration that the value of the property will form a part of his capital contribution. The asset must be taken in the accounts of the firm and shown as an asset in the Balance Sheet of the firm. It is also possible for a firm to purchase an asset from a partner. But in such a case registration would be necessary. However, the comments in this paragraph that no registration is required is subject to revision dependent on the State stamp law. In some States like Maharashtra, registration in such cases is now made mandatory.

The liability for capital gains for the partner who contributes the assets by way of his capital, is a matter which requires consideration. Section 45(3) would deem such pooling of the asset as deemed transfer for the purpose of capital gains tax. But then the value is not a matter on which the Assessing Officer can have any say, because the statute provides that the price to be reckoned for such deemed sale is "the amount recorded in the books of account of the firm". This gives an option to the erstwhile proprietor either to pay capital gains tax by placing a larger value and getting depreciation for firm on such enhanced amount or to avoid capital gains tax altogether and face lesser depreciation. After deletion of gift tax, the possibility of deemed gift in case of under-valuation is now absent.

It is possible to avoid capital gains tax altogether in respect of any real property by retaining ownership, but leasing it out to the firm. It is quite possible that such lease income, though ordinarily assessable as income from other sources, can take into consideration eligibility for depreciation which has been hitherto enjoyed. While in respect of machinery and plant, there is no ambiguity about depreciation, some problems might arise about buildings, when leased without plant and machinery, but used for business purposes. Care, however, should be taken to have the lease rent fixed in such a manner that it will not only be able to absorb the depreciation but will also be capable of being justified with reference to any objective criteria as a reasonable compensation for the assets made available to the firm. It is because one has to steer clear of section 40A(2), which would rule out any excessive or unreasonable amount payable to any interested person. There is a view that section 40A(2) can have no application, when payment is made to a partner, a view for which there is no precedent. On the other hand, section 40A(2) *prima facie* would have application, since it specifically lists a partner of a firm as a related person under section 40A(2)(iii) of the Act. With the application of transfer pricing rules for transactions under section 40A(2), pricing may become material.

While there are special provisions exempting liability from capital gains tax on conversion of proprietary business and firm's business as that of a company, there is no provision exempting conversion of proprietary business into firm's business. In such a case, where there is conversion of proprietary business to firm's business and the business is transferred to the firm by the proprietor as a going concern contributed as his capital, the assets of the proprietary business will become the assets of the firm under section 14 of the Partnership Act even if such business had immovable property without the need for registration and therefore not incurring liability for stamp duty. But section 45(3) treats such transfer as a taxable transfer on the value credited to the partner, which will be taken as the sale consideration. If, however, the sale is a severable one and not contributed as capital, the erstwhile proprietor will be assessable for capital gains on sale of the asset transferred with the assessee having to pay stamp duty, if the transfer is of immovable property and also losing the sales-tax concession in respect of taxable items.

There is exemption from capital gains tax on sale of proprietary business to a company subject to conditions under section 47(xiv) of the Act. If the transfer takes place by way of conversion of firm into company by registering the firm as company, there is no liability even otherwise since it does not constitute transfer as was decided in *CIT* vs. *Texspin Engineering and Manufacturing Works* (2003) 263 ITR 345 (Born.). Incentives enjoyed by the firm under Chapter VI-A prior to such conversion can be continued to be enjoyed by the company for the remaining eligible period as was decided by the Tribunal in *Chetak Enterprises (P) Ltd.* vs. *Asst. CIT* (2006) 281 ITR (AT) 162 (Jodh).

The view that capital gains tax is attracted in view of section 45(3) is supported by the decision of the Tribunal in *Dharamshibhai B. Shah* vs. *ITO/GTO* (2010) 1 ITR (Trib) 536 (Ahrn).

Conversion to Company

The other choice for the proprietor in reorganising his business for expansion is to convert the proprietary business to that of a company. It is very unfortunate that prior to A.Y.1999-2000, the general law or the tax laws were indifferent to the need for easier conversion in such cases in the larger interest of economy. Company being a separate legal entity, any transaction as between the firm and the company could have been treated as a transaction between two different persons even if the company happened to be what is loosely described as one-man company. The myth follows the English decision in *Salomon* vs. *Salomon & Co* (1897) AC 22 but the corporate veil is pierced for so many purposes to secure the interest of those dealing with companies including revenue. Such piercing of the veil is not permissible for the advantage of the individual or the company. In other words, the corporate existence is ignored for the purpose of revenue's benefit and not for the taxpayer, a veritable one-way street. It is for this reason that the cost of conversion should involve considerable tax as part of its cost.

Section 47 contains provisions relating to transactions which are not regarded as transfer for purposes of capital gains tax. Sub-section (xiv) of section 47 prescribes conditions in its proviso for granting exemption from capital gains on conversion of sole-proprietary concern to a company. Section 47(xiv) reads as under:

"*47(xiv)*. Where a sole proprietary concern is succeeded by a company in the business carried on by it as a result of which the sole proprietary concern sells or otherwise transfers any capital asset or intangible asset to the company:

Provided that-

(a) all the assets and liabilities of the sole proprietary concern relating to the business immediately before the succession become the assets and liabilities of the company.

(b) the shareholding of the sole proprietor in the company is not less than fifty per cent of the total voting power in the company and his shareholding continues to remain as such for a period of five years from the date of the succession; and

(c) the sole proprietor does not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company."

Immovable properties belonging to the individual can be transferred to a company only by a registered sale deed. Where business as a whole is taken over, registration is sometimes avoided for the time being, but such agreements usually provide for the contingency of registration in case it is so desired by the company. This is done so as to enable selective registration of the assets where it is so required. In case of immovable property, audit is bound to qualify the Balance Sheet in the absence of a registered document. The lending institutions would not treat the asset as that of the company with the result that it is not easy for the company to mobilise resources for its business without formal transfer of proprietary assets. If the asset has to be shown in the Balance Sheet without audit qualification, the cost of registration cannot be avoided. The consequent levy of capital gains tax could not have been avoided before the introduction of section 47(xiii) and 47(xiv). The burden of capital gains tax would have been higher in case of depreciable assets since the surplus over the written down value would be liable to tax as short-term capital gains under section 50 of the Act. Any attempt to lessen such liability by under-valuation of the asset does not now invite gift-tax, after its deletion, but there is no point in understating the value of an asset for the company in which the individual may not be the sole person interested in the company. It is in this context that the cost of conversion from individual to company may be found to be higher, where stamp duty is taken into consideration. At any rate, a larger levy of stamp duty is certain, amendment of Income-tax Act also is of no help in all cases.

There is also an additional point to be considered in such conversion. The individual even assuming has other income which takes him to maximum slab rate may be paying at a flat rate of 30% from A Y 1997-98 (with surcharge at 10% on tax). There is an element of double taxation in the case of a company, since its profit is taxed directly and again on distributed dividend. In contrast, a partner can withdraw his profit without any tax cost.

Mitigation of tax effect

Provision of salary

The only advantage which the individual may take is to ensure that he draws enough salary which can be allowed as a deduction from the company's income. This will avoid corporate tax; and the salary income would suffer the normal rate of tax in his hands. Care has to be taken to see that the salary received not only conforms to the ceiling under the company law which is now liberal, but also to be so designed to avoid resort by the Assessing Officer to section 40A(2), which enables him to disallow what he considers to be excessive or unreasonable. Transfer pricing rules are also made applicable from A.Y. 2013-2014.

Provision of interest

It is not ordinarily necessary that the entire capital employed by the erstwhile proprietor or partners should be treated as share capital of the company, if formed, since part of which may be by way of share capital and the remaining part treated as loan capital. Structuring of the capital of the company would have depended upon its requirement. Where part of the amount is treated as loan capital, interest could be charged. But if exemption is required, entire consideration has to be by way of share capital, since debentures are excluded for availing the benefit of exemption under section 47(xiv) of the Act. Preference shares not redeemable for five years (because of the requirement of retention for five years) should be permissible. As between the choice to convert the proprietary business to that of the firm or company, it would appear that formation of firm is less expensive and involves lesser formality. The question of stamp duty does not arise at all is most States, where the conversion is to the firm.

Business considerations may prompt conversion of individual business to a company with minimum effort rather than converting it into a firm and later on finding it necessary to convert it to a company. Tax cost in such changes on two occasions may be found to be even higher than otherwise. With escalation in prices, a direct takeover by the company now may be preferable to postponing it to a later date. The above comments have however been made with reference to the law as it stood prior to 1999 as well as post 1999.

Other options before the proprietor

It is true, that there is an option of registering the firm as a company so that it may be possible to consider the alternative of forming a firm with a view to register it as company. This is also an option which has to be considered in the light of what has been stated in the matter of conversion of firm into company.

9.2 ASSESSMENT OF HINDU UNDIVIDED FAMILY

U/s 4 of the Income Tax Act, 1961, Income-tax is payable by 'every person'. 'Person' includes a 'Hindu Undivided Family' as defined in sec. 2(31). The definition of 'Hindu Undivided Family' is not found in the Income-tax Act. Therefore the expression 'Hindu Undivided Family' must be construed in the sense in which it is understood under the 'Hindu Law' [Surjit Lal Chhabda vs. CIT 101 ITR 776(SC)].

According to Hindu Law, 'Hindu Undivided Family' is a family which consists of all persons lineally descended from a common ancestor and includes their wives and unmarried daughters. A 'Hindu Undivided Family' is neither the creation of law nor of a contract but arises from status.

A Hindu coparcenary includes those persons who acquire by birth an interest in joint family property. Only a male member of a family can be a coparcener while the membership of a HUF consists of both males and females. All the coparceners of the family constitute what is called a 'Coparcenery'. All the coparceners are members of a HUF but all members of a HUF are not coparceners. A coparcener of a joint family, who acquires by birth an interest in the joint property of the family, whether inherited or otherwise acquired by the family, may have a right to enforce partition whereas the members of the family who are not coparcenars have no right to enforce partition. When a partition takes place, member (mother or widow) of the joint family may get a share equal to the sons and also it is necessary to provide for maintenance and marriage of the unmarried daughter out of family property.

There are two schools of Hindu Law- (1) Mitakshara and (2) Dayabhaga. Under the Mitakshara school, each son acquires by birth an equal interest with his father in the ancestral property. Under the Dayabhaga School which prevails in West Bengal and Assam, a son does not acquire by birth in ancestral property. He acquires interest only on the death of his father. Father enjoys an absolute right to dispose of the property of the family according to his desire. After the death of father, his son does not, by operation of law, become members of the joint family. The sons remain as co-owners with definite shares in the properties left by father unless they decide to live as a joint family.

Case Laws:

(i) A single person, male or female, cannot constitute a Hindu Undivided Family. An individual, who has obtained a share on partition of a joint family, has potentialities of creating a joint family; but until he marries, he alone cannot be considered as a joint family [C. Krishna Prasad vs. CIT97 ITR 493].

(ii) A joint family may consist of a single male member with his wife and daughter(s) and it is not necessary that there should be two male members to constitute a joint family [Gowli Buddanna vs. CIT 60 ITR 193].

Jain & Sikh families are not governed by Hindu Law. However, for the purpose of Income tax Act, such families are treated as 'Hindu Undivided Families'.

The income of a joint Hindu family may be assessed in the status of HUF if the following conditions are satisfied:-

(i) There should be a coparcenership

(ii) There should be a joint family property which consists of ancestral property, property acquired with the aid of ancestral property and property transferred by its members. It may be pointed out that once a joint family income is assessed as that of Hindu Undivided Family, it will continue to be assessed as such in future years till partition is claimed by its coparceners.

Under the Hindu Law, ancestral property is the property which a person inherits from any of these three immediate male ancestors, i.e. his father, grandfather and great grandfather. Income of ancestral property is taxable as income of HUF in the following cases:

(i) family of husband and wife without any children;

(ii) family of two widows of deceased brothers;

(iii) family of two or more brothers;

(iv) family of uncle and nephew;

(v) family of mother, son and son's wife;

(vi) family of a person and his late brother's wife;

(vii) family of widow mother and her sons.

It will be seen that the substantive provision of old section 6 reiterates the position prevailing under the then existing Hindu Law that on the death of a Hindu male coparcener of HUF his interest in the HUF shall devolve upon the surviving coparceners of the family. This ensures that succession by survivorship continues to be the law in so far as succession to coparcenary interest in HUF property of a Hindu male is concerned but, having restated and reiterated this important concept of Hindu law in so far as succession is concerned, the Hindu Succession Act, 1956 goes on to severely circumscribe its applicability by the proviso which immediately follows the sub-section.

Where the property of the father is inherited by his son then, as per Section 8 of the Hindu Succession Act, the income from such house property shall be assessed in his individual capacity and not as Karta of the HUF. [Dr. H. N. Mehrotra vs. CIT (2005) 276 ITR 158 (All.)]

According to the proviso to section 6 the succession by survivorship provided in the substantive part of the section will not be applicable where a deceased Hindu male, who is a member of an HUF, leaves behind him any female heirs of Class I or male heirs in that class through such female. In that case, his interest in the HUF coparcenary will devolve upon these heirs by succession, either intestate or by testament and not by survivorship to the remaining coparceners of the HUF.

The following are female heirs of a Hindu male specified in Class I of the Schedule:-

(i) Widow;

(ii) Daughter;

(iii) Mother;

(iv) Widow of a predeceased son;

(v) Daughter of a predeceased son;

(vi) Daughter of a predeceased daughter;

(vii) Daughter of a predeceased son of a predeceased son;

(viii) Widow of a predeceased son of a predeceased son.

The only male heir specified in Class I of the Schedule is the son of a predeceased daughter.

There are thus nine categories of heirs mentioned in Class I of the Schedule, eight females and one male, being the son of a predeceased daughter.

Thus where proviso to Section 6 applies and interest of a deceased coparcener is to devolve by intestate succession, what is meant is that the share in the coparcenary property which would have been allotted to him on a partition taking place before his death would devolve on his heirs. The concept of notional partition is brought in for defining the nature and quality of the interest which devolves the succession. The quantum of share is fixed, the proportion in which the share is to be computed is also crystallized. This specific share is definite ascertained properties devolves on the heirs by intestate succession. But that does not affect the continuance of the HUF.

Assessments will continue to be framed on the HUF as the death of a coparcener does not dissolve or disrupt the HUF. It continues in the same manner as before but with one coparcener less. There is, however, a change in the assets owned by the family is on so far as the interest of the deceased coparcener in the HUF will now pass on to his successors – sons, widow, daughters, etc. Before the passing of the Hindu Succession Act, in 1956, there would have been no change in the property or assets of the HUF on the death of a coparcener as his interest in HUF would have passed on to other coparceners by survivorship and consequently remained with the HUF.

Due to amendment brought in the Hindu Succession Act, 1956 by the Hindu Succession (Amendment) Act, 2005, the daughters have been given following rights under section 6.

(1) The daughter of a coparcener shall by birth become a coparcener in her own right in the same manner as the son

(2) The daughter has the same rights in the coparcenary property as she would have had in the same manner as the son

(3) The daughter shall be subject to the same liability in the said coparcenary property as that of a son; and any reference to a Hindu Mitakshara coparceners shall be deemed to include a reference to a daughter of a coparcener

(4) The daughter is allotted the same share as is allotted to a son.

(5) The share of the pre-deceased son or a pre-deceased daughter shall be allotted to the surviving child of such pre-deceased son or of such predeceased daughter.

(6) The share of the pre-deceased child of a pre-deceased son or of a pre-deceased daughter shall be allotted to the child of such pre-deceased child of the pre-deceased son or a pre-deceased daughter.

Further, after the commencement of the Hindu Succession (Amendment) Act, 2005, no court shall recognize any right to proceed against a son, grandson or great-grandson for the recovery of any debt due from his father, grandfather or great- grandfather solely on the ground of the pious obligation under the Hindu law, of such son, grandson or great-grandson to discharge any such debt.

Except the above change relating to daughter being a coparcener, assessments will continue to be framed on the HUF as the death of a coparcener does not dissolve or disrupt the HUF. The interest of the coparcener is determined by assuming a national partition of HUF immediately before his death. The heirs of the deceased coparcener would hold their share of the property as tenants-in-common with the HUF.

While section 6 of the Hindu Succession Act deals with the succession to interest in coparcenary property where a Hindu male who is a coparcener of a HUF dies, section 8 governs succession to his separate and self-acquired property if he dies intestate. It provides that the self-acquired and separate property will devolve upon his heirs in the following order:

(1) Firstly, on the relations specified in Class I of the Schedule

(2) Secondly, if there are no relatives in Class I, then upon the relatives specified in Class II of the Schedule

(3) Thirdly, if there are no heirs of either Class I or Class II, then upon the agnates of the deceased

(4) Lastly, if there are no agnates, then upon the cognates of the deceased.

Agnates of the deceased are relatives from the paternal side. A person is said to be an agnate of another if the two are related by blood or adoption wholly through the males.

Cognates of the deceased are relatives through maternal side. A person is said to be cognate of the deceased if the two are related by blood and adoption not wholly through the males.

While computing income of a Hindu Undivided Family one should give due consideration of the following:

(i) Where a member of HUF converts his self acquired property into joint family, income from such property shall not be treated as income of HUF u/s 64(2). It shall continue to be taxed in the hands of the transferor who is the member of the HUF.

(ii) Income from an impartible estate is taxable in the hands of the holder of the estate and not in the hands of HUF.

(iii) Income from Stridhan of a woman is not taxable in the hands of HUF.

(iv) Personal income of members cannot be treated as income of HUF.

(v) Where the funds of HUF are invested in a company or a firm, fees or remuneration received by the member as a director or a partner in the company or a firm may be treated as income of HUF in case the fees and remuneration is earned essentially as a result of investment funds.

(vi) Where remuneration is paid by HUF to Karta or any other member for services rendered by him in conducting family's business, the remuneration is deductible provided the remuneration is paid :

    (a) under a valid bonafide agreement;

    (b) in the interest of, and expedient for the family business, and

    (c) genuine and not unreasonable.

Case law:

Remuneration and commission received by the Karta of HUF on account of his personal qualifications and exertions and not on account of investments of the family funds in the company cannot be treated as income of HUF [Subbiah Pillai (K.S.) vs. CIT 103 Taxman 400/237 ITR 11].

Taxable income shall be computed as follows :

Step 1 - Income under the different heads of income - First find out income under the five heads of income

Step 2 - Adjustment of losses of the current year and earlier years - Losses should be set off according to the provisions of sections 70 to 78. The income after adjustment of losses is the gross total income.

Step 3 - Deduction from gross total income - Deductions specified under Chapter VI A should be considered while calculating the gross total income.

Step 4 - Rounding off - The balance should be rounded off to the nearest ₹ 10. It is called as net income or taxable income or total income.

Calculation of Tax Liability:

Step 1 – Determine Net Income and tax payable thereon at the slab rate.

Step 2 – Add surcharge @ 12% if the total income exceeds ₹1 crore.

Step 3 – Add education cess and secondary and higher secondary education cess

Step 4 – Deduct rebate u/s 86, 90,90A and 91

Step 5 – Add interest payable (if any)

Step 6 – Deduct amount of prepaid taxes paid (Advance Tax, Tax Deducted at Source, etc.)

The Balance so arrived is the amount of tax to be paid.

Note: (i) From the Assessment Year 2013-14, tax payable (i.e. amount arrived at Step 3) cannot be less than 18.5 percent of "Adjusted Total Income" in some Specified Cases.

(ii) The total amount payable as income tax and surcharge on total income exceeding ₹1 crore shall not exceed the total amount payable as income tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹1 crore.

PARTITION OF HUF

'Partition' may be a (i) total or complete partition (ii) partial partition.

Where all the properties of the family are divided amongst all the members of the family, and the family ceases to exist as an undivided family, it is known as total or complete partition.

On the other hand, where one or more coparceners of the HUF may separate from others and the remaining coparceners may continue to be joint or some of the properties are divided and the balance remain joint it is known as partial partition.

Partition can only be claimed by a coparcener. But, when there is a partition of HUF the following persons are entitled to a share in the assets of the HUF:

(1) All coparceners.

(2) Mother is entitled to a share equal to the share of a son in case of death of the father.

(3) Wife gets a share equal to that of a son if a partition takes place between her husband and his sons. She enjoys this share separately even from her husband.

(4) A son in the womb of the mother at the time of the partition.

On a partition between the members of a joint family, the shares are allotted as under:-

(1) On a partition in a HUF which includes father, mother and sons, mother has no right to claim partition but when a partition is actually affected, she takes a share equal to the sons.

(2) On a partition between a father and his sons where mother is not living, each son takes a share equal to that of the father. Suppose there are four sons, each son of that father will take $1/5^{th}$ share of the property.

(3) If a joint family consists of brothers, they take equal shares on a partition.

(4) Each branch takes per stripe as regards every other branch, but members of each branch take per capita as regards each other.

(5) None of the unmarried daughters have a right to share on the partition but the partition should provide for their maintenance and education till marriage and for their marriage expenses. However, w.e.f. 9.9.2005, the daughter whether married on unmarried shall also be entitled to equal share on partition as she has also been treated as coparcener like son.

Procedure to effect partition and consequences after partition are as follows:

(1) A Hindu family hitherto assessed as undivided shall be deemed for the purposes of this Act to continue to be a Hindu Undivided Family, except where and in so far as the partition has been recognized by the Assessing officer under this section.

(2) Where, at the time of making an assessment under section 143 or section 144, it is claimed by or on behalf of any member of a Hindu Undivided Family assessed as undivided that a total partition has taken place among the members of such family, the Assessing Officer shall make an inquiry there into after giving notice of such inquiry to all the members of the family.

(3) On the completion of the inquiry, the Assessing Officer shall record a finding as to whether there has been total partition of the joint family property, and, if there has been such a partition, the date on which it has taken place.

(4) Order u/s 171 passed by the Assessing officer after issuing a call memo only to Karta of the HUF and not other members of the family did not comply with the mandatory requirement of Section 17(2), and therefore, illegal and not valid. Matter remanded back to the Assessing Officer with the direction to pass an order under section 171 after notifying all the members of the HUF and hearing them. [P.G. Srinivasetty & Sons (HUF) vs. ITO (2010) 41 DTR 283 (Kar.)]

(5) Where a finding of total partition has been recorded by the Assessing Officer under this section, and the partition took place during the previous year the total income of the joint family in respect of the period upto the date of partition shall be assessed as if so far no partition had taken place; and each member or group of members shall, in addition to any tax for which he or it may be separately liable and notwithstanding anything contained in Clause (2) of section 10, be jointly and severally liable for the tax on the income so assessed.

(6) Where the finding of total partition has been recorded by the Assessing officer under the section, and the partition took place after the expiry of the previous year, the total income of the previous year of the joint family shall be assessed as if no partition had taken place; and each member or the group of members shall be jointly and severally liable for the tax on the income so assessed.

(7) Notwithstanding anything contained in this section, if the Assessing Officer finds after completion of the assessment of a Hindu Undivided Family, that the family has already affected a partition, and every such person shall be jointly and severally liable for the tax on the income so assessed.

(8) For the purposes of this section, the several liability of any member or group of members thereunder shall be computed according to the partition of the joint family property allotted to him or it at the partition, whether total or partial.

(9) The provisions of this section shall, so far as may be, apply in relation to the levy and collection of any penalty, interest, fine or other sum in respect of any period upto the date of the partition, whether total or partial, of a Hindu Undivided Family as they apply in relation to the levy and collection of tax in respect of any such period.

The most important point to be noted for recognition of a partition in joint family which has been hitherto assessed is the condition that there should be a partition by metes and bounds. There should be a physical division of the property under the income-tax or wealth tax laws, although Hindu law recognizes partition by mere severance of status without a physical division. Though physical division by metes and bounds is mandatory, but if the property is not capable of physical division, an exception is possible. [Joint Family of Udayan Chinuttai vs. CIT (1967) 63 ITR 416]. But merely because property of the family consists of immoveable properties there need be no inference that they are indivisible. [Kalloomal Tapeswri Prasad (HUF) vs. CIT (1982) 133 ITR 690 (SC)].

A complete partition with unequal shares as may be agreed between the parties is not illegal and can be final. However, an unequal partition between karta as the sole adult member and the minor children may be challenged at the instance of the minor children on attaining majority of having a partition reopened by the Court. Such a reopening however, will not only be permitted if the division is unjust and unfair.

The Supreme Court in the case of Kapurchand Shrimal vs. CIT (1981) 131 ITR 451 (SC) held that the Assessing Officer cannot continue to make assessment on HUF without disposal of the application made for partition. If such assessment is done, it shall not be valid and it has to be set aside so that assessment can be made in conformity with the order under Section 171 which the Assessing Officer is bound to pass in accordance with law.

W.e.f. 31st December, 1978 partial partition is not recognised for tax purposes and as such the joint family shall continue to be liable to be assessed as if no such partial partition had taken place. Each member of such family, immediately before such partial partition and the family shall be jointly and severally liable for any sum payable under the Act. [Sec. 171(9)]

9.3 ASSESSMENT OF FIRMS

From the Assessment Year 1993-94 partnership firm has been classified for the purpose of computation of income and its assessment as under:

(a) Partnership Firm assessed as such (PFAS)

(b) Partnership Firm assessed as an Association of Person (PFAOP).

Provisions relating to assessment of firms and partners are analyzed as under :

Specific provisions to firm assessed as an AOP

Particulars	Sections
Disallowance of salary and interest to partner	40(ba)
Method of computing partner's share in the income of PFAOP	67A
Rate of tax in respect of income of AOP/BOI	167B
Taxability of partner's share of income	86, 110

Assessment of firms and conditions to be fulfilled to avail the status of PFAS [Sec. 184]

Where a firm wants to avail the status of PFAS, it has to satisfy the following conditions:-

(i) The firm shall be evidenced by an instrument and the individual shares of the partner shall be specified therein. [Sec. 184(1)]

(ii) A certified copy of the instrument of partnership shall accompany the return of income of the Previous Year relevant to the Assessment Year 1993-94 or subsequent year in respect of which assessment of the firm is first sought. [Sec.184(2)]

(iii) Wherever during a Previous Year a change takes place in the constitution of the firm or in the sharing ratio of partners, a certified copy of the revised instrument of partnership be submitted along with the return of income of the concerned year of assessment. [Sec. 184(4)]

(iv) There should not be any failure on the part of the firm as is specified in Sec. 144 [Sec. 184(5)]

It may be mentioned that once a firm is assessed as PFAS after fulfillment of the above conditions, it will be assessed as PFAS, for every subsequent year provided there is no change in either firm's constitution or partner's profit sharing ratio. However, there should not be any failure mentioned in Sec. 144. [Sec. 184(3)]

A partnership deed shall be certified in writing by all the major partners. Where, however, the firm is dissolved and the return is filed after its dissolution, then the copy of deed may be certified by all the major partners in the firm immediately before its dissolution. Where a partner is dead, then it will have to be certified by his legal representative. [Sec. 184(2) Expl.]

Computation of Income

The following provisions should be given due consideration while computing income of a firm-

(i) Provision relating to deductibility of remuneration paid to partners by firm.

(ii) Provision relating to deductibility of interest paid to partners by firm.

Essential conditions to be satisfied by a firm to be assessed as firm and to be eligible for deduction of interest, salary, etc, to the partners [Section 184] are as follows:

(A) In the first assessment year: The following conditions must be satisfied by the firm in the first assessment year to be assessed as a firm:

(1) Partnership is evidenced by an instrument i.e. there is a written document giving the terms of partnership.

The instrument of partnership may be in a single document or in more than one documents. Where the terms are spelt out in more than one document then all documents combined together would constitute instrument of partnership. But if such documents do not have the effect of bringing into existence a partnership then it will not amount to an instrument of partnership.[CIT vs. Wholesale Distt Cloth Importers Association (1973) Tax LR 867 (All.)]

(2) It is essential that a valid deed must specify as to how the profits of the business are to be shared among the partners. Profits include loss also. It is not necessary that the deed must specify the shares in exact arithmetical fraction or so. As long as the deed specifies the proportion in which profits are to be divided among partners the condition is satisfied. The partners may agree to share profits in any way they like. As long as the sharing of profits can be worked out according to the specification in the deed the condition is deemed to be satisfied.

Similarly, the deed also must spell out the proportion in which losses are to be shared among the partners. The problem can arise specially in cases where minors are admitted to the benefits of partnership and the major partners have unequal share in profits. Where there is no minor admitted to partnership then it may be presumed that the loss will be borne by the partners in the same proportion of profits.

(3) A certified copy of the said instrument of partnership shall accompany the return of income in respect of the assessment year for which the assessment as a firm is first sought.

(B) In the subsequent assessment years: Once the firm is assessed as a firm for any assessment year, it shall be assessed in the same capacity for every subsequent year if there is no change in the constitution of the firm or the share of the partners.

Where any such change had taken place in the previous year, the firm shall furnish a certified copy of the revised instrument of partnership along with the return of income for the assessment year relevant to such previous year.

The copy of the instrument of partnership deed should be certified by all partners, not being minors.

Where a firm had been assessed as a firm and in a later year, the salary and interest to be paid to partners has been changed in the partnership deed but the changed partnership deed is not attached alongwith the return of income of such assessment year the firm will be still assessed as firm but in such a situation, the interest and salary shall be allowed as deduction as per the earlier deed which was attached alongwith the return of income.

Presently, the assessee is nto required to file any documents alongwith the return of income, hence, the partnership deed will not be required to be filed alongwith the return of income but the same will be required to be produced on demand by the Assessing officer.

However, in the following two cases, the firm shall be assessed as a firm but shall not be eligible for any deduction on account of interest to a partner and remuneration to a working partner although the same are mentioned in the partnership deed:

(1) Where there is, on the part of the firm, any such failure as is mentioned in section 144 (relating to the best judgement assessment). [Section 184(5)]

(2) Where the firm does not comply with the three conditions mentioned under section 184 discussed above [Section 185].

However, in both the above two cases, such amount of interest, salary, bonus, etc. shall not be charged to tax in the hands of the partner.

Taxable income shall be computed as follows :

Step 1 - Income under the different heads of income - First find out income under the five heads of income

Step 2 - Adjustment of losses of the current year and earlier years - Losses should be set off according to the provisions of sections 70 to 78. The income after adjustment of losses is the gross total income.

Step 3 - Deduction from gross total income - Deductions specified under Chapter VI A should be considered while calculating the gross total income.

Step 4 - Rounding off - The balance should be rounded off to the nearest ₹ 10. It is called as net income or taxable income or total income.

Calculation of Tax Liability:

Step 1 – Determine Net Income and tax payable thereon at a normal rate of 30%.

Step 2 – Add surcharge @ 12% if the total income exceeds ₹1 crore

Step 3 – Add education cess and secondary and higher secondary education cess

Step 4 – Deduct rebate u/s 86, 90, 90A and 91

Step 5 – Add interest payable (if any)

Step 6 – Deduct amount of prepaid taxes paid (Advance Tax, Tax Deducted at Source, etc.)

The Balance so arrived is the amount of tax to be paid.

Note: (i) From the Assessment Year 2013-14, tax payable (i.e. amount arrived at Step 3) cannot be less than 18.5 percent of "Adjusted Total Income" in some Specified Cases.

(ii) Tht total amount payable as income tax and surcharge on total income exceeding ₹1 crore shall not exceed the total amount payable as income tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹1 crore.

Set off and carry forward of losses:

There are no special provisions for set-off and carry forward of losses of firms. These are the same as applicable in case of other assesses. The losses and unabsorbed depreciation of the firm can be carried forward by the firm only.

Where a change has occurred in the constitution of a firm, due to retirement of a partner or death of a partner, the firm shall not be entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner as exceeds his share of profits, if any, in the firm in respect of the previous year.

The loss for the purpose of section 78(1) and (2) above does not only mean loss under the head profits or gains from business or profession, it means loss under any head of income.

Where any person carrying on any business or profession has been succeeded in such capacity by another person otherwise than by inheritance, no person other than the person incurring the loss shall be entitled to have it carried forward and set off against is income. [Section 78(2)]

In other words, treatment in case of change in constitution of firm will be as follows:

Step 1: Calculate the share of profit of the retiring/ deceased partner in the year in which there is a change in the constitution due to such retirement/ death.

Step 2: Compute the share of loss of the retiring/deceased partner in the brought forward loss of the firm.

Step 3: Set off the share in the brought forward losses of the retiring/deceased partner from his share of the profit of the current year.

This set off of share of brought forward loss will be allowed to the extent of share of profit of such partner.

The balance loss, if any, will not be allowed to be carried forward either to such partner or to the firm.

On the other hand, if in the current year also the share of the partner is a loss, then share of the brought forward loss along with the share of loss of current year will not be allowed to be set off and carried forward.

Note:

Unabsorbed depreciation of the firm is not covered u/s 78 and therefore, the entire unabsorbed depreciation will be allowed to be carried forward in the hands of the firm, even if there is a change in the constitution of the firm.

Change in constitution of a firm [Section 187]

Where at the time of making an assessment u/s 143 or u/s 144, it is found that a change has occurred in the constitution of a firm, the assessment shall be made on the firm as constituted at the time of making the assessment. In other words, there will not be a separate assessment of firm even when there is a change in the constitution of the firm.

There is a change in the constitution of the firm:-

(a) If one or more of the partner cease to be partners or one or more new partners are admitted, in such circumstances that one or more of the persons who were partners of the firm before the change continue as partner or partners after the change; or

(b) Where all the partners continue with a change in their respective shares or in the shares of some of them.

Where a partnership deed provides that death shall not result into the dissolution of firm, such provision is lawful u/s 42 of the Partnership Act; on the death of the partner, a partnership is not dissolved and the business is continued by the re-constituted partnership, then only one assessment is to be made for the entire year [CIT vs. Empire Estate (1996) 218 ITR 355 (SC)].

Following are the examples of change in the constitution of the firm:

(1) A firm consists of 3 partners A, B & C. A retires from the firm on 31st July, 2014. This will be a case covered u/s 187 and if the Assessing Officer makes the assessment of income of the assessment year 2015-16 on 31st July, 2016, the assessment shall be made on the firm as constituted at the time of making the assessment on 31st July, 2016. However, the liability of the partners shall be governed by section 188A i.e. A, B & C shall be jointly and severally liable for any tax, interest and penalty of the firm.

(2) A firm consists of 3 partners A, B & C. A dies and as per partnership deed his son is taken as partner. This will also be a case covered u/s 187. However, liability of the partners shall be governed u/s 188A.

(3) A, B and S are three partners in a firm. A dies and there is nothing in the partnership deed as to what will happen if there is a death of a partner. In this case, the firm will be dissolved and it will be covered u/s 189.

(4) A and B are two partners of the firm. C joins the firm and B retires. It will be a case covered u/s 187. However, liability of the partners shall be governed by section 188A.

(5) A firm consists of 3 partners A, B & C. All the three partners go out and an entirely new set of partners say X, Y and Z come in. It would not amount to change in the constitution of the firm but would amount to the succession of one firm by another and section 188 would apply.

As stated above, this section would apply if at the time of making an assessment order under section 143 or 144 (which would also include reassessment section 147) it is found that a change has occurred in the constitution of the firm. The change might have occurred either in the relevant previous year, or in the assessment year or even later. The words "at the time of making an assessment" mean in the course of the process of assessment and do not refer merely to the act of making an assessment order. Thus, where a notice u/s 142(1)(i) for filing the return of income has been issued, the process of assessment of the person to whom notice is issued begins and would continue until an order of assessment is made and the assessment shall be made on the firm re-constituted if a change of the partners in the partnership occurs at any time before the assessment is made. However, this section has no application to a case where the change occurs after the assessment of the firm is completed.

Case Laws:

(1) The firm will be dissolved on the death of any of its partner, unless there is a specific provision in the partnership deed, that the firm would not be dissolved on the death of a partner. Thus, there will be two separate assessments. [CIT vs. Ayyanarappan & Co. (1999) 236 ITR 410 (SC)].

(2) A perusal of section 187(2)(a) of the Income Tax Act, 1961, shows that by legal fiction for the purposes of the Income Tax Act, if even one of the partners continues to remain in the firm then the firm will not be deemed to be dissolved. Hence, even if the partnership deed says that the firm will stand dissolved on the retirement of a partner, for the purposes of the Income Tax Act, it will not be deemed to be dissolved in view of section 187(2)(a). [CIT vs. Ratanlal Garib Das (2003) 261 ITR 200 (All)].

Where the firm is dissolved and reconstituted, it was merely a change in constitution of the firm under section 187 and not a case of succession under section 188. It was held that no separate assessment has to be made on two returns filed by the firm, instead only one assessment has to be made. [CIT vs. Hindustan Motors Finance Co. (2005) 276 ITR 382 (All)].

Where two partners out of 13 partners of the firm retire and on the same day two other partners joined alongwith eleven partners and the deed effecting these changes was described as a deed of dissolution and the firm filed two returns, one upto the date of retirement and the second after the date of retirement, it was held that the execution of the deed of the dissolution where two partners had retired and two new partners had come in would not make any difference and it would be a case of reconstitution of the firm. The case in hand was covered under section 187(1) of the Act and two assessments could not be made separately for the two periods. [CIT vs. Bliarat Steel Rolling Mills (2009) 313 ITR 406 (All)].

Where the firm is dissolved on the death of any of its partners it will not be considered as a change in the constitution of the firm as per clause (a) of section 187(2) given above. It will be covered under section 189.

Example:

(1) A, B & C are three partners of a firm. The partnership deed provides that on the death of a partner, the firm shall be dissolved. This case shall not be covered under section 187(2)(a) given above but it should be covered under section 189.

(2) A, B and C are three partners in a firm, A dies and there is nothing in the partnership deed as to what will happen if there is a death of a partner. In this case the firm will be dissolved and it will be covered under section 189.

The firm will be dissolved on the death of any of its partner, unless there is a specific provision in the partnership deed, that the firm would not be dissolved on the death of a partner. Thus, there will be two separate assessments. [CIT vs. Ayyanarappan & Co. (1999) 236 ITR 410 (SC)].

However, in the case of CIT vs. Jai Mewar Wine Contractors (2001) 251 ITR 785 (Raj) it was held that even if the partnership deed is silent on the contingency of death of a partner, it need not dissolve the firm as it was pointed out that a clause for continuation of the partnership without dissolution may not be expressed and it may be inferred from the conduct of the partners consequent on the death. The only exception in this case shall be where there are only two partners so that death of one cannot avoid dissolution.

Section 88 provides that where a firm carrying on a business or profession is succeeded by another firm, and the case is not one covered by section 187, separate assessments shall be made on the predecessor firm and the successor firm in accordance with the provisions of section 170.

As per section 170 the predecessor firm shall be assessed in respect of the income of the previous year in which succession took place up to the date of succession. The successor firm shall be assessed in respect of the income of the previous year after the date of succession.

Example: A, B & C a partnership firm is succeeded by X, Y & Z on 31.10.2015. In the case A, B & C shall be assessed in respect of income upto 31.10.2015 and X, Y & Z shall be assessed in respect of income after 31.10.2015.

According to section 189, where any business or profession carried on by a firm has been discontinued or where a firm is dissolved, the Assessing Officer shall make an assessment of the total income of the firm as if no such discontinuance or dissolution had taken place, and all the provisions of this Act, including the provisions relating to the levy of a penalty or any other sum chargeable under any provision of this Act, shall apply, so far as may be, to such assessment.

Every person who was at the time of such discontinuance or dissolution a partner of the firm, and the legal representative of any such person who is deceased, shall be jointly and severally liable for the amount of tax, penalty or other sum payable, and all the provisions of this Act, so far as may be, shall apply to any such assessment or imposition of penalty or other sum.

The tax payable, mentioned above, means the tax payable by the firm and not the tax assessed on the partners personally.

Where such discontinuance or dissolution takes place after any proceedings in respect of an assessment year have commenced, the proceedings may be continued against the person referred to above from the stage at which the proceedings stood at the time of such discontinuance or dissolution, and all the provisions of this Act shall, so far as may be, apply accordingly.

Where on the death of a partner or otherwise, the firm is actually dissolved by the partners and a new partnership deed is executed between some partners of the old firm or between new partner(s) and some partners of the old firm, it is a case of succession and hence there should be two separate assessments. However, in this case provisions of section 189 shall apply to the firm which is dissolved. On the other hand, if there is a succession to the business but the firm is not dissolved and it continues to exist although there will be two assessments as per section 188 but section 189 shall have no application.

Section 188A provides that every person who was, during the previous year, a partner of a firm and the legal representative of any such person who is deceased, shall be jointly and severally liable along with the firm for the amount of tax, penalty or other sum payable by the firm for the assessment year to which such previous year is relevant, and all the provisions of this Act, so far as may be, shall apply to the assessment of such tax or imposition or levy of such penalty or other sum.

Example: A partnership firm consisting of A, B, C & D was formed on 1.4.1999. Partner C retired on 17.6.2009 and E was taken in as partner on that very date. B retired on 15.10.2011 and F was taken in as partner on that date. The firm is dissolved on 15.9.2015.

In this case A, B, C & D are jointly and severally liable from assessment year 2000-2001 to 2009-10. E is also jointly and severally liable for assessment year 2010-11. For assessment year 2011-12 to 2012-13 A, B, E & D shall be jointly and severally liable. F is also jointly and severally liable for assessment year 2012-13. A, F, E & D shall be jointly and severally liable for assessment years 2012-13 to 2016-17.

9.4 ASSESSMENT OF LIMITED LIABILITY PARTNERSHIP (LLP)

A Limited Liability Partnership (LLP) is a body corporate formed or incorporated under the Limited Liability Partnership Act, 2008. It is a legally separate entity from its partners. It has perpetual succession i.e. any change in its partners will not have any impact on its existence, rights and liabilities. It is a corporate business form which gives benefits of limited liability of a company and the flexibility of a partnership. It contains elements of both a company as well as a partnership firm and thus it is called a hybrid between a partnership and a company. The Income-tax Act provides for the same taxation regime for a Limited Liability Partnership as is applicable to a partnership firm. It also provides tax neutrality (subject to fulfilment of certain conditions) to conversion of a Private Limited Company or an Unlisted Public Company into an LLP. However, Presumptive Tax Scheme u/s 44AD is not applicable to LLP.

An LLP being treated as a firm for taxation, has the following tax advantages over a company under the Income-tax Act :–

(i) it is not subject to Minimum Alternate Tax;

(ii) it is not subject to Dividend Distribution Tax (DDT); and

(iii) it is not subject to surcharge.

(iv) It is not subject to Wealth Tax.

In order to preserve the tax base vis-a-vis profit-linked deductions, a new Chapter XII-BA has been inserted in the Income-tax Act containing special provisions relating to certain Limited Liability Partnerships.

Calculation of Total income:

Step 1 - Income under the different heads of income - First find out income under the five heads of income

Step 2 - Adjustment of losses of the current year and earlier years - Losses should be set off according to the provisions of sections 70 to 78. The income after adjustment of losses is the gross total income.

Step 3 - Deduction from gross total income - Deductions specified under Chapter VI A should be considered while calculating the gross total income.

Step 4 - Rounding off - The balance should be rounded off to the nearest ₹ 10. It is called as net income or taxable income or total income.

Remuneration and interest to partners are deductible if condition of section 40(b) and 184 are satisfied.

Taxability:

Step 1 – Determine Net Income and tax payable thereon at a normal rate of 30%.

Step 2 – Add surcharge @ 12% if total income exceeds ₹ 1 crore

Step 3 – Add education cess and secondary and higher secondary education cess

Step 4 – Deduct rebate u/s 86, 90, 90A and 91

Step 5 – Add interest payable (if any)

Step 6 – Deduct amount of prepaid taxes paid (Advance Tax, Tax Deducted at Source, etc.)

The Balance so arrived is the amount of tax to be paid.

Note: (i) From the Assessment Year 2013-14, tax payable (i.e. amount arrived at Step 3) cannot be less than 18.5 percent of "Adjusted Total Income" if certain conditions are satisfied.

(ii) The total amount payable as income tax and surcharge on total income exceeding ₹ 1 crore shall not exceed the total amount payable as income tax on a total income of ₹ 1 crore by more than the amount of income that exceeds ₹ 1 crore.

Share of profit in LLP is not taxable in the hands of partners. However, remuneration and interest are taxable under section 28 under the "Profits and Gains of Business or Profession" in the hands of partners to the extent these are allowed as deduction in the hands of LLP.

Certain separate provisions of Limited Liability Partnership under Income Tax Act are as follows:

(A) The Finance (No. 2) Act, 2009 provided for the taxation of LLPs in the Income Tax Act on the same lines as applicable to partnership firms. Section 56 and section 57 of the Limited Liability Partnership Act, 2008 allow conversion of a private company or an unlisted public company (hereafter referred as company) into an LLP. Under the existing provisions of Income Tax Act, conversion of a company into an LLP has definite tax implications. Transfer of assets on conversion attracts levy of capital gains tax. Similarly, carry forward of losses and of unabsorbed depreciation is not available to the successor LLP.

The Act has inserted clause (xiiib) to section 47 to provide that the transfer of a capital asset or intangible asset by a private limited company or a non listed company, or any transfer of a share or shares held in the company by a shareholder on conversion of a private limited company or an unlisted company to a Limited Liability Partnership in accordance with section 56 and section 57 of the Limited Liability Partnership Act, 2008 shall not be regarded as a transfer for the purposes of capital gains tax under section 45, subject to certain conditions. These conditions are as follows:

(a) All the assets and liabilities of the company immediately before the conversion become the assets and liabilities of the Limited Liability Partnership;

(b) All the shareholders of the company immediately before the conversion become the partners of the Limited Liability Partnership and their capital contribution and profit sharing ratio in the Limited Liability Partnership are in the same proportion as their shareholding in the company on the date of conversion;

(c) The shareholders of the company do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of share in profit and capital contribution in the Limited Liability Partnership;

(d) The aggregate of the profit sharing ratio of the shareholders of the company in the Limited Liability Partnership shall not be less than 50% at any time during the period of five years from the date of conversion;

(e) The total sales, turnover or gross receipts in business of the company in any of the three previous years preceding the previous year in which the conversion takes place does not exceed ₹60,00,000; and

(f) No amount is paid, either directly or indirectly, to any partner out of balance of accumulated profit standing in the accounts of the company on the date of conversion for a period of three years from the date of conversion.

(B) Consequential amendments due to conversion of a private limited company or a non-listed company into LLP are as follows:

(1) The Act has amended, w.e.f. A.Y. 2011-12, sixth proviso to section 32(1) to provide that the aggregate depreciation allowable to the predecessor company and successor LLP shall not exceed, in any previous year, the depreciation calculated at the prescribed rates as if the conversion had not taken place. In other words, deprecation shall be allowed to the predecessor company and successor LLP in the proportion of a number of days the assets are used by the predecessor and success or assessee.

(2) W.e.f. A.Y. 2011-12 where there has been reorganisation of business, whereby a private company or unlisted public company is succeeded by a Limited Liability Partnership fulfilling the conditions laid down in the proviso to clause (xiiib) of section 47, the provisions of section 35DDA shall, as far as may be, apply to the successor LLP, as they would have applied to the said company, if reorganisation of business had not taken place.

(3) Explanation 13 to section 43(1) amended w.e.f. A.Y. 2011-12 to provide that the cost of acquisition of the capital asset for the successor LLP, in case the predecessor company has claimed deduction under section 35AD, shall be nil.

(4) W.e.f. A.Y. 2011-12, Explanation 2C in section 43(6) inserted to provide that the actual cost of the block of assets in the case of the successor LLP shall be the written down value of the block of assets as in the case of the predecessor company on the date of conversion.

(5) W.e.f. A.Y. 2011-12, where any of the conditions laid down in proviso to section 47(xiiib) are not complied with, in any subsequent assessment year the consequences shall be as under:

(a) the amount of profits or gains arising from the transfer of such capital asset or intangible asset not charged under section 45 by virtue of conditions laid down in the said proviso shall be deemed to be the profits and gains chargeable to tax of the successor LLP for the previous year in which the requirements of the said proviso are not complied with.

(b) the amount of profits or gains arising from the transfer of share was shares not charged u/s 45 by virtue of conditions laid down in the said proviso shall be deemed to be the profits and gains chargeable to tax of the share holder of the predecessor company for the previous year in which the requirements of the said proviso are not complied with.

(6) W.e.f. A.Y. 2011-12, Section 49(1) (iii) (e) provides that the cost of asset in the hands of the LLP in the case of conversion of a private limited company or an unlisted company shall be the cost to the previous owner.

(7) W.e.f. 01.04.2011, Section 49(2AAA) provides that where the capital asset being rights of a partner referred to in section 42 of the Limited Liability Partnership Act, 2008 became the property of the assessee on conversion as referred to in clause (xiiib) of section 47, the cost of acquisition of the asset shall be deemed to be the immediately before its conversion.

Section 42 of the Limited Liability Partnership Act, 2008 provides that Partner's transferable interest [Section 42]:

The rights of a partner to a share of the profits and losses of the LLP and to receive distributions in accordance with the LLP agreement are transferable either wholly or in part.

The transfer of any right by any partner pursuant to sub-section (1) does not by itself cause the disassociation of the partner or a dissolution and winding up of the LLP.

The transfer of right pursuant to this section does not, by itself, entitle the transferee or assignee to participate in the management or conduct of the activities of the LLP, or access information concerning the transactions of the LLP.

(8) W.e.f. A.Y. 2011-12, the Act has allowed carry forward and set-off of accumulated loss and unabsorbed depreciation to the successor LLP which fulfills the above mentioned conditions. [Section 72A(6A)].

The accumulated loss and the unabsorbed depreciation of the predecessor company, shall be deemed to be the loss or allowance for depreciation of the successor LLP for the purpose of the previous year in which business reorganisation was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly. In other words, accumulated loss shall be allowed for fresh 8 years and unabsorbed depreciation will be allowed to be carried forward indefinitely.

However, if any of the conditions laid down in the proviso of section 47(xiiib) are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the successor LLP, shall be deemed to be the income of the LLP chargeable to tax in the year in which such conditions are not complied with.

"Accumulated loss" means so much of the loss of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into LLP or the amalgamating company or the demerged company, as the case may be, under the head "Profits and gains of business or profession" (not being a loss sustained in a speculation business) which such predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, would have been entitled to carry forward and set off under the provisions of section 72 if the reorganisation of business or conversion or amalgamation or demerger had not taken place

"Unabsorbed depreciation" means so much of the allowance for depreciation of the predecessor firm or the proprietary concern or the private company or unlisted public company before conversion into LLP or the amalgamating company or the demerged company, as the case may be, which remains to be allowed and which would have been allowed to the predecessor firm or the proprietary concern or the company or amalgamating company or demerged company, as the case may be, under the provisions of this Act, if the reorganisation of business or conversion or amalgamation or demerger had not taken place.

(9) Credit in respect of tax paid by a company under section 115JB is allowed only to such company under section 115JAA. It has been clarified that the tax credit under section 115JAA shall not be allowed to the successor LLP.

(C) Like section 179 which is applicable for a private limited company, section 167C provides that notwithstanding anything contained in the Limited Liability Partnership Act, 2008, where any tax due from a LLP in respect of any income of any previous year or from any other person in respect of any income of any previous year during which such other person was a LLP cannot be recovered, in such case, every person who was a partner of the LLP at any time during the relevant previous year, shall be jointly and severally liable for the payment of such tax unless he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the LLP.

As an LLP and a general partnership is being treated as equivalent (except for recovery purposes) in the Act, the conversion from a general partnership firm to an LLP will have no tax implications if the rights and obligations of the partners remain the same after conversion and if there is no transfer of any asset or liability after conversion. If there is a violation of these conditions, the provisions of section 45 shall apply.

9.5 ASSESSMENT OF ASSOCIATION OF PERSONS / BODY OF INDIVIDUALS

Any payment of interest, salary, bonus, commission or remuneration by the AOP/BOI to a member is not allowable as deduction. Where interest is paid by AOP/BOI to a member who has also paid interest to the AOP/BOI, the amount of interest to be disallowed will be limited to the net amount of interest paid by the AOP/BOI. [Sec. 40(ba)]

Tax Rates :

		Where shares of members are determinate and known	Where shares of members are indeterminate or unknown
1.	None of the members having taxable income	At the rates applicable to individual	At the maximum marginal rate.
2.	Any member having income.	At the maximum marginal rate	At the maximum taxable marginal rate.

The amount of tax calculated shall be increased by a surcharge at the rate of 12% of such income tax in case the total income exceeds ₹1 crore. However, total amount payable as income tax and surcharge on total income exceeding ₹1 crore shall not exceed the total amount payable as income tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹1 crore.

Maximum Marginal Rate means the rate of tax (including surcharge, if any) applicable to the highest slab of income in case of individuals. [Sec. 2(29C)]

From the Assessment Year 2013-14, tax payable (i.e. tax liability) cannot be less than 18.5 percent of "Adjusted Total Income" in some specified cases.

Ascertainment of member's share in AOP/BOI where shares are determinate and its taxability [Sec. 67A, 86 & 110]

(i) Ascertainment of share in AOP/BOI [Sec. 67A]	₹
Total income of the AOP/BOI	***
Less: Interest, salary, commission or other remuneration paid to any member	***
Balance apportionable to the members in proportion to their shares	*******
Share of income allotted to a member	***
Add: Salary, interest, commission or other remuneration received by the member of the AOP or BOI	***
Total share	*******
Less: Interest paid on capital borrowed for the purpose of investment in the AOP/BOI	***
Net assessable share income	*******

(ii) Tax treatment of share income of members [Sec. 86 and Sec. 110]

In computing total income of an assessee, there shall be included share income of a member of an AOP or BOI subject to Sec. 86 and 110 of the I.T. Act.

The assessment of the members of AOP or BOI depends on whether the AOP or BOI is chargeable to tax at the maximum marginal rate or at slab rate or is not chargeable to tax at all.

Tax-treatment in the three cases is discussed below:

(i) Where AOP or BOI is chargeable to tax at a maximum marginal rate or any higher rate, the share of profit of a member is exempt from tax. Thus, it is not to be included in the total income of the member [Sec. 86(a)]

(ii) Where AOP or BOI is not taxed at the maximum marginal rate but it is taxed at slab rates, the share of profit of a member from AOP or BOI is to be included in the total income of the member only for rate purposes. The member is entitled to a rebate of tax on the entire share of profit at the average rate of tax applicable to total income. [Sec. 86(b)].

(iii) Where AOP or BOI is not chargeable to tax at all, the share of profit of a member from AOP or BOI is included in his total income and he will pay tax on it. He is not entitled to any rebate of tax on such profits [Proviso to Sec. 86(b)].

Taxation of AOP/BOI [Sec 167B]	**Tax treatment of share income in the hands of members of AOP/BOI [Sec. 86 & 110]**
1. AOP or BOI is taxed at maximum marginal rate or at a higher rate.	Share income of the member is not taxable.
2. AOP or BOI is taxed at normal rates applicable	Share income computed u/s 67A is included into an Individual. The total income of the member but rebate u/s 110 at the average of tax in respect of such share income has to be allowed.
3. AOP or BOI is not taxed at all	Share income will be included in the total income of the member and taxed at the rates applicable to him.

"Average rate of Income-tax" is defined u/s. 2(10) to mean the rate arrived at by dividing the amount of Income-tax calculated on the total income, by such total income.

9.6 ASSESSMENT OF COMPANIES

The total income of a company is also computed in the manner in which income of any other assessee is computed. The first and the foremost step in this direction is to ascertain Gross Total Income. Income computed under four heads (salary head is not applicable), is aggregated. While aggregating the income, section 60 and 61 shall be applicable. Further, effect to set off of losses and adjustment for brought forward losses will also be done. From the Gross Total Income so computed, the deductions u/s 80G, 80GGA, 80GGB, 80IA, 80IAB, 80IB, 80IC, 80ID, 80IE, 80JJA, 80JJAA & 80LA of Chapter VIA should be allowed.

The following are the special provisions under the Income Tax Act which are applicable to a company in which public are not substantially interested i.e. a closely held company:

(A) Carry forward and set off of losses [Section 79].

(B) Deemed dividend u/s 2(22)(e).

(C) Liability of directors [Section 179].

(A) Carry forward and set off of losses in case of certain companies [Section 79]

In the case of closely held companies where a change in shareholding has taken place in a previous year, no loss under any head incurred in any year prior to the previous year shall be carried forward and set off against the income of the previous year unless on the last day of the previous year in which loss is set off and on the last day of the previous year in which the loss was incurred, the shares of the company carrying not less than 51% of the voting power were beneficially held by the same persons.

In other words, where a change in voting power of more than 49% of the shareholding of a closely held company has taken place between two relevant dates (viz., the last day of previous year in which set off is claimed and the last date of the previous year in which the loss was incurred), the assessee will not be entitled to claim set off of such losses.

This provision shall not apply to a change in the voting power consequent upon:

(i) the death of a shareholder, or

(ii) on account of transfer of shares by way of gifts to any relative of the shareholder making such gift.

Further, section 79 shall not apply to any change in the shareholding of an Indian company which is subsidiary of a foreign company arising as a result of amalgamation or demerger of a foreign company subject to the condition that 51% of the shareholders of the amalgamating or demerged foreign company continue to remain the shareholders of the amalgamated or the resulting foreign company.

Section 79 applies to all losses, including losses under the head Capital Gains. However, overriding provisions of section 79 do not affect the set off of unabsorbed depreciation which is governed by section 32(2). [CIT vs. Concord Industries Ltd. (1979) 119 ITR 458 (Mad)].

(B) Deemed dividend [Section 2(22(e)]

Any payment by a company, not being a company in which the public are substantially interested, of any sum by way of advance or loan to a shareholder holding not less than 10% voting power or to a concern in which such shareholder is a member or a partner and in which he has substantial interest or any payment by such company on behalf or for the individual benefit of any such shareholder, to the extent to which company in either case possesses accumulated profit shall be treated as deemed dividend.

(C) Liability of directors of private company in liquidation [Section 179]

Where any tax due from a private company in respect of any income of any previous year cannot be recovered, then, every person who was a director of the private company at any time during the relevant previous year shall be jointly and severally liable for payment of such tax unless he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company.

The Finance Act, 2011 has inserted section 115BBD which provides as under:

(1) Sub-section (1) of this section provides that where the total income of an assessee, being an Indian company, for the previous year relevant to the assessment year beginning on the 1st day of April, 2012 includes any income by way of dividends declared, distributed or paid by a specified foreign company, the income-tax payable shall be the aggregate of—

  (a) the amount of income-tax calculated on the income by way of such dividends, at the rate of 15%; and

  (b) the amount of income-tax with which the assessee would have been chargeable had its total income been reduced by the aforesaid income by way of dividends.

(2) Sub-section (2) of this section provides that notwithstanding anything contained in this Act, no deduction in respect of any expenditure or allowance shall be allowed to the assessee under any provision of this Act in computing its income by way of dividends received from specified foreign company.

According to section 115BBD(3)(ii), "Specified foreign company" means a foreign company in which the Indian company holds 26% or more in nominal value of the equity share capital of the company.

The principal officer of the company is required to file the return of total income of the company on or before 31st October of the assessment year. A company is assessed like any other assessee. However, its liability differs in two respects:

(1) No exemption limit: A company does not enjoy any exemption limit.

(2) Flat Rate of Tax: A company pays income-tax at a flat rate instead of slab rate.

Rates of income-tax for the assessment years 2016-17 are as under:

1	Short Term Capital Gain on equity shares in a company or units of an equity oriented fund where the transaction is chargeable to securities transaction tax	15%
2	Tax on Long Term Capital Gains	20%
	Where the Long Term Capital Gains is covered by section 115AB, 115AC or 115AD,	10%
3	Tax on winnings from lotteries, cross word puzzles, races including horse races, etc.	30%
4	Tax on income by way of dividends declared, distributed or paid by a specified foreign company [Section 115BBD]	15%
5	Tax on any other income:	
	Domestic company	30%
	Foreign company:	
	Royalty received from Government or an Indian concern in pursuance of an agreement made by it with the Indian concern after March 31, 1961 but before 1st April, 1976 or fees for rendering technical services in pursuance of an agreement made by it after 29th February, 1964 but before 1st April, 1976 and where such agreement has in either case been approved by the Central Government	50%
	for any other income	40%

Surcharge: The amount of income-tax computed as above shall be increased by a surcharge of 5% in case of domestic companies and 2% in case of foreign companies provided the total income of such domestic/foreign company exceeds ₹1 crore.

However, the total amount payable as income tax and surcharge on total income exceeding ₹1 crore but not exceeding ₹10 crore, shall not exceed the total amount payable as income tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹1 crore. In case, the total income exceeds ₹10 crore, the amount payable as income tax and surcharge shall not exceed the total amount payable as income tax and surcharge on a total income of ₹10 crore by more than the amount of income that exceeds ₹10 crore.

Education cess: Education cess @ 2% shall be levied on the total tax (including surcharge) payable by the assessee.

SHEC: SHEC @ 1% shall be levied on the total tax (including surcharge) payable by the assessee. In other word SHEC shall be half of education cess.

Minimum Alternate Tax (MAT) [Sec. 115JB]

1. Section 115JB provides that, in the case of a company, if the tax payable on the total income as computed under the Income-tax Act in respect of any Previous Year is less than 18.5 per cent of its book profit, such book profit shall be deemed to be the total income of the assessee and the tax payable for the relevant Previous Year shall be 18.5% of such book profit.
2. The Profit and Loss Account should be prepared in accordance with Parts II and III of Schedule III of the Companies Act, 2013.

The Accounting Policies and the Accounting Standards adopted for preparing such accounts and the method and rates adopted for calculating the depreciation, shall be the same as have been adopted for the purpose of preparing such accounts and laid before the company at its AGM.

(a) the amount of income-tax paid or payable, and the provision therefor; or

(b) the amounts carried to any reserves, by whatever name called, other than a reserve specified under section 33AC; or

(c) the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities; or

(d) the amount by way of provision for losses of subsidiary companies; or

(e) the amount or amounts of dividends paid or proposed ; or

(f) the amount or amounts of expenditure relatable to any income to which section 10 *(other than the provisions contained in clause (38) thereof) or* section 11 *or* section 12 *apply; or*

Following clauses (fa), (fb) and (fc) shall be inserted after clause (f) in Explanation 1 below sub-section (2) of section 115JB by the Finance Act, 2015, w.e.f. 1-4-2016 :

(fa) the amount or amounts of expenditure relatable to, income, being share of the assessee in the income of an association of persons or body of individuals, on which no income-tax is payable in accordance with the provisions of section 86; or

(fb) the amount or amounts of expenditure relatable to income accruing or arising to an assessee, being a foreign company, from,—

(A) the capital gains arising on transactions in securities; or

(B) the interest, royalty or fees for technical services chargeable to tax at the rate or rates specified in Chapter XII,

if the income-tax payable thereon in accordance with the provisions of this Act, other than the provisions of this Chapter, it is a rate less than the rate specified in sub-section (1); or

(fc) the amount representing notional loss on transfer of a capital asset, being share or a special purpose vehicle to a business trust in exchange of units allotted by the trust referred to in clause (xvii) of section 47 *or the amount representing notional loss resulting from any change in carrying* *amount of said units or the amount of loss on transfer of units referred to in clause (xvii)* ofsection 47; or

(g) the amount of depreciation,

(h) the amount of deferred tax and the provision therefor,

(i) the amount or amounts set aside as provision for diminution in the value of any asset,

(j) the amount standing in revaluation reserve relating to revalued asset on the retirement or disposal of such asset,

Following clause (k) shall be inserted after clause (j) in Explanation 1 below sub-section (2) of section 115JB by the Finance Act, 2015, w.e.f. 1-4-2016:

(k) the amount of gain on transfer of units referred to in clause (xvii) of section 47 *computed by taking into account the cost of the shares exchanged with units referred to in the said clause or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through profit or loss account, as the case may be;*

if any amount referred to in clauses (a) to (i) is debited to the profit and loss account or if any amount referred to in clause (j) is not credited to the profit and loss account, and as reduced by,—

(i) the amount withdrawn from any reserve or provision (excluding a reserve created before the 1st day of April, 1997 otherwise than by way of a debit to the profit and loss account), if any such amount is credited to the profit and loss account.

Provided that where this section is applicable to an assessee in any previous year, the amount withdrawn from reserves created or provisions made in a previous year relevant to the assessment year commencing on or after the 1st day of April, 1997 shall not be reduced from the book profit unless the book profit of such year has been increased by those reserves or provisions (out of which the said amount was withdrawn) under this Explanation or Explanation below the second proviso to section 115JA, as the case may be; or

(ii) the amount of income to which any of the provisions of section 10 *(other than the provisions contained in clause (38) thereof) or* section 11 *or* section 12 *apply, if any such amount is credited to the profit and loss account; or*

(iia) the amount of depreciation debited to the profit and loss account (excluding the depreciation on account of revaluation of assets); or

(iib) the amount withdrawn from revaluation reserve and credited to the profit and loss account, to the extent it does not exceed the amount of depreciation on account of revaluation of assets referred to in clause (iia); or

Following clauses (iic), (iid), (iie) and (iif) shall be inserted after clause (iib) in Explanation 1 below sub-section (2) of section 115JB by the Finance Act, 2015, w.e.f. 1-4-2016 :

(iic) the amount of income, being the share of the assessee in the income of an association of persons or body of individuals, on which no income-tax is payable in accordance with the provisions of section 86, if any, such amount is credited to the profit and loss account; or

(iid) the amount of income accruing or arising to assessee, being a foreign company, from,—

(A) the capital gains arising on transactions in securities; or

(B) the interest, royalty or fees for technical services chargeable to tax at the rate or rates specified in Chapter XII,

if such income is credited to the profit and loss account and the income-tax payable thereon in accordance with the provisions of this Act, other than the provisions of this Chapter, is at a rate less than the rate specified in sub-section (1); or (iie) the amount representing,—

(A) notional gain on transfer of a capital asset, being share of a special purpose vehicle to a business trust in exchange of units allotted by that trust referred to in clause (xvii) of section 47; or

(B) notional gain resulting from any change in carrying amount of said units; or

(C) gain on transfer of units referred to in clause (xvii) of section 47,

if any, credited to the profit and loss account; or

(iif) the amount of loss on transfer of units referred to in clause (xvii) of section 47 *computed by taking into account the cost of the shares exchanged with units referred to in the said clause or the carrying amount of the shares at the time of exchange where such shares are carried at a value other than the cost through profit or loss account, as the case may be;*

(iii) the amount of loss brought forward or unabsorbed depreciation, whichever is less as per books of account.

Explanation.—For the purposes of this clause,—

(a) the loss shall not include depreciation;

(b) the provisions of this clause shall not apply if the amount of loss brought forward or unabsorbed depreciation is nil; or

(iv) to (vi) **[***]Omitted**

(vii) the amount of profits of sick industrial company for the assessment year commencing on and from the assessment year relevant to the previous year in which the said company has become a sick industrial company under sub-section (1) of section 17 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986) and ending with the assessment year during which the entire net worth of such company becomes equal to or exceeds the accumulated losses.

Explanation.—For the purposes of this clause, "net worth" shall have the meaning assigned to it in clause (ga) of sub-section (1) of section 3 of the Sick Industrial Companies (Special Provisions) Act, 1985 (1 of 1986); or

(viii) the amount of deferred tax, if any such amount is credited to the profit and loss account.

Explanation 2.—For the purposes of clause (a) of Explanation 1, the amount of income-tax shall include—

(i) any tax on distributed profits under section 115-O *or on distributed income under* section 115R;

(ii) any interest charged under this Act;

(iii) surcharge, if any, as levied by the Central Acts from time to time;

(iv) Education Cess on income-tax, if any, as levied by the Central Acts from time to time; and

(v) Secondary and Higher Education Cess on income-tax, if any, as levied by the Central Acts from time to time.

Explanation 3.—For the removal of doubts, it is hereby clarified that for the purposes of this section, the assessee, being a company to which the proviso to sub-section (2) of section 211 of the Companies Act, 1956 (1 of 1956) is applicable, has, for an assessment year commencing on or before the 1st day of April, 2012, an option to prepare its profit and loss account for the relevant previous year either in accordance with the provisions of Part II and Part III of Schedule VI to the Companies Act, 1956 or in accordance with the provisions of the Act governing such company.

Following Explanation 4 shall be inserted after Explanation 3 to sub-section (2) of section 115JB by the Finance Act, 2015, w.e.f. 1-4-2016:

Explanation 4.—For the purposes of sub-section (2), the expression "securities" shall have the same meaning as assigned to it in clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956 (42 of 1956).

(3) Nothing contained in sub-section (1) shall affect the determination of the amounts in relation to the relevant previous year to be carried forward to the subsequent year or years under the provisions of sub-section (2) of section 32 *or sub-section (3) of* section 32A *or clause (ii) of sub-section (1) of* section 72 *or* section 73 *or* section 74 *or sub-section (3) of* section 74A.

(4) Every company to which this section applies, shall furnish a report in the prescribed form from an accountant as defined in the Explanation below sub-section (2) of section 288, certifying that the book profit has been computed in accordance with the provisions of this section along with the return of income filed under sub-section (1) of section 139 *or along with the return of income furnished in response to a notice under clause (*i) of sub-section (1) of section 142.

(5) Save as otherwise provided in this section, all other provisions of this Act shall apply to every assessee, being a company, mentioned in this section.

(5A) The provisions of this section shall not apply to any income accruing or arising to a company from life insurance business referred to in section 115B.

(6) The provisions of this section shall not apply to the income accrued or arising on or after the 1st day of April, 2005 from any business carried on, or services rendered, by an entrepreneur or a Developer, in a Unit or Special Economic Zone, as the case may be.

Provided that the provisions of this sub-section shall cease to have effect in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April, 2012.

Provided that the provisions of this sub-section shall cease to have effect in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April, 2012.

The tribunals decision in case of Sutlej Cotton Mills vs. CIT and Sipani Automobiles vs. DCIT to the effect that profit on sale of assets need not form part of book profits now stand superseded by the decision of Bombay High Court in CIT vs. Veekaylal Investment Co. Pvt. Ltd (2001) 249 ITR 597 (Bom). The Bombay High Court observed as under:

Since capital gain has to be considered in computation of income, it cannot fail to be reckoned in computation of books profits as well, since in its view 'in the circumstances one fails to understand as to how in computing book profits under the Companies Act, the assessee company cannot consider capital gain for computing book profits under section 115J (now 115JB) of the Act. The High Court also felt, it would be inappropriate to directly transfer such amounts to capital reserves and that they are required to be shown vide clauses (2)(b) and 3(xii) of Part II of Schedule VI of the Companies Act.

Capital profit credited to profit and loss account is part of book profit, even if it is exempt under section 54EC [N.J. Jose & Co. (P) Ltd vs. CIT (2008) 174 Taxman 141 (Ker)].

On such analogy loss on sale of car/truck debited to Profit and Loss Account cannot be added back [Asian Diet Products vs. CIT (2007) 162 Taxman 210 (Del)(Mag)].

Under Part II of Schedule III of the Companies Act, where a company receives an amount of surrender of lease hold rights, it is bound to disclose in the Profit and Loss Account the said amount as nonrecurring transaction or a transaction of an exceptional nature irrespective of its nature whether it is capital or revenue. Further, Profit and loss account shall disclose every material feature including transaction or transaction of an exceptional nature, which includes profits on sale of fixed assets, therefore profit on sale of fixed assets formed part of the book profit under section 115JA (New section 115JB). [GKW vs. CIT (2011) 64 DTK 79 (Cal)].

3. Provisions shall not affect carried forward of depreciation and losses under the applicable provisions mentioned in sub-section (3) of section 115JB.

4. Profits of an Entrepreneur in SEZ or Developer of SEZ are not liable for MAT.

5. Tax paid under section 115JB for A.Y. 2012-13 and any subsequent year would be allowed as a credit from the normal tax payable for any subsequent year in accordance with the provisions contained in section 115JAA. However, the amount of tax credit cannot be carried forward for set off beyond the tenth Assessment Year immediately succeeding the Assessment Year in which tax credit becomes allowable.

6. A report in prescribed form (Form No. 29B as per Rule 40B) from an accountant as defined in the section 288 shall be furnished along with the return of income.

7. All companies are liable for payment of advance tax having regard to the provisions contained in new section 115JB. Consequently, the provisions of sections 234B and 234C for interest on defaults in payment of advance tax and deferment of advance tax would also be applicable where facts of the case warrant. - Circular : No. 13/2001, dated 9-11-2001.

Where a private company or unlisted public company is converted into limited liability partnership in any previous year, the Mat credit which was available to the company shall lapse. In other words the tax credit under section 115JAA shall not be allowed to the successor LLP.

A company registered under section 8 of the companies Act, whose income is exempt under principles of mutuality cannot be brought within the purview of section 115JB [Delhi Gymkhana Club Ltd vs. Dy. CIT (2010) 39 DTR 48 (Del) (Trib): (2010) 35 SOT 335 (Del)].

Although, the assessee is liable to pay tax @18.5% (plus surcharge if applicable) of the book profits if its total income computed as per Income-tax Act is less but it is entitled to determine unabsorbed depreciation under section 32(2), business loss under section 72(1), speculation loss under section 73 and capital loss under section 74 and loss under section 74A and shall be allowed to carry forward such unabsorbed depreciation or losses to the subsequent years(s) for claiming set off as per the normal provisions of Income-tax Act.

In the connection of old section 115J (the provisions of section 115JB are similar in this case) the Authority for Advance Rulings held that such provisions are applicable to foreign companies also and the foreign companies shall calculate its Indian profits separately for the purpose of minimum alternate tax [P No. 14 of 1997, In re (1998) 234 ITR 828 (AAR)]. However, where a non-resident's income is assessed on the basis of presumptive income under sections 44B, 44BB, 44BBA, etc or at a flat rate under section 115A on royalty and technical fee, the book profit becomes immaterial for regular assessment and the presumptive income tax will prevail [Timken India Ltd, In re (2005) 273 ITR 67 (AAR)].

As per section 115JB(5), save as otherwise provided in section 115JB, all other provisions of the Income-tax Act shall apply to such companies. Hence, all other provisions relating to advance tax, interest under sections 234A, 234B and 234C penalty, etc. shall apply to such companies also.

Companies liable to pay tax on the basis of MAT are required to pay advance tax and failure to pay advance tax in respect of the same will attract interest under sections 234B and 234C [JCIT vs. Rolta India Ltd (2011)330 ITR 470 (SC)].

Dividend Distribution Tax

As per section 115-O(1), the Domestic Company shall, in addition to the income-tax chargeable in respect of its total income, be liable to pay additional income-tax on any amount declared, distributed or paid by such company by way of dividend (whether interim or otherwise), whether out of current or accumulated profits. Such additional income-tax shall be payable @17.64706% plus surcharge @12% (w.e.f 1.10.14) plus education cess @ 2% plus SHEC @ 1% of the amount so declared, distributed or paid.

Dividend received from subsidiary company to be reduced from the above dividend to be distributed [Section 115-O(IA)] [W.r.e.f. A.Y. 2008-09]: For the purpose of computation of tax on distributed profits, the amount of dividend distributed by the domestic company during the financial year shall be reduced by the following:

(i) The amount of dividend, if any, received by the domestic company during the financial year, if—

- (a) such dividend is received from its subsidiary;
- (b) the subsidiary has paid tax under this section on such dividend; and
- (c) the domestic company is not a subsidiary of any other company.

(ii) The amount of dividend, if any, paid to any person for or behalf of the New Pension Scheme trust referred to in section 10(44).

However, that the same amount of dividend shall not be taken into account for reduction more than once.

For the purposes of section 115-O(1A), a company shall be a subsidiary of another company, if such other company holds more than half in nominal value of the equity share capital of the company.

Section 115-O of the Act provides that dividend liable for DDT in case of a company is to be reduced by an amount of dividend received from its subsidiary after payment of DDT if the company is not a subsidiary of any other company. This removes the cascading effect of DDT only in a two-tier corporate structure.

With a view to remove the cascading effect of DDT in multi-tier corporate structure, section 115-O(1A) of the Act has been amended to provide that in case any company receives, during the year, any dividend from any subsidiary and such subsidiary has paid DDT as payable on such dividend, then, dividend distributed by the holding company in the same year, to that extent, shall not be subject to Dividend Distribution Tax under section 115-O of the Act.

Dividend distribution tax which is also known as additional tax will have to be paid by the principal officer of the domestic company and the company within 14 days from the date of:

- (a) Declaration of any dividend; or
- (b) Distribution of any dividend; or
- (c) Payment of any dividend,

  whichever is earliest.

The company or the shareholder shall not be allowed any deduction in respect of the amount which has been charged to tax or the tax thereon under any provisions of the Income-tax Act.

As per section 115P, where the principal officer of a domestic company and the company fail to pay the whole or any part of the tax on distributed profits referred to in section 115-O(1) within the time, he or she or it shall be liable to pay simple interest @ 1% for every month or part thereof on the amount of such tax for the period beginning on the date immediately after the last date on which such tax was payable and ending with the date on which the tax is actually paid.

As per section 115Q, if the principal officer of a domestic company and the company does not pay tax on distributed profits in accordance with the provisions of section 115-O, then he or she or it shall be deemed to be an assessee in default in respect of the amount of tax payable by him or her or it and all the provisions of the Income-tax Act for the collection and recovery of income-tax shall apply. The assessee who is deemed to be in default in making the payment of tax on distributed profits is liable for penalty under section 221 of the Income-tax Act.

Further, as per section 271C, if any person fails to pay the whole or any part of the tax as required under section 115-O(2), then such person shall be liable to pay, by way of penalty, a sum equal to the amount of tax which such person failed to pay as aforesaid.

The penalty is, however, not applicable, if the assessee proves that there was reasonable cause for failure.

As per section 276B, if a person fails to pay to the credit of the Central Government the tax payable by the person under section 115-O(2), the person shall be punishable with rigorous imprisonment for a term which shall not be less than three months but which may extend to seven years and with fine.

However, no person will be punishable if the person proves that there was a reasonable cause for the default/failure.

As the dividend distribution tax is payable by a domestic company on the amount of dividend including deemed dividend covered under section 2(22)(a), (b), (c) and (d) paid, distributed or declared by it, such dividend shall be exempt in the hands of the shareholders under section 10(34).

However, deemed dividend covered under section 2(22(e)) shall be taxable in the hands of the shareholder.

Any amount of income distributed by: (i) a specified company, or (ii) a Mutual Fund to its unit holders shall be chargeable to tax and such specified company or Mutual Fund shall be liable to pay additional income-tax on such distributed income at the following rate:

1	(a) Where the income is distributed to any person being an individual or a HUF by a money market mutual fund or a liquid fund	25% + 7% or 12% SC + 2% EC + 1% SHEC
	(b) Where the income is distributed to any other person by a money market mutual fund or liquid fund	30% + 7% or 12% SC + 2% EC+1% SHEC
2	Where the income is distributed by a fund other than a money market mutual fund or a liquid fund and such income is distributed to—	
	(a) Individual or HUF	12.5% + 7% or 12% SC + 2% EC + 1% SHEC
	(b) Any person other than individual	30% + 7% or 12% SC + 2% EC or HUF +1%SHEC

1. 'Money market mutual fund' means a money market mutual fund as defined in sub-clause (p) of clause 2 of the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996.
2. 'Liquid fund' means a scheme or plan of a mutual fund which is classified by the Securities and Exchange Board of India as a liquid fund in accordance with the guidelines issued by it in this behalf under the SEBI Act, 1992 or regulations made thereunder.

The Finance Act, 2013 has amended section 115-O(1A) to provide as under:

For the purpose of computation of tax on distributed profits, the amount of dividend distributed by the domestic company during the financial year shall be **reduced** by the following:

the amount of dividend, if any, received by the domestic company during the financial year, if such dividend is received from its subsidiary and,—

(a) where such subsidiary is a domestic company, the subsidiary has paid the tax which is payable under this section on such dividend; or

(b) where such subsidiary is a foreign company, the tax is payable by the domestic company under section 115BBD on such dividend.

However, the same amount of dividend shall not be taken into account for reduction more than once.

Sunset provisions inserted regarding exemption from Minimum Alternate Tax (MAT) and Dividend Distribution Tax (DDT) in case of Special Economic Zones [Sections 115JB(6), 115-O(6) read with section 10AA & 80-IAB]

Under the existing provisions of section 10AA of the Income-tax Act, a deduction of 100% is allowed in respect of profits and gains derived by a unit located in a Special Economic Zone (SEZ) from the export of articles or things or services for the first five consecutive Assessment Years; of 50% for further five Assessment Years; and thereafter, of 50% of the ploughed back export profit for the next five years.

Further, under section 80-IAB of the Income-tax Act, a deduction of 100% is allowed in respect of profits and gains derived by an undertaking from the business of development of an SEZ notified on or after 1.4.2005 from the total income for any ten consecutive Assessment Years out of fifteen years beginning from the year in which the SEZ is notified by the Central Government.

Under the existing provisions of section 115JB(6), an exemption is allowed from payment of Minimum Alternate Tax (MAT) on book profit in respect of the income accrued or arising on or after 1.4.2005 from any business carried on, or services rendered, by an entrepreneur or a Developer, in a Unit or Special Economic Zone (SEZ), as the case may be.

Further, under the existing provisions of section 115-O(6), an exemption is allowed from payment of tax on distributed profits [Dividend Distribution Tax (DDT)] in respect of the total income of an undertaking or enterprise engaged in developing or developing and operating or developing, operating and maintaining a Special Economic Zone for any Assessment Year on any amount declared, distributed or paid by such Developer or enterprise, by way of dividends (whether interim or otherwise) on or after 1.4.2005 out of its current income. Such distributed income is also exempt from tax under section 10(34) of the Act.

The above provisions were inserted in the Income-tax Act by the Special Economic Zones Act, 2005 (SEZ Act) with effect from 10th February, 2006.

Currently, there is no sunset date provided for exemption from MAT in the case of a developer of an SEZ or a unit located in an SEZ. Similarly, there is no sunset date for exemption from DDT in the case of a developer of an SEZ.

The Finance Act, 2011 has sunset the availability of exemption from Minimum Alternate Tax in the case of SEZ Developers and units in SEZs in the Income-tax Act as well as the SEZ Act w.e.f. A.Y. 2012-13. Hence, units of SEZ and developers of SEZ shall be liable to MAT w.e.f. A.Y. 2012-13.

It has further discontinued the availability of exemption from dividend distribution tax in the case of SEZ Developers under the Income-tax Act as well as the SEZ Act for dividends declared, distributed or paid on or after 1.6.2011 which shall be taxable @ 20.358% [17.64706% + 12% SC + 3% (EC + SHEC)].

Consequential amendments have also be made by omitting *Explanation* to section 10(34) of the Income-tax Act w.e.f. 1.6.2011.

Amalgamation [Sec. 2(1B)]

Amalgamation in relation to companies means the merger of one or more companies with another company, or merger of two or more companies to form a new company. The company so merged goes out of existence is "amalgamating company." The company into which the amalgamating company merges, or the new company that is formed to effect amalgamation, is "amalgamated company" in such a manner that :–

(a) All property of amalgamating company, immediately before amalgamation, should become the property of amalgamated company,

(b) All liabilities of amalgamating company, immediately before amalgamation, should become the liabilities of amalgamated company,

(c) Shareholders holding 75% in value of the shares in amalgamating company should become shareholders of the amalgamated company. However, if the amalgamated company or its subsidiary/nominee already holds some shares in the amalgamating company, value of such shares is excluded for calculating 75% of the value of shares of the amalgamating company.

A merger of companies will not be treated as amalgamation in case of sale or liquidation of company.

The effective date in a scheme of amalgamation is the date of transfer specified in the scheme and not the date of high court's order approving the scheme. So long as the court does not modify the date specified in the scheme, amalgamation takes effect on date of transfer specified in the scheme. The income of the amalgamating company from such date of transfer shall be assessed as income of the amalgamated company and shall be assessed accordingly. [Marshall Sons and Co. (India) Ltd. vs. ITO (SC), 223 ITR 809]

Certain concessions are provided under various provisions of the Income-tax Act in respect of amalgamation which are as under:

(a) To amalgamating company

1) Sec. 47 (vi): In a scheme of amalgamation if an Indian Company satisfies the condition of Sec 2(1B), Capital Gains tax is not attracted in case of transfer of capital asset by the amalgamating company to the amalgamated company.

2) Sec. 47(via): Tax concession to foreign amalgamating company.

By virtue of Sec. 47(via), transfer of shares in an Indian Company held by a foreign company to another foreign company in a scheme of amalgamation is not treated as transfer if the following conditions are satisfies :-

(i) Shares in an Indian company held by a foreign company.

(ii) Business of the foreign company is taken over by another company in a scheme of amalgamation.

(iii) Atleast 25% of the shareholders of amalgamation foreign company continue to remain shareholders of the amalgamated company.

(iv) Such transfer does not attract tax on Capital Gains in the company in which the amalgamating company is incorporated.

(b) To shareholders of an amalgamating company

Sec. 47(vii) : Transfer by a shareholder in a scheme of amalgamation of a capital asset being a share or shares held by him in amalgamating company if such transfer is made in consideration of allotment to him of shares in the amalgamated company and the amalgamated company is an Indian Company.

(c) To amalgamated company

The following benefits in the hands of amalgamating company are available to the amalgamated company:

Sec. 35(5) : Expenditure on scientific research

Sec. 35A(6) : Expenditure on acquisition of patent right or copy right

Sec. 35AB(3) : Expenditure on know how

Sec. 35ABB(6) : Expenditure for obtaining license to operate telecommunication services

Sec. 35D(5) : Amortisation of preliminary expenses

Sec. 36E(7) : Deduction for expenditure on prospecting etc. for certain minerals

Sec. 36(ix) : Expenditure incurred for the purpose of promoting family planning.

Sec. 72A : Carry forward and set off of accumulated and unabsorbed depreciation

Further, the amalgamated company is entitled for :

Sec. 35DD : Amortisation of expenditure in case of amalgamation or demerger

As per section 72A the amalgamated company is entitled to carry forward the unabsorbed depreciation and accumulated loss of the amalgamating company provided the following conditions are fulfilled:

(1) There should be an amalgamation of—

(a) a company owning an industrial undertaking or ship or a hotel with another company, or

(b) a banking company referred in section 5(c) of the Banking Regulation Act, 1949 with a specified bank, or

(c) one or more public sector company or companies engaged in the business of operation of aircraft with one or more public sector company or companies engaged in the similar business.

(2) The following conditions laid down under section 72A(2) are satisfied by the amalgamating company and the amalgamated company as the case may be:

(a) Conditions to be satisfied by the amalgamating company

(i) The amalgamating company has been engaged in the business, in which the accumulated loss occurred or depreciation remains unabsorbed, for 3 or more years.

(ii) The amalgamating company has held continuously as on the date of the amalgamation at least 75% of the book value of fixed assets held by it two years prior to the date of amalgamation;

In other words, if an amalgamation takes places on 5-11-2015, then 75% of the book value of assets which were held by the amalgamating company on 5-11-2015 should continue to held by it on 5-11-2017.

Example: Suppose X Ltd holds the following assets on 5-11-2015.

Assets	Book value on 5-11-2015 ₹ (in lakh)
A	30
B	50
C	60
D	40
E	12
F	8
	200

In this case, assets carrying book value of at least ₹150 lakh (75% of ₹200 lakh) as on 5-11-2015 should be held on 5-11-2017 as well. Thus, if the company has assets A, B, C and D on 5-11-2017 it shall satisfy the above condition as total value on 5-11-2015 was ₹180 lakh. Alternatively, it should have at least assets B, C and D (₹ 150 lakh) or assets A, C, D, E, F (₹150 lakh) or A, B, C, E (₹150 lakh) on 5-11-2017. It may noted that the value of these assets as on the date of amalgamation i.e. 5-11-2017 is not relevant.

(b) Conditions to be satisfied by the amalgamated company

(i) the amalgamated company holds continuously for a minimum period of 5 years from the date of amalgamation at least 75% of the book value of fixed assets of the amalgamating company acquired in the scheme of amalgamation;

(ii) the amalgamated company continues the business of the amalgamating company for a period of 5 years from the date of amalgamation;

(iii) the amalgamated company fulfils such other conditions as may be prescribed (See Rule 9C mentioned below) to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purposes laid down by section 72A(2)(b)(iii).

Conditions for carrying forward or set-off of accumulated loss and unabsorbed depreciation allowable in case of amalgamation [Rule 9C]:

The conditions referred to in section 72A(2)(b)(iii) shall be the following, namely:

(a) The amalgamated company, owning an industrial undertaking of the amalgamating company by way of amalgamation, shall achieve the level of production of at least fifty per cent of the installed capacity of the said undertaking before the end of four years from the date of amalgamation and continue to maintain the said minimum level of production till the end of five years from the date of amalgamation.

Provided that the Central Government, on an application made by the amalgamated company, may relax the condition of achieving the level of production or the period during which the same is to be achieved or both in suitable cases having regard to the genuine efforts made by the amalgamated company to attain the prescribed level of production and the circumstances preventing such efforts from achieving the same.

(b) The amalgamated company shall furnish to the Assessing Officer a certificate in Form No. 62, duly verified by an accountant, with reference to the books of account and other documents showing particulars of production, along with the return of income for the assessment year relevant to the previous year during which the prescribed level of production is achieved and for subsequent assessment years relevant to the previous years falling within five years from the date of amalgamation.

(1) Installed capacity means the capacity of production existing on the date of amalgamation.

(2) Accountant means the accountant as defined in the Explanation below sub-section (2) of section 288 of the Income-tax Act, 1961.

If the conditions mentioned under (2)(a) and (2)(b) previously are satisfied by both the amalgamating and amalgamated company, then the accumulated loss and unabsorbed depreciation of the amalgamating company shall become the business loss and unabsorbed depreciation of the amalgamated company. Such accumulated loss will be allowed to be carried forward by the amalgamated company for fresh 8 years and unabsorbed depreciation can be carried forward indefinitely.

Accumulated loss means so much of the loss of amalgamating company under the head "profits and gains of business or profession" (not being a loss sustained in a speculation business) which the amalgamating would have been entitled to carry forward and set off under the provisions of section 72 if amalgamation had not taken place. Further, brought forward loss under the head "house property" or "capital gain" whether short or long-term of the amalgamating company will get lost and neither company can avail it as there is no special provision in this regard.

Although unabsorbed depreciation and accumulated business loss will be carried forward by the resulting company in a scheme of demerger provided conditions mentioned in section 72A are complied with, but unabsorbed capital expenditure on scientific research cannot be brought either under unabsorbed depreciation or accumulated business loss [ITO vs. Mahyco Vegetable Seeds Ltd (2009) 308 ITR (AT) 205 (Mum)].

As per section 72A(3), where if the conditions laid down under clause (b) above are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the amalgamated company shall be deemed to be the income of the amalgamated company chargeable to tax for the year in which such conditions are not complied with. Further, the balance accumulated loss and unabsorbed depreciation not yet set off shall not be allowed to be carried forward and set off.

If any amalgamation takes place within the meaning of section 2(1B) of the income-tax, the following tax concession shall be available:

(1) Tax concession to amalgamating company.

(2) Tax concession to shareholders of the amalgamating company.

(3) Tax concession to amalgamated company.

Tax concession to amalgamating company

(i) Capital Gains tax not attracted: According to section 47(vi), where there is a transfer of any capital asset in the scheme of amalgamation, by an amalgamating company to the amalgamated company, such transfer will not be regarded as a transfer for the purpose of capital gain provided the amalgamated company, to whom such assets have been transferred, is an Indian company.

(ii) Tax concession to a foreign amalgamating company [Section 47(via)], where a foreign company holds any shares in an Indian company and transfers the same, in the scheme of amalgamation, to another foreign company, such transaction will not be regarded as transfer for the purpose of capital gain under section 45 of the Income-tax Act if the following conditions are satisfied:

(1) Atleast 25% of the shareholders of amalgamating foreign company should continue to remain shareholders of amalgamated foreign company, and

(2) Such transfer does not attract tax on capital gains in the country, in which the amalgamating company is incorporated.

Tax concessions to the shareholders of a amalgamating company [Section 47(vii)]: Where a shareholder of an amalgamating company transfers his shares, in a scheme of amalgamation, such transaction will not be regarded as a transfer for capital gain puiposes, if following conditions are satisfied:

(i) the transfer of shares is made in consideration of the allotment to him of any share or shares in the amalgamated company except where the shareholder itself is the amalgamated company, and

(ii) the amalgamated company is an Indian company.

Tax concessions to the amalgamated company: The amalgamated company shall be eligible for tax concessions only if the following two conditions are satisfied:

(a) The amalgamation satisfies all the three conditions laid down in section 2(1B); and

(b) The amalgamated company is an Indian company.

The result of such amalgamation [i.e. which takes places within the meaning of section 2(1B)] is that neither the company which gets amalgamated nor the shareholders of such company become liable for capital gain tax.

(1) **Expenditure on Scientific Research [Section 35(5)]:** Where an amalgamating company transfers any asset represented by capital expenditure on the scientific research to the amalgamated Indian company in a scheme of amalgamation, the provisions of section 35 which were applicable to the amalgamating company shall become applicable to the amalgamated company consequently:—

  (i) Unabsorbed capital expenditure on scientific research of the amalgamating company will be allowed to be carried forward and set off in the hands of the amalgamated company.

  (ii) If such asset ceases to be used in a previous year for scientific research related to the business of amalgamated company and is sold by the amalgamated company without having being used for other purposes, the sale price, to the extent of the cost of the asset shall be treated as business income of the amalgamated company. The excess of the sale price over the cost of the asset shall be subject to the provisions of the capital gains.

(2) **Expenditure for obtaining licence to operate telecommunication services [Section 35ABB(6)]:** Where in a scheme of amalgamation, the amalgamating company sells or otherwise transfer its licence to the amalgamated company (being an Indian company), the provisions of section 35ABB which were applicable to the amalgamating company shall become applicable in the same manner to the amalgamated company, consequently:

(i) The expenditure on acquisition of licence, not yet written off, shall be allowed to the amalgamated company in the same number of balance installments.

(ii) Where such licence is sold by the amalgamated company, the treatment of the deficiency/surplus will be same as would have been in the case of amalgamating company.

(3) **Treatment of preliminary expenses [Section 35D(5)]:** Where an amalgamating company merges in a scheme of amalgamation with the amalgamated company, the amount of preliminary expenses of the amalgamating company, which are not yet written off, shall be allowed as deduction to the amalgamated company in the same manner as would have been allowed to the amalgamating company.

(4) **Amortisation of expenditure in case of amalgamation [Section 35DD]:** (i) Where an assessee, being an Indian company, incurs any expenditure, on or after the 1st day of April, 1999, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the previous year in which the amalgamation or demerger takes place.

(ii) No deduction shall be allowed in respect of the expenditure mentioned in sub-section (1) under any other provision of this Act.

(5) **Treatment of expenditure on prospecting, etc. of certain minerals [Section 35E(7A)]:** Where an amalgamating company merges in a scheme of amalgamation with the amalgamated company, the amount of expenditure on prospecting, etc. of certain minerals of the amalgamating company, which are not yet written off, shall be allowed as deduction to the amalgamated company in the same manner as would have been allowed to the amalgamating company.

(6) **Treatment of capital expenditure on family planning [Section 36(1)(ix)]:** Where the asset representing the capital expenditure on family planning is transferred by the amalgamating company to the Indian amalgamated company, in a scheme of amalgamation, the provisions of section 36(1)(ix) to the amalgamating company shall become applicable, in the same manner, to the amalgamated company. Consequently:

(i) The capital expenditure on family planning not yet written off shall be allowable to the amalgamated company in the same number of balance installments.

(ii) Where such assets are sold by amalgamated company, the treatment of the deficiency/surplus will be same as would have been in the case of amalgamating company.

(7) **Treatment of bad debts [Section 36(1)(vii)]:** Where due to amalgamation, the debts of amalgamating company have been taken over by the amalgamated company and subsequently such debt or part of the debt becomes bad as per Income Computation and Disclosure Standard (ICDS), such bad debt will be allowed as a deduction to the amalgamated company.

(8) **Deduction available under section 80-IAB or 80-IB or 80-IC or 80-IE:** Where an undertaking which is entitled to deduction under section 80-IAB/80-IB/80-IC/80-IE is transferred in the scheme of amalgamation before the expiry of the period of deduction under section 80-IAB or 80-IB or 80-IC or 80-IE, then—

(i) no deduction under section 80-IAB/80-IB/80-IC/80-IE shall be available to the amalgamating company for the previous year in which amalgamation takes place; and

(ii) the provisions of section 80-IAB/80-IB/80-IC/80-IE shall apply to the amalgamated company in such manner in which they would have applied to the amalgamating company.

The benefit of section 80-IA is not available to the amalgamated company where the amalgamation takes place on or after 1-4-2007 [Section 80-IA(12A)].

(9) Carry forward and set off of business losses and unabsorbed depreciation of the amalgamating company: In addition to the above benefits/concessions, the amalgamated company shall be allowed to carry forward and set off the business losses and unabsorbed depreciation of the amalgamating company if all the conditions mentioned in section 72A are satisfied.

(10) Apportionment of depreciation between the amalgamating company and amalgamated company [Proviso 5 to section 32]: If in any previous year there is any amalgamation then for the purpose of computing depreciation for that previous year it will be first assumed as if no amalgamation had taken place and thereafter depreciation so computed shall be apportioned between the amalgamating company and the amalgamated company in the ratio of the number of days for which the assets were used by them.

There can be two types of assets which can be transferred by an amalgamating company to the Indian amalgamated company in the scheme of amalgamating viz:

(i) Non-depreciable assets. (ii) Depreciable assets.

The cost of acquisitions of assets in each case is as under:

Acquisition cost in case of non-depreciable assets for purposes of capital gains under section 45: In this case, the cost of acquisition of the asset shall be deemed to be the cost for which the previous owner of the property acquired it, as increased by cost of any improvement of asset, incurred or borne by the previous owner or the assessee, as the case may be.

However, if the capital asset is a non-depreciable asset and is acquired by the previous owner before 1-4-1981, the cost of acquisition to the amalgamated company can be taken as cost of acquisition to the previous owner or the Fair Market Value of the asset on 1-4-1981, at the option of the amalgamated company.

(1) Since in the above case, the cost of the previous owner is taken, the period for which the previous owner had held the asset shall also be considered for determining whether the capital gain is short-term or long-term.

(2) However, indexation of cost shall be done from the year in which it was first held by the amalgamated company i.e. the year of amalgamation.

For other provision of income-tax the cost of these assets to the amalgamated company shall not be the value at which it is actually transferred to the company but it shall be taken to be the same as it would have been if the amalgamating company had continued to hold the capital asset for the purpose of his own business.

Acquisition cost in case of depreciable assets:

(i) Cost of acquisition for purpose of business income i.e. for calculating depreciation: It shall be the written down value of the block of assets as in the case of the amalgamating company for the immediately preceding previous year as reduced by the amount of depreciation actually allowed in relation to the said preceding previous year.

(ii) For purpose of capital gains: In the case of depreciable assets, transferred by the amalgamating company to the amalgamated company, the period of holding and indexed cost of acquisition are irrelevant as, these assets will be included in the 'block of assets' of the amalgamated company and according to section 50, if any capital asset of the block is transferred, or the entire block of assets is transferred, the capital gains, if any, on such transfer will be treated as short-term capital gain.

As per section 41(1), where an amalgamating company was earlier allowed any allowance/deduction in respect of loss, expenditure, or trading liability and subsequently the amalgamated company has obtained/recovered whether in cash or in any other manner any amount in respect of which any allowance/deduction was allowed to the amalgamating company, such amount shall be deemed to be the profits and gains of business or profession of the amalgamated company of the previous year in which it is obtained or recovered.

Where any tax is payable by the amalgamating company in respect of its income of business or profession of the earlier period, the amalgamated company shall be liable to pay such tax, if it cannot be recovered from the amalgamating company. However, the amalgamated company shall be liable for the following period:

(i) for previous year in which the amalgamation took place but only up to the date of amalgamation;

(ii) for previous year preceding the year in which the amalgamation takes place.

For example: If the amalgamation took place on 17-7-2014 the liability of tax of the amalgamating company for the previous year 2013-14 and previous year 2014-15 (up to 17-7-2014 only) can be recovered from the amalgamated company.

Every amalgamation scheme is effective from the specified/appointed date. The important tax issue that arises is whether the transfer is effective from the date mentioned in the scheme or from the date in which the scheme was approved by the Court. The Madras High Court in United India Life Insurance Co. Ltd vs. CIT (1963) 49 ITR 965 (Mad) held that it is effective from that date of approval by the court.

However, the Bombay High Court in CIT vs. Swastik Rubber Product Ltd (1983) 140 ITR 304 (Bom) held that it is effective from the appointed date as specified in the scheme of amalgamation.

The above issue of specified/appointed date was put at rest by Supreme Court in Marshal Sons & Co. (India) Ltd vs. CIT (1997) 223 ITR 809 (SC) where it was held that it is effective from the date mentioned in the scheme and not from the date on which the courts sanctioned the order. However the courts while sanctioning the scheme, is open to modify the said date and prescribe such date of amalgamation as it thinks appropriate in the facts.

Demerger [Sec. 2(19AA)]

"Demerger" in relation to companies, means the transfer, pursuant to a scheme of arrangement under sections 230 to 232 of the Companies Act, 2013, by a demerged company of its one or more undertakings to any resulting company in such a manner that —

(i) all the property of the undertaking, being transferred by the demerged company, immediately before the demerger, becomes the property of the resulting company by virtue of the demerger;

(ii) all the liabilities relatable to the undertaking being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;

(iii) the property and the liabilities of the undertaking or undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger;

(iv) the resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis;

(v) the shareholders holding not less than three-fourths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or, its subsidiary) become shareholders of the resulting company or companies by virtue of the demerger. Otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;

(vi) the transfer of the undertaking is on a going concern basis;

(vii) the demerger is in accordance with the conditions, if any, notified under sub-section (5) of section 72A by the Central Government in this behalf.

For the purpose of this definition, "undertaking" shall include any part of an undertaking, or a unit of division of an undertaking or a business activity taken as a whole, but does not include individual assets and/or liabilities or a combination of these not constituting a business activity. For determining the value of the property which is subject matter of demerger, any change in the value of assets on account of revaluation shall be ignored.

Splitting up or the reconstruction of any authority or a body constituted or established under any Act, or a local authority or a public sector company, into separate authorities or bodies or local authorities or companies shall be deemed to be the demerger if such split up or reconstruction fulfils the conditions as may be notified by the Central Government.

- **Demerged Company [Section 2(19AAA)] :** It means the company whose undertaking is transferred, pursuant to a demerger, to a resulting company.
- **Resulting Company :** means one or more companies (including wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and the resulting company in consideration of such transfer of undertaking, issues shares to shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger.

If any demerger takes places within the meaning of section 2(19AA) of the Income-tax Act, the following tax concession shall be available:

(1) Tax concessions to demerged company.

(2) Tax concessions to shareholders of demerged company.

(3) Tax concessions to resulting company.

These concessions are on similar lines as are available in case of amalgamation discussed earlier. However some concessions available in case of amalgamation are not available in case of demerger.

(1) Tax concession to demerged company:

(i) **Capital gains tax not attracted [Section 47(vib)]:** According to section 41(vib) where there is a transfer of any capital asset in a demerger by the demerged company to the resulting company, such transfer will not be regarded as a transfer for the purpose of capital gain provided the resulting company is an Indian company.

(ii) **Tax concession to a foreign demerged company [Section 47(vic)]:** Where a foreign company holds any shares in an Indian company and transfers the same, in a demerger, to another resulting foreign company, such transaction will not be regarded as transfer for the purpose of capital gain under section 45 if the following conditions are satisfied:

(a) at least seventy-five per cent of the shareholders of the demerged foreign company continue to remain shareholders of the resulting foreign company; and

(b) such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated.

(iii) **Reserves for shipping business:** Where a ship acquired out of the reserve is transferred in a scheme of demerger, even within the period of eight years of acquisition there will be no deemed profits to the demerged company.

(2) Tax concessions to the shareholders of the demerged company [Section 47(vid)]: Any transfer or issue of shares by the resulting company, in a scheme of demerger to the shareholders of the demerged company shall not be regarded as a transfer if the transfer or issue is made in consideration of demerger of the undertaking.

In the case of demerger the existing shareholder of the demerged company will now hold:

(a) shares in resulting company; and

(b) shares in demerged company,

and in case the shareholder transfers any of the above shares subsequent to the demerger, the cost of such shares shall be calculated as under:—

Cost of acquisition of shares in the resulting company [Section 49(2C)]: It shall be the amount which bears to the cost of acquisition of shares held by the assessee in the demerged company the same proportion as the net book value of the assets transferred in a demerger bears to the net worth of the demerged company immediately before such demerger.

In other words:

$$\begin{array}{c}\text{Cost of}\\ \text{acquisition of}\\ \text{the shares in}\\ \text{the resutlting}\\ \text{company}\end{array} = \begin{array}{c}\text{cost of acquisition}\\ \text{of share held by the}\\ \text{assessee in the}\\ \text{demerged company}\end{array} \times \frac{\begin{array}{c}\text{Net book value of the}\\ \text{assets transferred in a}\\ \text{demerger}\end{array}}{\begin{array}{c}\text{Net worth of the demerged}\\ \text{company immediately}\\ \text{before demerger}\end{array}}$$

Cost of acquisition of shares in the demerged company [Section 49(2D)]: The cost of acquisition of the original shares held by the shareholder in the demerged company shall be deemed to have been reduced by the amount as so arrived at under section 49(2C) above.

For the above purpose net worth shall mean the aggregate of the paid up share capital and general reserves as appearing in the books of account of the demerged company immediately before the demerger.

Period of holding of shares of the resulting company [Section 2(42A)(g)]: In the case of a capital asset, being a share or shares in an Indian company, which becomes the property of the assessee in consideration of a demerger, there shall be included the period for which the share or shares held in the demerged company were held by the assessee.

(3) Tax concession to the resulting company: The resulting company shall be eligible for tax concessions only if the following two conditions are satisfied:

(i) The demerger satisfies all the conditions laid down in section 2(19AA); and

(ii) The resulting company is an Indian company.

The following concessions are available to the resulting company pursuant to a scheme of demerger:

(a) Expenditure for obtaining licence to operate telecommunication services [Section 35ABB(7)]: Where in a scheme of demerger, the demerged company sells or otherwise transfer its licence to the resulting company (being an Indian company), the provisions of section 35ABB which were applicable to the demerged company shall become applicable in the same manner to the resulting company, consequently:

(i) The expenditure on acquisition of licence, not yet written off, shall be allowed to the resulting company in the same number of balance installments.

(ii) Where such licence is sold by the resulting company, the treatment of the deficiency/ surplus will be same as would have been in the case of demerged company.

(b) Treatment of preliminary expenses [Section 35D(5A)]: Where the undertaking of an Indian company which is entitled to deduction of preliminary expenses in transferred before the expiry of 10 years/5 years, as the case may be, to another company in a scheme of demerger, the preliminary expenses of such undertaking which are not yet written off shall be allowed as deduction to the resulting company in the same manner as would have been allowed to the demerged company. The demerged company will not be entitled to the deduction thereafter.

(c) **Treatment of expenditure on prospecting, etc. of certain minerals [Section 35E(7A)]:** Where the undertaking of an Indian company which is entitled to deduction on account of prospecting of minerals, is transferred before the expiry of period of 10 years to another company in a scheme of demerger, such expenditure of prospecting, etc. which is not yet written off shall be allowed as deduction to the resulting company in the same manner as would have been allowed to the demerged company. The demerged company will not be entitled to the deduction thereafter.

(d) **Treatment of bad debts [Section 36(1)(vii)]:** Where due to demerger the debts of the demerged company have been taken over by the resulting company and subsequently by such debt or part of debt becomes bad as per ICDS, such bad debt will be allowed as a deduction to the resulting company.

(e) **Amortisation of expenditure in case of demerger [Section 35DD]:** According to sub-section 1 where an assessee, being an Indian company, incurs any expenditure, on or after 1-4-1999, wholly and exclusively for the purposes of demerger of an undertaking, the assessee shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the previous year in which the demerger takes place.

No deduction shall be allowed in respect of the expenditure mentioned in sub-section (1) under any other provision of this Act.

(f) **Carry forward and set off of business losses and unabsorbed depreciation of the demerged company [Section 72A(4) & (5)]:** The accumulated loss and unabsorbed depreciation, in a demerger, should be allowed to be carried forward by the resulting company if these are directly relatable to the undertaking proposed to be transferred. Where it is not possible to relate these to the undertaking, such loss and depreciation shall be apportioned between the demerged company and the resulting company in proportion of the assets coming to the share of each as a result of demerger.

(g) **Deduction available under section 80-IA or 80-IB:** Where an undertaking which is entitled to deduction under section 80-IA/80-IB is transferred in the scheme of demerger before the expiry of the period of deduction under section 80-IA or 80-IB, then—

(i) no deduction under section 80-IA/80-IB shall be available to the demerged company for the previous year in which amalgamation takes place; and

(ii) the provisions of section 80-IA/80-IB shall apply to the resulting company in such manner in which they would have applied to the demerged company.

The benefit of section 80-IA for the unexpired period shall not be available to the resulting company where the demerger takes place on or after 1-4-2007 [Section 80-IA(12A)].

As per section 2(42C), "slump sale" means the transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such sales.

(1) "Undertaking" shall have the meaning assigned to it in Explanation 1 to clause (19AA).

(2) The determination of the value of an asset or liability for the sole purpose of payment of stamp duty, registration fees or other similar taxes or fees shall not be regarded as assignment of values to individual assets or liabilities.

As per section 50B, any profits or gains arising from the slump sale effected in the previous year shall be chargeable to income-tax as capital gains arising from the transfer of long-term capital assets and shall be deemed to be the income of the previous year in which the transfer took place.

However, any profits or gains arising from the transfer under the slump sale, of any capital asset being one or more undertakings owned and held by an assessee for not more than thirty-six months immediately preceding the date of its transfer shall be deemed to be the capital gains arising from the transfer of short-term capital assets.

In relation to capital assets being an undertaking or division transferred by way of such sale, the "net worth" of the undertaking or the division, as the case may be, shall be deemed to be the cost of acquisition and the cost of improvement for the purposes of sections 48 and 49 and no regard shall be given to the provisions contained in the second proviso to section 48.

Net worth shall be the aggregate value of total assets of the undertaking or division as reduced by the value of liabilities of such undertaking or division as appearing in its books of account.

However any change in the value of assets on account of revaluation of assets shall be ignored for the purposes of computing the net worth.

For computing the net worth, the aggregate value of total assets shall be,—

(a) in the case of depreciable assets, the written down value of the block of assets determined in accordance with the provisions contained in section 43(6)(c)(i) relating to written down value in case of slump sale;

(b) in the case of other assets, the book value of such assets.

Conversion of Firm into Company

As per section 47(xiii) if the following conditions are satisfied then the transfer of capital asset in case of a firm into company is not chargeable to tax.

(a) all the assets and liabilities of the firm relating to the business immediately before the succession become the assets and liabilities of the company;

(b) all the partners of the firm immediately before the succession become the shareholders of the company in the same proportion in which their capital accounts stood in the books of the firm on the date of the succession;

(c) the partners of the firm do not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company;

(d) the aggregate of the shareholding in the company of the partners of the firm is not less than 50% of the total voting power in the company and their shareholding continues to be as such for a period of 5 years from the date of the succession.

Conversion of sole proprietary business into a company

As per section 47(xiv) if the following conditions are satisfied then the transfer of capital asset in case of a sole proprietary firm into company is not chargeable to tax:

(a) all the assets and liabilities of the sole proprietary concern relating to the business immediately before the succession become the assets and liabilities of the company;

(b) the shareholding of the sole proprietor in the company is not less than 50%, of the total voting power in the company and his shareholding continues to remain as such for a period of 5 years from the date of the succession; and

(c) the sole proprietor does not receive any consideration or benefit, directly or indirectly, in any form or manner, other than by way of allotment of shares in the company [Section 47(xiv)].

Withdrawal of exemption in both the above cases [Section 47A(3)]

As per section 47A(3), where the aggregate of the shareholding of the partners or the shareholding of the sole proprietor, as the case may be, in the company does not continue to remain 50% of the total voting power for a period of 5 years from the date of succession, the capital gain not chargeable to tax earlier at the time of succession due to the provisions of section 47(xiii) or (xiv) shall be chargeable to tax in the hands of successor company in the previous year in which such requirement is not complied with.

Carry forward of loss of property firm/firm by company [Section 72A(6)]

According to section 72A(6), where there has been reorganisation of business, whereby, a firm is succeeded by a company fulfilling the conditions laid down in clause (xiii) of section 47 or a proprietary concern is succeeded by a company fulfilling the conditions laid down in clause (xiv) of section 47, then, notwithstanding anything contained in any other provisions of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor firm or the proprietary concern, as the case may be, shall be deemed to be the loss or allowance for depreciation of the successor company for the purpose of previous year in which business reorganization was effected and other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.

In other words, the accumulated loss and unabsorbed depreciation of the predecessor company shall become the accumulated loss and unabsorbed depreciation of the successor company of the previous year in which business reorganization was effected and such business loss can be carried forward for fresh 8 assessment years and the unabsorbed depreciation will be carried forward indefinitely.

Consequences if the conditions laid down under section 47(xiii) and (xiv) are not complied with [Proviso to section 72A(6)]: If any of the conditions laid down under section 47(xiii) and (xiv) are not complied with, the set off of loss or allowance of depreciation made in any previous year in the hands of the successor company, shall be deemed to be the income of the company chargeable to tax in the year in which such conditions are not complied with.

9.7 ASSESSMENT OF CO-OPERATIVE SOCIETIES

Introduction

Cooperative society is a society registered under the Cooperative Societies Act, 1912, or under any other law for the time being in force in any State for registration of co-operative societies.

The deduction provided to various co-operative societies under section 8OP are as under:

(A) Where 100% deduction is allowed

In the case of the following co-operative societies, full deduction is allowable in respect of following incomes:

(I) Profits attributable to certain specified activities [Section 80P(2)(a)]: 100% of the profits, included in Gross Total Income, attributable to any one or more of the following activities are deductible:

- (i) carrying on the business of banking or providing credit facilities to its members; or
    - (1) W.e.f. assessment year 2007-08, the exemption shall not be available to co-operative banks other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank. However, deduction shall still be available to a cooperative society which is engaged in the business of providing credit facilities to its members.
    - (2) Regional Rural Banks are not eligible to take deduction under section 8OP. [Circular No. 6/2010, dated 29-0-2010].
- (ii) a cottage industry; or
- (iii) the marketing of the agricultural produce grown by its members; or

(iv) the purchase of agricultural implements, seeds, livestock or other articles intended for agriculture for the purpose of supplying them to its members; or

(v) the processing, without the aid of power, of the agricultural produce of its members; or

(vi) the collective disposal of the labour of its members; or

(vii) fishing or allied activities, that is to say, the catching, curing, processing, preserving, storing or marketing of fish or the purchase of materials and equipment in connection therewith for the purpose of supplying them to its members.

However, in case of co-operative societies falling under clauses (vi) and (vii) above, the deduction, is available subject to the condition that the rules and bye-laws of the society restrict the voting rights to the following classes of its members, namely:—

(1) the individuals who contribute their labour or, as the case may be, carry on the fishing or allied activities;

(2) the co-operative credit societies which provide financial assistance to the society;

(3) the State Government.

(II) Profits of certain primary co-operative societies [Section 80P(2)(b)]: 100% of the profits, included in Gross Total Income are deductible in the case of a co-operative society, being a primary society engaged in supplying milk, oilseeds, fruits or vegetables raised or grown by its members to

(i) a federal co-operative society, being a society engaged in the business of supplying milk, oilseeds, fruits, or vegetables, as the case may be; or

(ii) the Government or a local authority; or

(iii) a Government company as defined in section 2(45) of the Companies Act, 2013 or a statutory corporation (being a company or corporation engaged in supplying milk, oilseeds, fruits or vegetables, as the case may be, to the public).

Where district societies like the assessee collected milk from primary societies at village or taluk level and thereafter processed the milk and supplied it to the affiliated federal societies, it was held that the assessee was one step above the primary co-operative societies. The assessee was a federal cooperative society not only collecting and supplying milk but also processing the milk. The processing activities carried on by the assessee did not match the expression "being a primary society engaged in supplying the milk" used under section 80P(2)(b) of the Act. Therefore, the assessee was not entitled to deduction under section 8OP of the Act [Asstt. CIT vs. Salem District Co-op. Milk Producers Union Ltd (2009) 313 ITR (AT) 43 (Chennai)].

(III) Income from investment with other co-operative societies [Section 80P(2)(d)]: 100% of the profits, included in Gross Total Income are deductible in respect of any income by way of interest or dividends derived by the co-operative society from its investments with any other co-operative society.

(IV) Income from letting of 'godowns or warehouse' [Section 80P(2)(e)]: 100% of the profits, included in Gross Total Income are deductible in respect of any income derived by the co-operative society from the letting of godowns or warehouses for storage, processing or facilitating the marketing of commodities.

(B) Where deduction is allowed to a limited extent

In the following cases, the co-operative societies are entitled to deduction to a limited extent:—

(1) Co-operative society engaged in other activities [Section 80P(2)(c)]: In the case of a co-operative society engaged in activities, other than those specified in I and II of (A) above, either independently of, or in addition to, all or any of the activities so specified, the profits and gains attributable to such other activities up to the limits indicated below are deductible.

(i) where such co-operative society is a consumers' cooperative society ₹1,00,000;

(ii) in any other case ₹50,000.

(a) Consumer co-operative means a society for the benefit of consumers.

(b) Where the assessee co-operative society, supplied coal and diesel to its members for use in production of bricks and tiles, the society was not a 'consumer' cooperative society as the purchases by the members was not for their own consumption [Tamil Nadu Brick and Tiles Manufacturers Industrial Service Co-operative Society Ltd vs. CIT (2004) 265 ITR 332 (Mad)].

(2) Entire income by way of interest on securities or income from house property if gross total income of a co-operative society (other than specified co-operative society) does not exceed ₹20,000 [Section 80P(2)(f)]: 100% of the income from interest on securities or income from house property shall be allowed as deduction in case of a co-operative society not being—

(i) a housing society or

(ii) an urban consumer society, or

(iii) a society carrying on transport business, or

(iv) a society engaged in the performance of any manufacturing operation with the aid of power provided its gross total income does not exceed ₹20,000.

Urban Consumer Co-operative Society means a society for the benefit of the consumers within the limits of municipal corporation, municipality, municipal committee, notified area committee, town area or cantonment.

Where an assessee is also entitled to deduction u/s 80-IA, deduction u/s 8OP shall be allowed with reference to such profits and gains as reduced by the deduction allowed under those Sections [Section 80P(3)].

Case Laws:

(1) Each clause or sub-clause of section 80P(2) is to be treated as a separate and distinct head of exemption without being influenced by conditions) of any other clause or sub-clause. As section 8OP is introduced with a view to encouraging and promoting the growth of the co-operative sector in the economic life of the country and in pursuance of the declared policy of the Government, the correct way of reading the different heads of exemption enumerated in that section would be to treat each as a separate and distinct head of exemption. Whenever a question arises as to whether any particular category of an income of a cooperative society is exempt from tax what has to be seen is whether the income fell within any of the several heads of exemption. If it fell within any one head of exemption, it would be free from tax notwithstanding that the conditions of another head of exemption are not satisfied and such income is not free from tax under that head of exemption [Kerala State Co-operative Marketing Federation Ltd vs. 077(1998) 231 ITR 814, 819 (SC)].

(2) 100% deduction can be availed only where the income is from the activities specified. Activity which is not so specified shall not enjoy the full exemption. Thus, income from a printing press business run by a co-operative society was held not entitled to full exemption [ACIT vs. U.P. Co-operative Cane Union (1978) 114 ITR 70 (All)].

(3) If a co-operative society carries on certain activities income from which is exempted and also certain activities income from which is not exempted, the profits and gains attributable to the exempted activities shall enjoy the exemption and those attributable to the non-exempted activities shall be taxed. At the same time, it is just and proper that in order to ascertain the income referable to non-exempt activities the proportionate expenditure out of the total expenditure should be deducted [Cf. CIT vs. Sabarkantha Zilla Kharid Vechan Sangh Ltd (1977) 107 ITR 447 (Guj); Sabarkantha Zilla Kharid Vechan Sangh Ltd vs. CIT (1993) 203 ITR 1027 (SC)].

In other words, if a co-operative society is carrying on a business and earning income, part of which is exempted and part of which is not exempted, the profits and gains attributable to the exempted activity has to be arrived at on the basis of the books of account maintained by the assessee. If separate sets of books or separate accounts of expenditure have been maintained for the exempted and non-exempted activities, there is no problem. If separate sets of books of account have not been maintained and the expenses have been incurred jointly for earning both the incomes, then such expenses have to be estimated by the Assessing Officer which are relatable to earn the income from non-exempted activities in order to arrive at the true and correct income. It cannot be presumed that no expenditure was incurred in earning the exempted income.

Following the Supreme Court decision in Gandevi Taluka Khedut (1993) 203 ITR 1027 (SC), Sahakari Sangh Ltd vs. CIT (1994) 207 ITR 175, 179 (Guj) it has been held that while granting deduction under section 80P(2)(a)(iv) only the net income attributable to the activities under section 80P(2)(a)(iv) for the purchase of agricultural implements, live stock, etc. intended for supplying to agriculturists which is included in the gross total income can be deducted and not the entire income from such activities.

(4) If the society has income some of which is exempt under one clause and the other under another clause of section 80P(2), both will enjoy exemption [Allahabad Dist. Coop. Bank Ltd. vs. Union of India (1972) 83 ITR 895 (All)].

Under the amended provisions of section 80P(2)(a)(iii), exemption is available in respect of income derived from activities specified in the said provision ie income of marketing of produce grown by its members. In the instant case, income derived by the assessee was from dealing in wheat gram, maize, bazra and potatoes which was not grown by its members. The said income was not exempt from tax [CIT vs. Haryana State Co-operative Marketing Federation Ltd. (2008) 171 Taxman 138 (P&H)].

'Primary Co-operative Bank' means a co-operative society, other than a primary agricultural credit society—

(1) the primary object or principal business of which is the transaction of banking business;

(2) the paid-up shares capital and reserves of which are less than ₹1,00,000; and

(3) the bye-laws of which do not permit admission of any other cooperative society as a member: However, this provision shall not apply to the admission of a Co-operative Bank as a member by reason of such co-operative Bank subscribing to the share capital of such co-operative society out of funds provided by the State Government for the purpose.

'Primary agricultural credit society' means a co-operative society,—

(i) the primary object or principal business of which is to provide financial accommodation to its members for agricultural purposes or for purposes connected with agricultural activities (including the marketing of crops); and

(ii) the bye-laws of which do not permit admission of any other co-operative society as member:

the above sub-clause shall not apply to the admission of a co-operative bank as a member by reason of such co-operative bank subscribing to the share capital of such co-operative society out of funds provided by the State Government for the purpose.

The term **'primary co-operative agricultural and rural development bank'** has now been defined to mean a society whose area of operation is confined to a taluka and has as its principal object the provision of long-term credit for specified activities.

On the basis of divided case following receipts can be regarded as income attributable to business of banking:

(1) Ordinarily, banks invest their money in Government securities. One of the purposes of such activity is to ensure availability of ready money to meet various exigencies of the banking business. In case of

co-operative banks, holding of Government securities would indeed appropriately be connected with the banking business and thus their matter would be covered by the first part of section 80P(2)(a)(i) [Berhampur Co-operative Central Bank vs. Addl CIT (1974) 93 ITR 168 (Ori)].

At the same time, the investment contemplated above must be from out of the circulating capital or stock-in-trade of the society [M.P. State Co-operative Bank Ltd vs. Addl. CIT (1979) 119 ITR 327 (MP)].

(2) Interest on Government securities held as stock-in-trade is eligible for deduction under the provisions similar to section 80P(2)(a)(i). To such interest provisions similar to section 80P(2)(f) are not applicable. [Addl. CIT vs. Rajasthan State Co-operative Bank Ltd, (1987) 163 ITR 213 (Raj)].

(3) The income derived by the assessee from the investment in Government securities placed with the State Bank of India/Reserve Bank of India cannot be regarded as an essential part of its banking activity in as much as the same does not form part of its stock-in-trade or working/circulating capital. Thus such income shall not be deductible under section 80P(2)(a)(i) but deduction shall be available under section 80P(2)(c) [Madhya Pradesh Co-operative Bank Ltd vs. Addl. CIT (1996) 218 ITR 438 447 (SC)].

(4) However, the larger bench of the Supreme Court in case of CIT vs. Karnataka State Co-operative Apex Bank (2001) 251 ITR 194 (SC) held that interest on investments made by a Co-operative Bank in compliance with statutory provision to enable it to carry on banking business out of reserve fund has to be treated as eligible income from its banking business as there is a nexus of such income to the business of the assessee and hence it was eligible for deduction under section 80P(2)(a)(i).

(5) In CIT vs. Ma Sahakari Kendriya Bank Maryadit [(1997) 225 ITR 421 (MP)], income from interest on securities earmarked to reserve fund and gratuity has been held not entitled to deduction under section 80P.

(6) In case of a co-operative society, interest from Government securities interest on fixed deposits with other banks, etc is income from banking business, hence exempt under section 80P(2)(a)(i): Co-operative banks are eligible for exemption under section 80P(2)(a)(i) on income from the business of banking. Interest from Government securities interest on fixed deposits with other banks, excess collection of interest tax, locker rent, etc were all to be treated as income from banking [Surat District Co-operative Bank Ltd vs. ITO (2003) 262 ITR (AT) 1 (Ahd) (SB)].

(7) The Supreme Court in the case of CIT vs. Ramanathapuram Distt. Coop. Central Bank Ltd [(2002) 255 ITR 423 (SC)] held that (i) interest on securities, (ii) subsidies for the Government, and (iii) dividend received by the assessee, a cooperative society carrying on banking business, were business income of the assessee, and the assessee was entitled to deduction under section 80P(2)(a)(i) in respect thereof.

(8) If income derived by a co-operative society (bank) is from the business of banking, then only it will fall within the exemption, but if it arises from and out of the business with a third party as in the case of investment of surplus assets, the exemption is not available because investment of fluid assets is not a part of the business of the banking. The income must be attributable to banking facility. The investment made to generate income must form part of the circulating capital or stock-in-trade of the (co-operative) bank and the business must have a direct or proximate connection with or nexus to the earnings in order to attract the provisions of section 80P(2)(a)(i) of the Act. Thus, each investment has to be examined, considered and decided on its merits. Thus on the basis of facts found, investments in Indira Vikas Patra was held to be from the funds generated from the banking business [CIT vs. Ratnagiri Dist. Central Co-operative Bank Ltd (2002) 254 ITR 697 (Bom)]. It was made clear that the judgement was confined to the facts of the case as found by tribunal.

(9) Income of co-operative society from collecting electricity charges on behalf of Public Sector Undertaking is exempt: Income earned by a bank, a co-operative society, by way of fee or

commission for collecting electricity charges on behalf of Public Sector Undertaking was income from banking business and thus exempt under section 80P(2)(c)(i).

The expression providing credit facilities to its members has not been explained in the Income-tax Act. On the basis of various case laws meaning of expression 'providing credit facilities to its members' is as under:

(1) In order to claim the benefit of deduction under section 80P(1) read with section 80P(2)(a)(i), the co-operative society should be engaged in carrying on the business of banking or providing credit facilities to its members. As the provision is intended to encourage co-operative societies, a liberal construction should be given to the language employed in the provision. Hence, if a co-operative society is engaged in carrying on the business of providing credit facilities to its members that would suffice to attract the benefit of deduction. Where one of the objects of the assessee co-operative society was to lend money to its members for the purpose of building houses, it was held that the co-operative society shall be entitled to deduction of the interest received over the interest paid by the society as various objects of the society were distinct and independent objects. The activity of the assessee society in making funds available to its members had to be regarded as one of providing credit facilities to its members [CIT vs. Pondicherry Co-operative Housing Society Ltd (1991) 188 ITR 671 (Mad)].

(2) The words 'providing credit facilities' occurring in section 80P(2)(a)(i) of the Act, should be construed as similar or akin to the 'carrying on business of banking', the preceding clause in the same sub-section. The word 'providing credit facilities to its member' means providing credit by way of loan and not selling goods on credit [Kerala Co-operative Consumers' Federation Ltd vs. CIT (1988) 170 ITR 455 (Ker)].

(3) Where the one of the main objects of the co-operative society was providing better quality of seeds of sugarcane, manure and fertilizer, pesticides, agricultural implements, irrigation equipment and arrangement of other articles for agriculture purposes and to provide or to arrange credit facilities for this purpose to the members, it was held section 80P(2)(a)(i) was applicable as one of the main object was to lend to its members and the interest earned by the assessee society from its members qualified for exemption there under [CIT vs. Krishak Sahkari Ganna Samiti Ltd (2002) 258 ITR 594 (All)].

(4) Providing credit facility to members is eligible for deduction and the word member is used in its normal sense and would not include member of member society. Thus providing credit facilities to member of its member societies would not be providing credit facilities to its members [U.P. Co-operative Cane Union Federation Ltd vs. CIT (1999) 237 ITR 574 (SC)].

(5) The expression providing credit facilities, in section 80P(2)(a)(i) takes its colour from the activity of banking. In order that the same may constitute a business, it is necessary that these activities must be the chief source of income. A person who advances loans or supplies goods on credit in connection with and in the course of some other business of manufacture or purchase or sale of goods, etc, cannot be said to be carrying on the business of providing credit facilities [Addl. CIT vs. U.P. Co-op. Cane Union (1978) 114 ITR 70 (All)].

(6) A credit society within the meaning of these provisions can only mean a society which provides credit by way of loans of money to its members and not a society which sells goods on credit [CIT vs. Coral Mills Workers Co-operative Stores Ltd (1977) 106 ITR 868, 871 (Mad)].

(7) The expression providing credit facilities in section 80P(2)(a)(i) would comprehend the business of lending money on interest. It would also comprehend the business of lending services on profit for guaranteeing payments, because guaranteeing payments is as much a part of banking business for affording credit facility as advancing loans [CIT vs. U.P. Co-operative Cane Union Federation Ltd (1980) 122 ITR 913, 916 (All)].

(8) If a society only acts as an agent between its members and a bank without the involvement directly or indirectly in the matter of repayment of loan, the society cannot be termed as engaged in the business of providing credit facilities to its members [CIT vs. Anakapalli Co-op Marketing Society Ltd (2000) 111 ITR 702 (AP)].

Cottage Industry

According to Circular No. 722, dated 19-9-1995—

(a) a cottage industry is one which is carried on a small-scale with a small amount of capital and a small number of workers and has a turnover which is correspondingly limited;

(b) it should not be required to be registered under the Factories Act;

(c) it should be owned and managed by the co-operative society;

(d) the activities should be carried on by the members of the society and their families. For this purpose, a family would include self, spouse, parents, children, spouses of children and any other relative who customarily lives with such a member. Outsiders (i.e. persons other than members and their families) should not work for the society. In other words, the co-operative society should not engage outside hired labour;

(e) a member of a co-operative society means a shareholder of the society;

(f) the place of work could be an artisan shareholder's residence or it could be a common place provided by the co-operative society;

(g) the cottage industry must carry on activity of manufacture, production or processing; it should not be engaged merely in trade, ie, purchase and sale of the same commodity.

It is further clarified that in the case of a weavers' society, so long as weaving is done by the members of the society at their residences or at a common place provided by the society, without any outside labour, such a society will be eligible for deduction under section 80P(2)(a)(ii) even if certain payments have been made to outside agencies for dyeing, bleaching, transport arrangements, etc, provided it satisfies all other conditions necessary for availing of the deduction under section 80P(2)(a)(ii) of the Income-tax Act, 1961.

The Assessing Officer ought to have called for the bye-laws of the assessee to determine (i) whether a weaver could have became a member of apex society and (ii) whether the assessee was engaged in cottage industry. The department was directed to decide the applicability of section 8OP keeping in mind the bye laws of the assessee and the scheme [CIT vs. Rajasthan Raiya Bunkear S. Samiti Ltd (2010) 323 ITR 365 (SC)].

The activity of marketing of agricultural produce of its members, referred to in section 80P(2)(a)(iii), must be confined to the direct produce from agriculture and not to anything manufactured or processed out of it. For instance, paddy is an agricultural produce. If a co-operative society undertakes the sale of paddy grown by its members, the profits derived therefor will gain exemption under this section. But if the society undertakes the sale of rice processed out of such paddy, the exemption is not attracted [South Arcot Dist, Co-op. Supply & Marketing Society Ltd v CIT (1974) 97 ITR 500 (Mad)].

Steps in computing tax liability of Cooperative Societies

The steps are-

Step- I : Compute gross total income, ignoring income exempt from tax u/s. 10 to 13A

Step-II : Deduct permissible deductions u/ss. 80G, 80GGA, 80I, 80I-A 80IB, 80JJA, etc. and 80P as applicable.

Step-III : Apply the tax rates for the relevant Assessment Year to arrive at the tax incidence.

The tax rates applicable are as follows :– The rates of Income-tax are —

Income Range	Rates of tax
1. Where the total income does not exceed ₹ 10,000	10% of the total income
2. Where the total income exceeds ₹ 10,000 but which the does not exceed ₹ 20,000	₹ 1,000 plus 20% of the amount by total income exceeds ₹10,000
3. Where the total income exceeds ₹ 20,000	₹ 3,000 plus 30%, of the amount by which the total income exceeds ₹ 20,000

However, the tax payable by every cooperative society shall be increased by surcharge @ 12% if total income exceeds ₹1 crore, education cess @2% and secondary and higher education cess @ 1%.

The total amount payable as income tax and surcharge on total income exceeding ₹1 crore shall not exceed the total amount payable as income tax on a total income of ₹1 crore by more than the amount of income that exceeds ₹1 crore.

However, from the Assessment Year 2013-14, tax payable cannot be less than 18.5% of "Adjusted Total Income" in some specified cases.

Business Reorganisation in case of Co-operative Bank

As per section 47, the following shall not be treated as transfer:

(1) Any transfer in a business reorganisation, of a capital asset by the predecessor co-operative bank to the successor co-operative bank.

(2) Any transfer by a shareholder, in a business reorganisation, of a capital asset being a share or shares held by him in the predecessor co-operative bank if the transfer is made in consideration of the allotment to him of any share or shares in the successor co-operative bank.

Explanation — For the purposes of clauses (vica) and (vicb), the expressions "business reorganisation", "predecessor co-operative bank" and "successor co-operative bank" shall have the meanings respectively assigned to them in section 44DB.

(3) Special provisions for computing deduction in the case of business reorganization.

Where a business reorganization (ie amalgamation and demerger) of a co-operative bank has taken place during the financial year, the deduction under section 32 (relating to depreciation), section 35D (relating to preliminary expenses), section 35DD (relating to amortization of expenditure in case of amalgamation and demerger) or section 35DDA (relating to amortisation of expenditure incurred on voluntary retirement scheme) shall be allowed in accordance with the following:

1. Deduction for the previous year of business organization (i.e. amalgamation or demerger)

(a) Proportionate deduction to the predecessor co-operative bank [Section 44DB(2)].

The amount of deduction allowable to the predecessor co-operative bank under section 32, section 35D, section 35DD or section 35DDA shall be determined in accordance with the formula—

$$A \times \frac{B}{C}$$

where A = the amount of deduction allowable to the predecessor cooperative bank if the business reorganisation had not taken place;

B = the number of days comprised in the period beginning with the 1st day of the financial year and ending on the day immediately preceding the date of business reorganisation; and

C = the total number of days in the financial year in which the business reorganisation has taken place.

(b) Proportionate deduction to the successor co-operative bank [Section 44DB(3)]:

The amount of deduction allowable to the successor co-operative bank under section 32, section 35D, section 35DD or section 35DDA shall be determined in accordance with the formula—

$$A \times \frac{B}{C}$$

where A = the amount of deduction allowable to the predecessor cooperative bank if the business reorganisation had not taken place;

B =the number of days comprised in the period beginning with the date of business reorganisation and ending on the last day of the financial year; and

C = the total number of days in the financial year in which the business reorganisation has taken place.

2. Deduction to be allowed to the successor co-operative bank for the unexpired period after the year of reorganization [Section 44DB(4)]

If the reorganisation has taken place before the expiry of period specified in section 35D or 35DD or 35DDA (i.e. 5 years), the deduction subsequent to the year of business organization for the unexpired period shall be allowed to the successor co-operative bank in the same manner as would have been allowed to the predecessor bank.

(4) Carry forward and set off of loss and unabsorbed depreciation [Section 72AB].

Where the amalgamation of a co-operative bank or co-operative banks has taken place during the previous year, the successor co-operative bank shall be allowed to set off the accumulated loss and the unabsorbed depreciation, if any, of the predecessor bank as if the amalgamation had not taken place and all the other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly provided the following conditions are satisfied.

Demerger of a co-operative bank [Section 72AB(3)]: Where any demerger of any co-operative bank has taken place during the previous year, the resulting co-operative bank shall be allowed to set off the accumulated loss and unabsorbed depreciation, if any, as under:

(a)	Where the whole of amount of such loss or unabsorbed depreciation is directly relatable to the undertaking transferred to the resulting co-operative bank	The whole of such loss or unabsorbed depreciation		
(b)	Where such accumulated loss or unabsorbed depreciation is not directly relatable to the undertaking transferred to the resulting cooperative bank	Accumulated loss or unabsorbed depreciation of the demerged cooperative bank before demerger	×	$\frac{\text{Assets of the undertaking transferred to resulting co-operative bank}}{\text{Assets of the demerged co-operative bank before demerge}}$

(a) Conditions to be satisfied by the predecessor bank [Section 72AB(2)(a)]:

The predecessor bank should:

(i) have been engaged in the business of banking for three or more years; and

(ii) have held atleast 75% of the book value of fixed assets as on the date of reorganization, continuously for two years prior to the date of business re-organization.

(b) Conditions to be satisfied by the successor co-operative bank (amalgamated co-operative bank or resulting co-operative bank) [Section 72AB(2)(b)].

The successor co-operative bank should:

(i) hold at least 75% of the book value of fixed assets of the predecessor co-operative bank acquired through business reorganisation, continuously for a minimum period of five years immediately succeeding the date of business reorganisation;

(ii) continue the business of the predecessor co-operative bank for a minimum period of five years from the date of business reorganisation; and

(iii) fulfil such other conditions as may be prescribed to ensure the revival of the business of the predecessor co-operative bank or to ensure that the business reorganisation is for genuine business purpose.

- The Central Government may, for the purposes of this section, by notification in the Official Gazette, specify such other conditions as it considers necessary, other than those prescribed under section 12AB(2)(b)(iii), to ensure that the business reorganisation is for genuine business purposes [Section 72AB(4)].
- The period commencing from the beginning of the previous year and ending on the date immediately preceding the date of business reorganisation, and the period commencing from the date of such business reorganisation and ending with the previous year shall be deemed to be two different previous years for the purposes of set off and carry forward of loss and allowance for depreciation [Section 72AB(5)].
- In a case where the conditions specified in section 72AB(2)(b) or notified under section 72AB(4) are not complied with, the set off of accumulated loss or unabsorbed depreciation allowed in any previous year to the successor co-operative bank shall be deemed to be the income of the successor co-operative bank chargeable to tax for the year in which the conditions are not complied with [Section 72AB(6)].

9.8 ASSESSMENT OF TRUSTS

Trusts can be broadly classified into two categories, viz— (i) Public, (ii) Private.

However, there may be trusts which are a blend of both and are known as Public-cum-Private Trusts.

Private Trust

Private Trust is created and governed by Indian Trusts Act, 1882. It may be created inter vivos or by will. If a trust in created by will it shall be subject to the provisions of Indian Succession Act, 1925.

The following are the requisites for creation of a Trust:

(i) The existence of the author/settlor of the Trust or someone at whose instance the Trust comes into existence and the settlor to make an unequivocal declaration which is binding on him.

(ii) There must be a divesting of the ownership by the author of the trust in favour of the trustee for the beneficial enjoyment by the beneficiary.

(iii) A Trust property.

(iv) The objects of the trust must be precise and clearly specified.

(v) The beneficiary who may be particular person or persons.

Unless all the above requisites are fulfilled, a trust cannot be said to have come into existence.

In order to constitute a valid trust the author of the trust must indicate with reasonable certainty—

(a) the intention on his part to create a trust;

(b) the purpose of the trust;

(c) the beneficiaries;

(d) the trust property;

(e) transfer of property to the trust [CIT vs. Brig Kapil Mohan (2001) 252 ITR 830 (Del)]; and

(f) A trust has to be certain as to the beneficiary. Where it is for the benefit of an individual, it is expected that an alternative beneficiary should be provided in case of pre-decease of such individual before maturity of the trust. Where a trust created for two minors-provided for the contingency of predecease of either of them, but not for the contingency of both, the Assessing Officer held the trust to be invalid on the ground of uncertainty as regards the beneficiaries. The High Court in CIT vs. Mehra Trust (2006) 284 ITR 149 (All) found that in such a case, section 77 of the Trust Act would provide for the extinguishment of the trust, so that it will revert back to the settlor. There is, therefore, no uncertainty as presumed by the Assessing Officer. The trust was held to be valid.

In case of private trust, the beneficiaries are individuals or families. Private trusts are further broadly classified into:—

(i) Private specific trust, also referred to as Private Discretionary Trust with beneficiaries and shares determinate in respect of both.

(ii) Private Discretionary Trust where the beneficiaries or their share or either is indeterminate.

Public Trust

Public trusts may be created inter vivos or by will. In the case of Hanmantram Ramnath vs. CIT (1946) 14 ITR 716 (Bom), it was held that although the Indian Trusts Act does not specifically apply to charitable trusts, there are three certainties required to create a charitable trust. They are:

(i) a declaration of trust which is binding on settlor,

(ii) setting apart definite property and the settlor depriving himself of the ownership thereof, and

(iii) a statement of the objects for which the property is thereafter to be held, i.e. the beneficiaries.

It is essential that the transferor of the property viz the settlor or the author of the trust must be competent to contract. Similarly, the trustees should also be persons who are competent to contract. It is also very essential that the trustees should signify their assent for acting as trustees to make the trust a valid one.

When once a valid trust is created and the property is transferred to the trust, it cannot be revoked, if the trust deed contains any provision for revocation of the trust, provisions of sections 60 to 63 of the Income-tax Act will come into play and the income of the trust will be taxed in the hands of the settlor as his personal income.

Trust Deed

For creation of a valid trust, it is not necessary to execute a 'trust deed'. The trust, may be testamentary (deed in writing) or non-testamentary (without a written deed). It is now well settled that a formal deed of trust is not absolutely essential to constitute a trust still less to constitute a legal obligations binding the trustee [Radhasoami Satsang vs. CIT (1992) 193 ITR 321 (SC)].

A charitable trust may be created by words sufficient to show the intention. So long as there is clear manifestation of intention to create a charitable or religious trust and there is a formal vesting of the ownership of the property, the dedication is complete [CIT vs. Sant Baba Mohan Singh (1979) 118 ITR 1015 (All)].

A formal deed is not necessary to constitute a public trust, still less to constitute a legal obligation binding the trustees. In the case of a dedication to a public trust, what is essential is that there should be an unambiguous expression of intention to divest and an actual divestment of the interest of the donor for the benefit of the charity. Such divestiture can be proved by a written document or by other evidence as it is not necessary that there should be a writing to constitute a valid dedication [Jai Narayan Jai Govind vs. Controller of E.D. (1963) 49 ITR (ED) 105, 117 (Mad)].

Where there is no formal document or any such document of trust is available, eligibility is not lost. Although a trust can be oral but for recognition as charitable institution, it should be in writing. Evidential documents like revenue records for lands, property tax receipts, affidavits and such other documents, may be accepted in the place of a formal trust deed. Where the existence of the trust is established by these documents, a formal document was not considered necessary [Patel (AJ) vs. CIT (1974) 97 ITR 683 (Bom)].

Rectification of Trust Deed

Ordinarily it is not possible to rectify the objects of a trust but where there is an ambiguity or mutual mistake in the trust deed, it can be got corrected by a suit for rectification under orders of a court under section 26 of the Specific Relief Act, 1963. But that provision does not enable a modification of the trust deed under the guise of rectification. However, where the author of the trust files a suit under that provision to which the trustee are made a party and the deed is rectified by the decree of the Court, the rectification is binding on the trustee and so will have to be recognised by the Assessing Officer in determining the question of eligibility for exemption under these provisions [Yogiraj Charity Trust vs. CIT (1981) 128 ITR 377 (Del) and approved by the Supreme Court in CIT vs. Kamla Town Trust (1996) 217 ITR 699 (SC)]. However, such rectification deed can have no retrospective effect and will operate prospectively from the date on which such rectification is effected by the Court order.

Further, the Supreme Court in Trustees of H.E.H. The Nizam.'s Pilgrimage Money Trust vs. CIT (2000) 243 ITR 676 (SC) held that a civil court had no jurisdiction for altering the objects of a public trust under section 34 of the Indian Trust Act, 1882 since Indian Trust Act, 1882 was applicable only to private trusts. The deed of charitable trust could be amended only by the Court provided it satisfies the requirement of section 92(3) of the Code of Civil Procedure. As per section 92(3) of Code of Civil Procedure, the Court may alter the original purposes of any express or constructive trust created for public purposes of a charitable or religious nature and allow the property or income of such trust or any portion thereof to be applied cypres in one or more of the following circumstances, namely:—

(a) where the original purposes of the trust, in whole or in part,— (i) have been, as far as may be, fulfilled; or (ii)cannot be carried out at all, or cannot be carried out according to the directions given in the instrument creating the trust, or where there is no such instrument, according to the spirit of the trust; or

(b) where the original purposes of the trust provide a use for a part only of the property available by virtue of the trust; or

(c) where the property available by virtue of the trust and other property applicable for similar purposes can be more effectively used in conjunction with, and to that end can suitably be made applicable to any other purpose, regard being had to the spirit of the trust and its applicability to common purposes; or

(d) where the original purposes, in whole or in part, were laid down by reference to an area which then was, but has since ceased to be, a unit for such purposes; or

(e) where the original purposes, in whole or in part, have, since they were laid down,—

(i) been adequately provided for by other means, or (ii) ceased, as being useless or harmful to the community, or (iii) ceased to be, in law, charitable, or (iv) ceased in any other way to provide a suitable and effective method of using the property available by virtue of the trust, regard being had to the spirit of the trust.

In the case of a private trust, rectification can be done only with the consent of all beneficiaries.

In the context of lingering tax benefits for private trust, one may examine the lingering tax benefits in creation of a private trust, after many of the benefits taken away by anti-avoidance provisions, prescribing maximum rate of tax on income derived by media of private trusts.

The benefits that are still available are as follows:

(1) The second category of trust is the trust created for the benefit of minor children. Notwithstanding the clubbing provision, it has been held that trust in which the minors have the right to the trust property with the income accretion being available only after attaining majority, the aggregation provision will not be applicable. Such a view has been upheld by the Supreme Court in case of CIT vs. M. R. Doshi (1995) 211 ITR 1 (SC) with the result that it has become a safe method to avoid clubbing provisions. But such non inclusion in the year of accrual is hardly a consolidation, since the bunched income during the minority will be taxable in a single year being the year on which the minor attains majority as decided in Ganesh Chhababhai Vallabhai Patel vs. CIT (2002)258 ITR 193 (Guj), where the trustee was held assessable on this basis.

(2) The third advantage is in the creation of trust by a Will. The first proviso (ii) to section 164(1) dispenses with the need for adoption of maximum rates even where the shares of the beneficiaries are indeterminate, if a trust is declared by a Will exclusively for the benefit of dependent relatives and such trust is the only trust so declared by the settlor this could be useful for those persons who have not made any trust.

(3) Unborn children may also be beneficiaries. It may be pointed out that even a trust inter vivos for the benefit of unborn children or prospective wife cannot be aggregated. This decision was followed by Madras High Court in the case of L. Gouthamchand vs. CIT (1989) 176 ITR 442 (Mad.). It was also held so in CIT vs. Brig. Kapil Mohan (Lt. Col.) (2001) 252 ITR 830 (Del). However, it was held in CIT vs. Trustees of Keshav Motha Family Trust (1998) 232 ITR 875(Cal.) that the trust was not valid, when the beneficiary is not in existence like , for example, a would-be wife since the contingency is always there for the person not marrying at all , hence, the importance of providing alternate beneficiaries. In the above case, the trust deed should have spelt out what should be done, if the concerned person did not marry at all. Care must be taken to see that every eventuality including demise of the child before marriage is covered and alternatives provided.

(4) After the provision of maximum rate of tax, where the beneficiary is not identifiable, it is likely that the revenue may seek to apply the maximum rate of tax under section 164, the possible argument being that the income during the year is not specifically receivable on behalf of or for the benefit of any one person on the ground that the future wife or unborn child has not come into existence during accounting year. Such a view is being taken, though the argument of revenue can be resisted on the ground that alternative beneficiaries have been provided in the event of failure of the provisions relating to unborn child or a future wife. At any rate, the fact that such income is carried over and at the time of accretion there is no definiteness does not mean that the shares are not specified, because definiteness is ensured at the time when the contingency provided for occurs or on determination of the trust.

The exemption under section 11 is allowed to the following:

(1) a charitable trust,

(2) a religious trust.

However, the word 'trust' as used in the context of sections 11 to 13 of the Income-tax Act, includes in addition to the 'trust' any other legal obligation.

Trust itself is a legal obligation, as the trustees are legally bound to apply the income of the trust in the manner and for the purposes specified by the author of the trust and it includes the following:

(i) Property of the estate of deceased held by executor(s) under a legal obligation.

(ii) Section 8 'Companies' or 'Guarantee Companies'. Such companies are also holding the properties under legal obligation.

(iii) Muslim Wakfs.

(iv) Religious Endowments under the Hindu Law.

(v) Institutions registered under the Societies Registration Act, 1860 as the properties of the society are held under a legal obligation.

(vi) Bar Councils, Chamber of Commerce, endowments, monasteries, maths, etc. are all instances where the 'property is held under legal obligation'.

Where the assessee, a statutory body, engaged in the activities of development and maintenance of ports in the State of Gujarat, made an application for registration under section 12A, which was rejected by the Commissioner on the ground that the assessee could not be considered as lawful trust within the meaning of term trust, it was held, that the assessee was a charitable institution and eligible for registration as there was no mention of either trust or institution in the definition of person in section 2(31) and merely because it was termed as a local authority, it would not be a bar to its registration. The assessee was an institution within the meaning of section 12AA(1). Section 12A did not make any distinction between trusts and institutions. If an assessee is an institution whose object is charitable as defined under section 2(15), the institution would be entitled to registration under section 12A. In this case, the object of the assessee was to maintain and develop ports in the State of Gujarat which was an object of general public utility [CIT vs. Gujarat Maritime Board (2007) 289ITR 139 (Guj)].

Similarly, an institution established for regulating, procurement and supply of agricultural produce was accepted by the Tribunal as an object of general public utility so as to be eligible for registration as charitable institution under section 12A. The arguments of the department that such committee should have been registered as a trust to qualify for exemption was dismissed because there is no such requirement under the Act [CIT vs. Agricultural Produce & Marketing Committee (2007) 291 ITR 419 (Bom)].

For claiming exemption under section 11, the following conditions must be satisfied:

(a) Trust must have been created for any lawful purpose;

(b) Such trust/institution must be for charitable or religious purposes.

(c) The property from which income is derived should be held under trust by such charitable or religious trust/institution.

(d) The accounts of the trust/institution should be audited for such accounting year in which the total income, before giving effect to provisions of section 11 or 12, exceeds the maximum amount which is not chargeable to tax and the person in receipt of the income should obtain an audit report in Form No. 10B [Rule 17B] and furnish the same along with the return of income.

Filing of audit report on or before the due date is directory and not mandatory: In the case of CIT vs. Hardeodas Agarwalla Trust (1992) 198 ITR 511 (Cal), it has been held that an omission to file audit report alongwith the return of income may be rectified by filing the report at a later stage before assessment is completed. However, audit report shall have to be filed for claiming exemption.

Failure to file the audit report in time need not deprive the assessee of the benefit of exemption, since it was only a technical lapse [CIT vs. Shreyas Nidhi, Swasti Nidhi, Venu Nidhi and Swasthya Nidhi (2002) 258 ITR 712 (Guj)].

Where for reasons beyond the control of the assessee, some delay has occurred in filing the audit report, the exemption, as available to such trust under sections 11 and 12, may not be denied merely on account of delay in furnishing the auditor's report and the Assessing Officer should record reasons for accepting a belated audit report [Instruction No. 1/1148 — CBDT F. No. 257/482/77-IT (Part), dated 9-2-1978].

(e) The trust must get itself registered with the Commissioner of Income-tax within the prescribed time.

For claiming benefit under section 11(1)(a), registration under section 12A (Now section 12AA) is a condition precedent [U.P. Forest Corporation & Anr vs. DCIT (2008) 297 ITR 1 (SC)].

(f) Where the 'property held under a trust' includes a business undertaking, the provisions of section 11(4) shall be applicable. On the other hand, if the trust wishes to carry on business, the profits or gains earned from such business shall not be exempt under section 11, unless the business is incidental to the attainment of the objectives of the trust/institution and separate books of account are maintained by such trust and institution in respect of such business.

(g) The charitable trust created on or after 1-4-1962 should satisfy the following further conditions:

(i) it should not be created for the benefit of any particular religious community or caste;

(ii) no part of the income of such charitable trust or institutions should enure directly or indirectly for the benefit of the settlor or other specified persons; and

(iii) the property should be held wholly for charitable purposes.

However, the religious trust created before or after 1.4.1962 may not satisfy the condition (i) mentioned above, but if it is created after 1-4-1962, it should satisfy the conditions (ii) and (iii) mentioned above.

Thus, the charitable trust or religious trust created before 1-4-1962 can be partly public charitable or religious trust and partly private charitable/religious trust but charitable or religious trust created after 31-3-1962 should be wholly for charitable or religious purposes.

(h) The funds of the trust should be invested or deposited in the permissible forms and modes prescribed in section 11(5).

According to section 2(15), charitable purpose includes relief of the poor, education, medical relief and the advancement of any other object of general public utility.

With a view to limiting the scope of the phrase 'Advancement of any other object of general public utility', the Finance Act, 2008 has inserted Proviso 1 to section 2(15) w.e.f. assessment year 2009-10 so as to provide that 'the advancement of any other object of general public utility' shall not be a charitable purpose if it involves the carrying on of—

(a) any activity in the nature of trade, commerce or business or,

(b) any activity of rendering of any service in relation to any trade, commerce or business,

for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity, or the retention of such income, by the concerned entity.

Amendment made by the Finance Act, 2010, w.r.e.f. assessment year 2009-10

The Finance Act, 2010 has inserted second proviso to section 2(15) w.r.e.f. assessment year 2009-10 (i.e. from the assessment year from which proviso 1 is applicable) to avoid hardship faced by the organizations which receive sundry consideration from the above commercial activities. The Act has therefore amended section 2(15) to provide that "the advancement of any other object of general public utility" shall continue to be a "charitable purpose" if the aggregate value of receipts from any activity in the nature of trade, commerce or business, or any activity of rendering any service in relation to any trade, commerce or business do not exceed ₹10 lakh in the previous year (increased to ₹2,500,000 by the Finance Act, 2011, w.e.f. assessment year 2012-13).

As per amendment made by the Finance Act, 2012 where the commercial receipt of the above said charitable trust exceeds ₹25,00,000 in any previous year, there will be no need to cancel the registration of such trust but that exemption under sections 11 and 12 shall not be allowed for that previous year.

Educational Institution

The Uttarakhand High Court in the case of CIT vs. Queens' Educational Society (2009) 177 Taxman 326 (Uttarakhand) held that where an educational institution generates surplus and makes investment in fixed assets which were properties of this assessee exemption should be refused.

However, the Punjab and Haryana High Court in a very elaborate judgement where the above case of Uttarakhand High Court was also considered decided that even if there remains a surplus at the hands of the educational institution, it would be entitled to exemption under section 10(23C)(vi) provided that educational institution solely exists for educational purposes; capital expenditure has to be deducted from the gross income of the educational institution in determining whether 85 per cent of the income has been applied for its objects [Pinegrove International Charitable Trust & Ors. vs. UOI & Ors (2010) 37 DTK (105) (P&H)].

The assumption, that for exemption there should not be any surplus and if it is otherwise the institution society exists for profit and not charity, is not justified. Thus, exemption cannot be rejected merely because there is a surplus. Vanita Vishram Trust (2010) 327 ITR 121 (Bom); Maa Saraswati Trust 194 TM 84 (HP) and Pinegrove International Charitable Trust vs. UOI & Ors (2010) 327 ITR 73 (P&H) followed) [St. Lawrence Educational Society vs. CIT (Delhi High Court).

Merely, because an educational institution accumulates income, it does not go out of consideration of section 10(23C)(vi). The exemption can be lost if application of income is for purpose other than education [Maa Saraswati Educational Trust vs. UOI (2010) 194 Taxman 84 (HP)].

Charitable Organisation

A charitable organisation is ordinarily formed by way of a trust or a company limited by guarantee under section 8 of the Companies Act, 2013 or a society under the Societies Registration Act, 1860 (Central) or under a State Act in case there is one. As far as the tax angle in concerned, it makes no difference whether the charitable organisation is formed by way of trust, a company or a society.

A trust can be oral but for recognition as a charitable institution, it should be in writing and should have three certainties:

(i) certainty as regards property which is the object of the trust;

(ii) the object themselves; and

(iii) the beneficiaries for whom they are intended.

Forming a formal trust with specified objects which are charitable with a small contribution by the settlor and appointing trustees with provision of future trustees is a normal form of creation of charitable institution. The advantage of trust is that it is in the control of few persons who are appointed as trustees and not elected. They could be nominated for life or lesser period.

Even a settlor can himself be a sole trustee or one of the trustees.

A Wakf under Mohammaden Law is created under the Wakf Act, 1995 (previously under the Musalman Wakf Act, 1923). The difference between trust law and wakf is that the latter is created either by a Muslim or by a competent court by dedication of immovable property to God for religious, pious or charitable purposes. Such wakfs are managed by Mutawali whose powers are at par with that of trustee.

Some States have their own laws relating to public trusts as in Andhra Pradesh, Gujarat, Maharashtra, Rajasthan and have regulatory agencies under the respective laws. It would be necessary for the trust located in the respective States to conform to these laws as well but non-compliance may not always means that the trust is invalid or that they would not be eligible for exemption.

A public limited company should be at par with section 8 of the Companies Act provided the following conditions are satisfied:—

(i) The objects of the company should conform to the requirement of law.

(ii) It should not be allowed to distribute dividends to the shareholders.

(iii) Surplus, if any, will have to be utilised for its objects i.e. for charitable purposes.

The following Acts has been decided as acts for charitable purpose by the various courts and authorities:

Promotion of sports: The board has clarified that promotion of sports and games can be considered to be a charitable purpose within the meaning of section 2(15) of the Income-tax Act, 1961. Therefore, an association or institution engaged in promotion of sports and games can claim exemption under section 11 of the Income-tax Act, 1961, even if it is not approved under section 10(23) of the Act relating to exemption from tax of sports associations and institutions having their objects as the promotion, control, regulation and encouragement of specified sports and games [Circular No. 395, dated 24th September, 1984].

Relief of poor: The relief of the poor must not be relief to a body of private individuals but must have a public character [Mercantile Bank of India (Agency) Ltd (1942) 10 ITR 512 (Cal)]. Therefore trusts for the relief of poverty of poor relatives of the settlor were not for a charitable purpose since no element of public benefit was involved [CIT vs. Jamal Mohd. Sahib (1941) 9 ITR 375 (Mad)].

Activity of giving micro finance and earning Interest is charitable: Where an assessee is registered under section 8 of Companies Act, 2013, it in itself shows that the company intends to apply its profit in promoting charity. And where the object of the assessee states that it shall promote micro finance services to poor person and help them arise out of poverty, mere surplus from such micro finance service cannot by itself be a ground to say that no charitable purpose exists. Followed Thanthi Trust (2001) 247 ITR 785 (SC) and Agricultural Produce and Market Committee (2007) 291 ITR 419 (Bom) [Dish India Micro Credit vs. CIT (ITAT-Del).

Education: What education connotes in section 2(15) is the process of training and developing the knowledge, skill, mind and character of students by normal schooling [Sole Trustee, Loka Shikshana Trust vs. CIT (1975) 101 ITR 234, 241 (SC); Addl. CIT vs. Victoria Technical Institute (1979) 120 ITR 358, 370-1 (Mad)]. Education, in order to be charitable, must relate to the public and a trust created for the education of the members of a family or the descendants of a certain named individual are not for charitable purposes [D.V. Arur vs. CIT (1945) 13 ITR 465 (Bom)]. Though newspapers have an educative value, advancement of education results only indirectly. Advancement of education resulting indirectly does not come under the head of education [CIT vs. Sole Trustee, Loka Shikshana Trust (1970) 77 ITR 61, 75 (Mys)].

Where the objects of society make it abundantly clear that the society exists for charitable purpose and the activities of the society includes letting out of the properties to the educational institution and there was a concurrent finding of the fact on the part of the Commissioner (Appeal) and the ITAT that the rental income earned by the society is being utilised again for the purpose of imparting education by maintaining the buildings and constructing new building for the same purpose, it was held that in this case charitable purpose is not lost and it cannot be said that the assessee is not entitled to exemption claimed by it under section 11 of the Act [CIT vs. Jyoti Prabha Society (2009) 310 ITR 162 (Uttarakhand)].

A Government company meant exclusively for publication and selling text books to the students as per the norms prescribed and approved by the Education Department, could well be treated as an educational institution even though it is not imparting formal education [Assam State Text Book Production and Publication Corporation Ltd. vs. CIT (2009) 319 ITR 317 (SC)].

Any other object of general public utility: General means pertaining to a whole class; public means the body of people at large including any class of the public; and utility means usefulness. Therefore, the advancement of any object of benefit to the public or a section of the public as distinguished from an individual or a group of individuals would be of charitable purpose [CIT vs. Ahmedabad Rana Caste Association (1973) 88 ITR 354 (Guj)].

The expression object of general public utility, however, is not restricted to objects beneficial to the whole mankind. An object beneficial to a section of the public is an object of general public utility. To serve a charitable purpose, it is not necessary that the object should be to benefit the whole of mankind or even all persons living in a particular country or province. It is sufficient if the intention is to benefit a section of the public as distinguished from specified individuals. The section of community sought to be benefited must undoubtedly be sufficiently defined and identifiable by some common quality of a public or impersonal nature. Where there is no common quality uniting the potential beneficiaries into a class, it might not be regarded as valid charitable trust [CIT vs. Andhra Chamber of Commerce (1965) 55 ITR 722 (SC)].

State Bar Council has been held to be a body constituted for general public utility although its objects are beneficial to section of a public [CIT vs. Bar Council of Maharashtra (1981) 130 ITR 28 (SC)].

The Satsangis of Radhaswami Satsang Sabha being followers of one religion, are cross-section of the public, and a charitable trust for the benefit of Satsangis as such must be deemed to be a trust for an object of a general public utility [CIT vs. Radhaswami Satsang Sabha (1954) 25 ITR 472 (All)].

A trust created for charitable or religious purposes will enjoy the exemption although it is named after a private person [CWT vs. HEH The Nizam Supplemental & Religious Endowment Trust (1973) 89 ITR 80 (AP)].

Where the primary objects are, charitable, exemption cannot be denied if a subsidiary object is found to be non-charitable but which is intended to subserve the religious and charitable objects [Yograj Charity Trust vs. CIT (1976) 103 ITR 777 (SC)].

The object of an association of chartered accountants to organise seminars, conferences and workshops to educate people on commercial laws, tax laws, auditing accounting, direct and indirect taxes, is an object of general public utility, so as to entitle such society to be treated as a charitable institution and therefore eligible for registration under section 12A and exemption under section 11 [CIT vs. Jodhpur Chartered Accountants Society (2002) 258 ITR 548 (Raj)].

Where the main object is to promote export of diamonds and develop the trade and export market and for this purpose a diamond bourse is established to facilitate liaison between industries in India and abroad, so that there could be a modem diamond market, the object is one of general public utility and the company, which was formed for the purpose is entitled to exemption [Director of Income-tax vs. Bharat Diamond Bourse (2003) 259 ITR 280 (SC) following Addl. CIT vs. Surat Art Silk Cloth Manufacturers Association (1980) 121 ITR 1 (SC)].

The Finance Act, 2008 has inserted proviso to section 2(15) w.e.f. assessment year 2009-10 so as to provide that 'the advancement of any other object of general public utility' shall not be a charitable purpose if it involves the carrying on of—

(a) any activity in the nature of trade, commerce or business or,

(b) any activity of rendering of any service in relation to any trade, commerce or business,

for a fee or cess or any other consideration, irrespective of the nature of use or application of the income from such activity, or the retention of such income, by the concerned entity.

However, the above proviso shall not apply if the aggregate value of the receipts from such commercial activities is ₹1,000,000 or less (increased to ₹2,500,000 by the Finance Act, 2011, w.e.f. assessment year 2012-13).

Subject to the provisions of sections 60 to 63, the following incomes of a religious or charitable trust or institution are not included in its total income:

(a) As per section 11(1)(a), income derived from property held under trust, wholly for charitable and religious purposes, shall be exempt—

  (i) to the extent such income is applied in India for such purposes; and

  (ii) where any such income is accumulated or set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of 15% of the income from such property,

(b) As per section 11(1)(b), income derived from property held under trust in part only for such purpose, shall be exempt:

  (i) to the extent such income is applied in India for such purposes, provided, the trust in question is created before the commencement of Income-tax Act, 1961 i.e. before 1-4-1962; and

  (ii) where any such income is finally set apart for application to such purposes in India, to the extent to which the income so accumulated or set apart is not in excess of 15% of the income from such property.

(c) As per section 11(1)(c),—

  (i) Income derived from property held under trust, created on or after 1-4-1952 for charitable purpose which tends to promote international welfare in which India is interested, shall be exempt to the extent to which such income is applied to such purpose outside India. Religious trusts are not covered here.

  (ii) Income derived from property held under a trust for charitable or religious purposes, created before 1-4-1952, shall be exempt to the extent to which such income is applied to such purposes outside India.

In the above two cases, it is necessary that the Board, by general or special order, has directed in either case that it shall not be included in the total income of the person in receipt of such income.

(d) As per section 11(1)(d), income in the form of voluntary contributions made with a specific direction, that they shall form part of the corpus of the trust or institution, shall be fully exempt. The condition that at least 85% of the income should be applied during the previous year in which it is earned is not applicable in this case.

The essential condition of section 11(1) is that the property itself must be held under trust. That section does not say anything about the income (from the property) held under trust, etc. Therefore, unless the property itself is held under trust the exemptions under the section does not come into play [Cricket Association of Bengal vs. CIT (1959) 37 ITR 277 (Cal); Delhi Stock Exchange Association Ltd vs. CIT (1980) 126 ITR 532 (Del)]. It is not sufficient that the property is indirectly responsible for the income; it is necessary that the income must directly and substantially arise from the property held under trust. The property must be the effective source from which the income arises [J.K. Trust vs. CIT (1953) 23 ITR 743 (Bom)].

Section 11(1) does not apply to cases where a trust or legal obligation is not created on any property but only the income derived from any particular property or source is set apart and charged for a charitable or religious purpose [Raja P.C. Lall Chaudhry vs. CIT(1957) 31 ITR 226 (Pat)]. Where a religious head, a Swamiji was teaching and accepted offerings, it cannot be said that the money received from offering is derived from a property held under a trust or under other legal obligation [Swami Narsingh Giri vs. CIT(1971) 79 ITR 544 (All)].

But bhents made by the followers to the deity (Radhaswami Dayal) in pursuance of the dictates of their faith and in accordance with the constitution of the Sabha vested in the Sabha under a legal obligation wholly for religious or charitable purposes would be exempt [CIT vs. Radhaswami Satsang Sabha (1954) 25 ITR 472 (All); CIT vs. Avtar Singh (Babd) (1972) 83 ITR 738 (Del)].

Where, the trust deed creates an overriding title in the beneficiaries thereunder (viz, the various cross-sections of the public covered by it to require that the income from the properties which are made the subject-matter of the trust be utilised in the manner set out therein and in no other manner, after the execution of the trust deed, the properties are no longer held by the assessee as the absolute owner thereof; they are held by the assessee under trust and a legal obligation to apply the income exclusively for charitable purposes, thus attracting the provisions for exemption contained in the Act [Moti Lal Chhadami Lal Jain vs. CIT (1991) ITR 1 (SC)].

Treatment of voluntary contributions made to trust with a specific direction that it shall form part of corpus of the trust

Any voluntary contribution received by the trust with a specific direction that it shall form part of the corpus of the trust is fully exempt under section 11(1)(d) and the condition that at least 85% of the income should be applied during the previous year in which it is earned is not applicable in this case.

The question, whether a particular contribution has been towards corpus or otherwise would depend upon the facts of the case. Where the contribution is made for a specific purpose and not for general purpose, it can be understood that the donation is towards corpus [CIT vs. Shri Plot Swetamber Murti Pujak Jain Mandal (1995) 211 ITR 293 (Guj)]. Where the amount was given with specific direction for construction of Wadi, it shall be treated as having been made for corpus [CIT vs. Sthanakvasi Vardhman VanikJain Sangh (2003) 260 ITR 366 (Guj)].

Donations collected by the assessee, in a donation box in the face of its appeal that the amounts so collected would be used for the construction of a building can be considered as carrying specific directions for being used for construction of building and therefore, it is to be treated as donations toward corpus as such amount did not constitute income for the purpose of section 11 or 12 [Shree Mahadevi Tirath Sharda Ma Seva Sangh vs. ITO (2010) 133 TTJ 57 (Chd)(UO)].

Treatment of corpus donations: Corpus donations cannot be treated as income in view of the exception under section 12, so that such corpus donations need not be applied for the objects as required for other donations. It is sufficient, if the income therefrom is applied. It is not unusual for trusts to receive such donations for specified purposes not available for application at the discretion of the trustees according to the objects of the trust, so that the main trust need not lose its right to exemption either for non-application or even for the reason that the specific object of such tied-up donation does not fall within the ambit of the objects of the trust [CIT vs. Sthanakvasi Vardhman VanikJain Sangh (2003) 260 ITR 366 (Guj)].

As per section 12, Voluntary Contributions received by a trust/institution created wholly for charitable or religious purposes (not being contributions made with a specific direction that they shall form part of the corpus of the trust or institution) shall be deemed to be income derived from property held under trust wholly for charitable or religious purposes and the provision of section 11 (including the application of atleast 85% of income) and the provision of section 13 shall apply accordingly. Thus as per Explanation 1 to section 11 in computing the 15% of income which may be accumulated or set apart, such voluntary contributions, shall be deemed to be part of the income. It may be noted that if such voluntary contributions are received by a trust created partly for charitable or religious purposes, the exemption shall not be available.

For claiming exemption under section 11, atleast 85% of the income should be applied during the previous year towards the purpose for which the trust has been created.

Income applied during the previous year for this purpose includes the following:

(a) income actually applied during the previous year for charitable and religious purposes,

(b) income deemed to have been applied for charitable or religious purposes in India during the previous year.

Applied, in this context, means that the income is actually applied for the charitable or religious purposes of the trust [H.E.H. Nizams Religious Endowment Trust vs. CIT (1966) 59 ITR 582, 588 (SC)]. The word applied need not necessarily imply spent. Even if an amount is irretrievably earmarked and allocated for the charitable or religious purpose(s), it may be deemed to have been applied for its purposes [CIT vs. Radhaswami Satsang Sabha (1954) 25 ITR 472, 522-3 (All); CIT vs. H.E.H. The Nizams Charitable Trust (1981) 131 ITR 497, 501-02 (AP)]. A mere credit entry in the books of the trust in the expectation of future income is not sufficient [Nachimuthu Industrial Association vs. CIT (1980) 123 ITR 611 (Mad)] but a credit entry made to allocate already earned income followed by some payments made in the year was held proper application [CIT vs. Thanthi Trust (1982) 137 ITR 735 (Mad)].

It is not necessary that in order to treat any amount as 'application' within the meaning of these provisions, the particular amount should be spent for charitable purposes only after the trust has earned profits.

Application of income may not result into revenue expenditure: Where income is applied for purchase of a capital asset, it would still be application of income to the charitable purpose. If the assessee invests in construction of a building, which is a permissible investment under section 11(5) of the Income-tax Act, so as to augment its resources for fulfilling the objectives of the institution, there is no doubt that such outlay would qualify as income applied for charitable purposes [CIT vs. St. George Parana Church (1988) 170 ITR 62 (Ker)].

Assessee trust established for the purpose of running hospitals, nursing home etc, spending the income for construction of hospital building, is an application of income for the objects of running hospitals and entitled to exemption [CIT vs. Mool Chand Sharbati Devi Hospital Trust (2010) 41 DTR(All) 153].

Repayment of a debt incurred for charitable purposes by a charitable trust and loans advanced by educational trusts are application of income:

Section 11 of the Income-tax Act requires 100% of the income of a charitable and religious trust to be applied for religious and charitable purposes to be entitled to the exemption under the said section. Two questions have been considered regarding the application of income:

(i) Where a trust incurs a debt for the purposes of the trust, whether the repayment of the debt would amount to an application of the income for the purposes of the trust? and

(ii) Whether loans advanced by an educational trust to students for higher studies would be treated as application of income for charitable purposes?

Board has decided that repayment of the loan originally taken to fulfil one of the objects of the trust will amount to an application of the income for charitable and religious purposes. As regards the loans advanced for higher studies, if the only object of trust is to give interest-bearing loans for higher studies, it will amount to carrying on of money- lending business. If, however, the object of the trust is advancement of education and granting of scholarship loans as only one of the activities carried on for the fulfilment of the objectives of the trust, granting of loans, even interest-bearing, will amount to the application of income for charitable purposes. As and when the loan is returned to the trust, it will be treated as income of that year [Circular No. 100, dated 24-1-1973].

When the amount is returned by the beneficiaries of the trust, the receipt in the hands of the trust can only be its income of the years in which it is received [CIT vs. Cutchi Memon Union (1985) 155 ITR 51 (Karn)].

Repayment of loan taken for construction of a building by the assessee for the purpose of augmenting its funds shall qualify as income applied for charitable purpose [CIT vs. Janmabhoomi Press Trust (2000) 242 ITR 703 (Karn)].

Repayment of loan taken by the charitable institution for construction of commercial complex so as to augment the resources of the trust would amount to application of income [Director of Income-tax (Exemption) vs. Govindu Naicker Estate (2009) 315 ITR 237 (Mad)].

Repayment out of rental income of the funds borrowed for construction of the building was to be treated as application of income for charitable purpose and thus the assessee shall be eligible for exemption under section 11. It was further pointed out that as and when the loans are discharged and the assessee becomes free to utilize the rental income, the trust will apply the same for charitable purpose set out in the trust deed and that it is at that juncture that the Assessing Officer could insist that the application of the income be for the purpose mentioned in the trust deed [Director of Income Tax (Exemption) vs. Span Foundation (2009) 178 Taxman 436 (Del)].

Payment of taxes held application: Expenditure by way of payment of tax out of current year's income has to be considered as application for charitable purposes because the payment has been made to preserve the corpus, the existence whereof is essential for the trust itself [CIT vs. Janaki AmmalAyya Nadar Trust (1985) 153 ITR 159 (Mad)].

Donation by one charitable trust to another amounts to application: When a charitable trust donates its income to another charitable trust, the provisions of section 11(1)(a) can be said to have been met by the donor-trust and the donor-trust can be said to have applied its income for charitable and religious purposes. However w.e.f. assessment year 2003-04, any donation made out of income referred to section 11(1)(a) or (b) read with explanation to that sub-section which is not applied, but is accumulated or set apart either during the period of accumulation or thereafter to any trust or institution registered under section 12AA or to any fund, institution or trust or any university or other education institution or any hospital or other medical institution referred to in section 10(23C)(iv), (v), (vi) or (via) shall not be treated as application of income for charitable or religious purposes.

It has been decided by the Board that as the law stands at present, the payment of a sum by one charitable trust to another for utilisation by the donee-trust towards its charitable objects is proper application of income for charitable purpose in the hands of the donee-trust; and the donor-trust will not lose exemption under section 11 of the Income-tax Act, 1961, merely because the donee-trust did not spend the donation during the year of receipt itself [Extracted at (1988) 172 ITR 709 (Guj)].

Where loans were advanced to economically weaker persons for housing purposes in pursuance of the objects of a public charitable trust and such amounts are subsequently written off, the amount so written off could be treated as application for the object of general public utility [CIT vs. Sacred Heart Church (2005) 278 ITR 180 (Guj)].

Other cases of application: Other cases holding that in the facts of those cases, the expenditure or outgoing did constitute application of income for charitable purposes, are:

(1) CIT vs. Kannika Parameswari Devasthanam & Charities (1982) 133 ITR 779 (Mad) [capital expenditure incurred on improving or maintaining property of the trust].

(2) Application of surplus funds in construction of additional buildings with the purpose of letting them out and utilising the rent for the objects of the trust would amount to applying funds for religious and charitable purposes [St. George Parana Church (1988) 170 ITR 62 (Ker)].

(3) Spending on production and exhibition of a film, as also spending for the construction of a overhead tank on land belonging to the legal heirs of the founder of the assessee-trust is application [CIT vs. Divine Light Mission (1990) 183 ITR 56 (Del)].

(4) Expenditure on salaries and miscellaneous expenses for the purpose of carrying out the objects and purposes of the trust must be considered as application for charitable purposes [CIT vs. Birla Janahit Trust (1994) 208 ITR 372 (Cal)].

(5) Where the assessee is a charitable institution, legal expenses incurred by the assessee-association for defending the persons running the association against criminal charges are allowable as a permissible deduction while computing the total income of the assessee association [Ananda Marga Pracharaka Sangha vs. CIT (1996) 218 ITR 254 (Cal)].

(6) Income for the purposes of section 11 should be understood in its commercial sense and, therefore, loss on sale of shares to make investments in specified investments within the meaning of section 11(5) has to be treated as application of income of the trust [Chidambaram Chettiar Foundation vs. ITO (1991) 39 TTJ 82 (AT)(Mad)].

As per clause (2) of the Explanation to section 11(1), if the income applied to charitable or religious purposes during the previous year falls short of 85% of the income derived during the year either:

(a) for the reason that whole or part of the income has not been received during the previous year or

(b) for any other reason,

then the charitable trust has been given the option to spend such income for charitable or religious purposes in the following manner:

(i) In case of (a) either during the previous year in which the income is so received or in the immediately following previous year. Example, if the income of previous year 2014-15 is received on 15-4-2016, such income should be applied for charitable or religious purposes either during previous year 2016-17 and/or 2017-18.

(ii) In case of (b) during the previous year immediately following the previous year in which the income was derived. Example, if the income is received on 28-1-2015 and it could not be spent in the previous year 2014-15 for any reason, it could be applied in the next previous year i.e. 2015-16.

To avail the facility of the above extended period of application of income, the trust has to excise such option before the expiry of the time allowed under section 139(1) for furnishing the return of Income in such form or manner as may be prescribed.

If such option is exercised by the trust, such income shall be deemed to have been applied for charitable and religious purposes during the previous year in which the income is earned, though it is actually spent at a later date. In this case, as such income is deemed to have been applied during the previous year in which it was derived, it shall not be treated as application of income for charitable purposes, of the previous year in which it is actually spent.

Where the income for which an option has been exercised by the assessee is not actually applied within the prescribed time, it shall be treated as the income of the previous year immediately following the year of receipt, in case of reason (a) mentioned above.

In case of reason (b) it will be treated as the income of the previous year immediately following the previous year in which such income was derived.

The amount of depreciation debited to the accounts of the charitable institution has to be deducted to arrive at the income available for application to charitable and religious purposes [CIT vs. Sheth Manilal Ranchhoddas Vishram Bhavan Trust (1992) 198 ITR 598 (Guj), CIT vs. Bhomka Public Welfare Trust (1999) 240 ITR 513 (Cal)].

As per newly inserted sub-Section (6) of section 11 of the income tax Act, where any income is required to be applied or accomulated or set apart for application, then, for such purposes the income shall be determined without any deduction or allowance by way of depreciation or otherwise in respect of any assets, acquisitions of which has been claimed as an appliation of income under this section in the same or any other previous year.

As per amended Section 115BB(1)(ii), the amount of income-tax Act, with which the assessee would have been chargeable had his total income been reduced by the aggregate of anonymous donations received in Excess of the amount referred to in sub-clause (A) or sub-clause (B) of clause (i), as the case may be.

Depreciation is also application of income: (a) Depreciation shall be allowed on the assets, the cost of which had been fully allowed as application of income under section 11.

(b) Depreciation is allowable on assets received on transfer when the assessee had not incurred the cost of acquiring the assets, even though it has already treated as application of income in the hands of the transferor trust [CIT vs. Institute of Banking Personnel Selection (IBPS) (2003) 264 ITR 110 (Bom)].

Where in the light of Escorts Ltd vs. UOI (1993) 199 ITR 43 (SC) a charitable trust was disallowed the depreciation by the Assessing Officer on the ground that since the income of the assessee was exempt from tax under section 11, allowing depreciation would amount to conferring double benefit as the assessee has already claimed deduction of the cost of the asset treating as application of income, it was held that in Escorts Limited's case, the Supreme Court rendered decision in the context of section 35(1)(iv), which barred depreciation under section 32 for an equipment acquired for research, the cost of which had been allowed as deduction under section 35. In case of charitable trust, the depreciation is reduced from the income for determining the percentage of funds which have to be applied for the purpose of the trust. Hence, distinguishing the Escorts Ltd case, it was held that double deduction is not being given in allowing claim of depreciation for computing income for purposes of section 11 [CIT vs. Market Committee, Pipli (2011) 330 ITR 16 (P&H). CIT vs. Tiny Tots Education Society (2011) 330 ITR 21 (P&H)].

Assessee charitable trust is entitled to the claim for depreciation on the assets owned by it. If depreciation is not allowed as a necessary deduction in computing the income of a charitable trust, then there would be no way to preserve the corpus of trust [CIT vs. Shri Gujarati Satnaj (Regd.) (2011) 64 DTR 76 (MP)].

Where a trust or institution expends or applied more than its income, it can only mean that such excess amount is from corpus or future income. The intention whether from corpus or future income should be manifest from the accounts. If such deficit is debited to corpus, it should ordinarily mean that the coipus is used or applied for the purpose of the trust so that there can be no objection to such use. On the other hand, if the deficit is merely carried forward, it would be clear, that the intention is to absorb such deficit against future income.

When a trust had spent in excess of its income for the current year resulting in a deficit which was carried forward to the next year, it was held that in considering the application of income for the next year, the carried forward deficit was first to be set off against the income of the subsequent year [CIT vs. Maharana of Mewar Charitable Foundation (1987) 164 ITR 439 (Raj)].

Adjustment of expenses incurred by the trust in the earlier years against the income earned by the trust in the subsequent year will have to be regarded as application of income by the trust in the subsequent year [CIT vs. Institute of Banking Personnel Selection (IBPS) (2003) 264 ITR 110 (Bom). Set off or carry forward of loss of earlier years, or in other words, deficit of earlier years can be set off against surplus of the succeeding year. See also CIT vs. The Trustees of Seth Merwarjee Framji Panday Charitable Fund (2003) 177 Taxation 19, 20 (Bom)].

Excess expenditure of an earlier year can be adjusted against income of subsequent year and such adjustment is to be treated as application of income in subsequent year [CIT vs. Shri Plot Swetamber Murti Pujak Jain Mandal (1995) 211 ITR 293 (Guj)].

The excess of application of the current year/past year can be set off against the income of subsequent/ current year [Raghuvanshi Charitable Trust and others vs. DIT (2011) 221 Taxation 250 (Del)].

Expenditure incurred in the earlier year can be met out of the income of the subsequent year and utilization of such income for meeting the expenditure of the earlier year would amount to such income being applied for charitable or religious purposes [CIT vs. Shri Gujarati Samaj (Regd.) (2011) 64 DTR 76 (MP)].

Anonymous donations to form part of income of trust [Section 13]

As per the new section 115BBC, anonymous donation shall now be taxable at the maximum marginal rate of 30%. Consequently, a new sub-section (7) has been inserted in section 13 to provide that nothing contained in section 11 or section 12 shall operate so as to exclude from the total income of the Previous Year of the person in receipt thereof, any anonymous donation referred to in the new section 115BBC on which tax is payable in accordance with the provisions of that section. In other words anonymous donation shall not be excluded from the total income of the assessee.

Taxation of Trust

A. Public Trust u/s. 164(2) —

(i) If income is not exempt u/s 11 or 12, income of Trust is taxable at the rates applicable to an Association of Person.

(ii) If the exemption is forfeited due to contravention of Sec. 13(1)(c) or 13(1)(d), such income of trust is taxable at maximum marginal rate.

B. Private Trust (shares of beneficiaries are determinate or known) —

(i) If income does not include business Profits, the trustee is assessable at the rates applicable to each beneficiary. [Sec. 161(1)]

(ii) If income includes profits from business, the whole income is taxable at maximum marginal rate. [Sec. 161(1A)]

C. Private Trust (share of beneficiaries in determinate or unknown) [Sec. 164(1)] —

(i) If income does not include business profits, income is taxable at the rates applicable to an AOP if –

- none of the beneficiaries has taxable income or is a beneficiary in any other trust.
- the trust is non-testamentary trust created before 1.3.1970
- exclusively for the relative dependents of the settle; or
- it is the only trust declared by a WILL exclusively for the benefit of any dependent relative. In any other case, income is taxable of maximum marginal rate.

(ii) If income includes business profits, the whole income is taxable at maximum marginal rate.

D. Oral Trust [Sec. 160(1)(v), Sec. 164A] : "Oral Trust" means a trust which is not declared by a duly executed instrument in writing including any wakf deed which is valid under the Mussalman wakf validating Act, 1913 and which is not deemed to be trust by virtue of Explanation 1 to Sec. 160.

(i) Income of Oral trust is taxable at maximum marginal rate.

(ii) If Oral trust is declared to be a trust by furnishing a statement in writing containing purposes, particulars and details of trust, beneficiaries and property to the assessing officer within 3 months from the date of declaration of the trust, indicating the share of beneficiaries, the income of the trust is assessable in the hands of trustee at the rates applicable to beneficiaries.

E. Income from property held under Trust partly for religious purposes and partly for other purposes [Sec. 164(3)]

Where property is held under trust partly for religious purposes and partly for other purposes and the individual share of the beneficiaries in the income applicable to purposes other than charitable purposes, is not known, the Income-tax liability will be aggregated as follows :

(i) the tax which would be chargeable on the part of the relevant income which is applicable to charitable or religious purposes (as reduced by the income which is exempt u/s 11 as if such part were the total income of an Association of Persons); and

(ii) the tax on that part of income attributable to purposes other than charitable or religious and in respect of which shares of beneficiaries are indeterminate or unknown, at the maximum marginal rate.

F. Securitisation Trust [Sections 115TA to 115TC]:

Securitisation Trust means a trust set up to undertake securitisation activities.

(i) If income of the trust consists of business income or the participants have taxable income, then trust is subject to maximum marginal rate of tax.

(ii) The income from the activity of securitisation of such trust will be exempt from tax u/s 10(23DA) with effect from the Assessment Year 2014-15.

(iii) Such trust will be liable to pay additional income tax on income distributed to its investors @ 25% if the income is distributed to investors being Individual or HUF or 30% for other case. Such amount of tax will be subject to increase by surcharge @10%, Education Cess @ 2% and Secondary and Higher Secondary Education Cess @1%.

(iv) The additional income tax shall not be payable if the income so distributed by such trust is received by a person who is exempt from tax under the Act.

(v) Amount of tax on distributed income shall be remitted within 14 days from the date of payment or distribution of income.

Where any part of income is not exempt u/s 11 or 12 by virtue of sec. 13(1)(c) or (d), tax is charged on the relevant income at the maximum marginal rate.

The amount of tax will be increased by surcharge @ 12%, Education Cess @ 2% and Secondary and Higher Education Cess @ 1%.

However, the total amount payable as income tax and surcharge on total income exceeding ₹1 crore shall not exceed the total amount payable as income tax on a total income of ₹1 crore, by more than the amount of income that exceeds ₹1 crore.

Case Laws :

(i) For purpose of section 164(1) what is relevant is that income is receivable on behalf of beneficiaries and is not necessary that income is received by beneficiaries - Gosar Family Trust vs. CIT 81 Taxman 146/215 ITR 55.

(ii) Provision merely sets out how tax is to be charged and does not create a charge on the income - CIT vs. Kamalini Khatau 209 ITR 101.

Exemption under section 11(2) shall be allowed subject to the following conditions being satisfied:

(a) such person furnishes a statement in the prescribed form and in the prescribed manner to the Assessing Officer, stating the purpose for which the income is being accumulated or set apart and the period for which the income is to be accumulated or set apart, which shall in no case exceed five years;

(b) the money so accumulated or set apart is invested or deposited in the forms or modes specified in section 11(5);

(c) the statement referred to in clause (a) is furnished on or before the due date specified under section 139(1) for furnishing the return of income for the previous year.

Provided that in computing the period of five years referred to in clause (a), the period during which the income could not be applied for the purpose for which it is so accumulated or set apart, due to an order or injunction of any court, shall be excluded.

Section 11(5) specifies the following modes of deposit/investment:

(1) Investment in Government Saving Certificates and any other Securities or Certificates issued by the Central Government under its Small Saving Scheme.

(2) Deposits with Post Office Savings Banks.

(3) Deposits with Scheduled Banks or Co-operative Banks (including a Cooperative Land Mortgage Bank or a Cooperative Land Development Bank).

(4) Investments in the units of Unit Trust of India.

(5) Investments in Central or State Government Securities.

(6) Investments in debentures issued by or on behalf of any company or corporation. However both the principal and interest thereon must have been guaranteed by the Central or the State Government.

(7) Investment or deposits in any public sector company.

An investment or deposit in a public sector company shall continue to be one of the eligible modes of investment for charitable or religious trusts, for a period of three years (in the case of shares), and till the date of maturity of other investment or deposit from the date a public sector company ceases to be a public sector company.

(8) Investment in bonds of approved financial corporation providing long term finance for industrial development.

(9) Investment in bonds of approved public companies whose principal object is to provide long-term finance for construction or purchase of houses in India for residential purposes.

(10) Investment in immovable property excluding plant and machinery, not being plant and machinery installed in a building for the convenient occupation thereof.

(11) Deposits with or investment in any bonds issued by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for urban infrastructure in India.

Explanation — For the purposes of this clause, —

(a) long-term finance means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years;

(b) public company shall have the meaning assigned to it in section 2(71) of the Companies Act, 2013;

(c) urban infrastructure means a project for providing potable water supply, sanitation and sewerage, drainage, solid waste management, roads, bridges and flyovers or urban transport.

(12) Deposits with the Industrial Development Bank of India.

(13) Any other form or mode of investment or deposit as may be prescribed. Rule 17C has prescribed the following forms and mode of investments for this purpose:

(i) investment in the units issued under any scheme of mutual fund referred to in section 10(23D) of the Income-tax Act, 1961;

(ii) any transfer of deposits to the Public Account of India;

(iii) deposits made with an authority constituted in India by or under any law enacted either for the purpose of dealing with any satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or for both;

(iv) investment by way of acquiring equity shares of a depository as defined in section 2(1)(e) of the Depositories Act, 1996;

(v) investment by way of equity share capital of a specified company;

(vi) investment by way of acquiring equity shares of an incubatee by an incubator.

As per Explanation given under section 11(2), any amount credited or paid out of the income referred to in section 11(1)(a) or (b) read with explanation to that sub-section which is not applied, but is accumulated or set apart, to any trust or institution registered under section 12AA or to any fund or institution or trust or any university or other educational institution or any hospital or other medical institution referred to in section 10(23C)(iv), (v), (vi) and (via) shall not be treated as application of income for charitable or religious purposes, either during the period of accumulation or thereafter.

Further, as per section 11(3), where the income of trust referred to in section 11(2) is credited or paid to any trust or institution registered under section 12AA or any institution or trust referred to in section 10(23C)(iv), (v), (vi) or (via) it shall be treated as not applied for charitable purpose, and such income shall be deemed to be the income of the previous year in which such amount is paid or credited.

As per section 11(3), where the income of the trust referred to in section 11(2)—

(a) is applied for purposes other than charitable or religious purposes, or ceases to be accumulated or set apart for application thereto, or

(b) ceases to remain invested or deposited in any mode mentioned under section 11(5) above, or

(c) is not utilized for the purpose for which it is so accumulated or set apart during the period specified (not exceeding 10/5 years) or in the year immediately following thereof,

(d) is credited or paid to any trust or institution registered under section 12AA or any institution or trust referred to in section 10(23C)(iv), (v), (vi) or (via),

such income shall be deemed to be the income,—

in case of (a) of the previous year in which it is so applied for other purpose or ceases to be accumulated or set apart, or

in case (b) of the previous year in which it ceases to remain so invested or deposited, or

in case of (c) of the previous year immediately following the expiry of period specified therein, or

in case of (d) of the previous year in which it is paid or credited.

As per section 11(3A), where the income invested/deposited in approved modes cannot be applied for the purposes for which it was accumulated or set apart, due to circumstances beyond the control of the assessee, such assessee can make an application to the Assessing Officer specifying such other purpose for which he wants to utilise such accumulated income. Such other purposes should also be in conformity to the objects of the trust. The Assessing Officer in this case, may allow the application of such income to such other purposes. On such an application being allowed by the Assessing Officer, the funds may be accumulated and/or applied for the purposes newly specified and the provisions regarding withdrawal of exemption will be applicable on the basis that new purposes were the ones that had been specified in the notice for accumulation given under section 11(2). However, the Assessing Officer shall not allow application of such income by way of payment or credit made for donation to other trust or other institutions, but the Assessing Officer may allow application of such accumulated income for the purpose of donation to other trust or institution in the year in which such trust or institution was dissolved.

The grants which are received for specific purposes did not belong to the assessee society; such grants did not form corpus of the assessee or its income. Those grants were not donations to the assessee so as to bring them under the purview of section 12. Voluntary contribution covered by section 12 is those contribution which are freely available to the assessee without any stipulation, which the assessee can utilise towards its objectives according to its own discretion and judgement. Tied up grants for specified purpose would only mean that the assessee which was a voluntary organisation had agreed to act as a trustee of a special fund granted by the donor with the result that it need not be pooled or integrated with the assessee normal income or corpus. Hence, even when the assessee had been assessed as AOP and deprived of section 11 benefits, the Assessing Officer could assess only net income of the assessee and not gross receipts. The assessee should have actually credited the grant in the personal account of the donor and any asset spent against the grant should have been debited to that separate account of the donor. That incoming and outgoing need not be reflected in the income and expenditure account of the assessee. At the end of the project, the balance, if any, available to the credit of the donor, could be treated as income of the assessee, if the donor did not insist for the repayment of the balance amount [Nirmal Agricultural Society vs. ITO (1999) 71 ITD 152 (Hyd). Also see Society for Integrated Development in Urban & Rural Area vs. DCIT (2004) 90 ITD 493 (Hyd)].

Any profit or gain arising from the transfer of capital asset being property held under trust shall be treated as capital gain. Since such capital gain, whether short-term or long-term, is also part of the income as per section 2(24)(vi), to claim exemption under section 11 the Charitable Trust should also apply income from such capital gain for charitable purposes during the previous year like any other income. It means that trust shall have to apply atleast 85% of the income from such capital gain for charitable purposes during the previous year.

Section 11(1A) which deals with treatment of capital gains, was not there at the inception of the Act. In the absence of such sub-section, all charitable or religious trusts or institutions were required to apply the capital gains for charitable or religious purpose to claim exemption under section 11(1)(a).

As capital assets were normally bought with corpus funds, the requirement of applying capital gain for the objects of the trust to claim exemption under section 11(1)(a) resulted into depletion of corpus. Hence, it was felt necessary to allow an option to such trusts or institutions whereby they could reinvest the sale proceeds from capital assets in some other capital assets, to enable the trust or institutions to maintain the corpus funds for the future.

Therefore, instructions were issued by Circular No. 2-P [LXX-5], dated 15-5-1963 which allowed the charitable or religious trust to reinvest the sale proceeds of the capital asset in another assets and still regard the same as applied for charitable or religious purpose. As per the Circular — where a religious or charitable trust transfers a capital asset forming part of the corpus of its property solely with a view to acquiring another capital asset for the use and benefit of the trust and utilizes the capital gains arising from the transaction in acquiring the new capital asset, the amount of capital gain so utilized should be regarded as having been applied for the religious or charitable purposes of the trust within the meaning of section 11(1).

Some changes were made in section 11(1) by the Finance Act, 1970 and the question was raised whether the instructions contained in Circular No. 2-P above shall be operative after the amendment made by the Finance Act, 1970. It was decided by the Board that the above instructions should continue to be operative notwithstanding the changes made in the scheme of the exemption of charitable or religious trusts through the Finance Act, 1970 [Circular No. 52 [F. No. 152(55) 70-TPL], dated 30-12-1970].

Thus prior to insertion of sub-section (1A) to section 11, the intention of the legislature was not in favour of imposing tax liabilities in case where the capital gain as well as the consideration is applied for acquisition of new capital assets.

The above concession already allowed under executive orders were formalized by the insertion of sub-section (1A) to section 11 by the Finance (No. 2) Act, 1971 w.r.e.f. 1-4-1962. Sub-section (1A) provided that the capital gains for the purpose of sub-section (1) shall be deemed to have been applied for charitable or religious purposes to the extent specified by the said sub-section (1A). In this connection explanatory circular No. 72, dated 6-1-1972 explained the reasons for insertion of sub-section (1A).

Section 11(1A) deals with two situations where income from capital gain shall be deemed to have been applied for charitable purposes:

(1) Transfer of capital asset held under trust wholly for charitable or religious purposes.

(2) Transfer of capital asset held under trust in part only for charitable or religious purposes.

(1) Transfer of capital asset held under trust wholly for charitable or religious purposes Section 11(1A)(a): Where any capital asset being property held under trust wholly for charitable or religious purposes

is transferred, and

(i) the whole of the net consideration is utilised for acquiring another capital asset; or

(ii) part of the net consideration is utilised for acquiring another capital asset.

then, the capital gain arising from such transfer shall be deemed to have been applied to charitable purposes to the extent specified hereunder:

Amount of net consideration utilized	Amount deemed to be applied
Where the whole of the net consideration of such asset is utilized in acquiring a new capital asset	The whole of the capital gain.
Where only a part of the net consideration is utilized for acquiring the new capital asset	So much of such capital gain as is equal to the amount, if any, by which the amount so utilized exceeds the cost of the transferred asset i.e. amount invested minus cost of the transferred asset.

(2) Transfer of capital asset held under trust in part only for charitable or religious purposes [Section 11(1A)(b)]: As already discussed such trusts are eligible for exemption under section 11 only when they have been created before the commencement of the Income-tax Act, 1961.

Where capital assets being a property held under trust in part only for such purposes is transferred, the treatment of capital gains shall be as under:

Amount of net consideration utilized	Amount deemed to be applied
Where the whole of the net consideration is utilised in acquiring the new capital asset	The appropriate fraction of the capital gain arising from the transfer of the capital asset
In any other case	The exemption shall be limited to so much of the appropriate fraction of the capital gain as is equal to the amount, if any, by which the appropriate fraction of the amount utilized for acquiring the new capital assets, exceeds the appropriate fraction of the cost of the transferred asset

Appropriate fraction means the fraction which represents the extent to which the income derived from the capital asset transferred was immediately before such transfer applicable to charitable or religious purposes;

Cost of the transferred asset means the aggregate of the cost of acquisition (as ascertained for the purposes of sections 48 and 49) of the capital asset which is the subject of the transfer and the cost of any improvement thereto within the meaning assigned to that expression in section 55(1)(6);

Net consideration means the full value of the consideration received or accruing as result of the transfer of the capital asset as reduced by any expenditure incurred wholly and exclusively in connection with such transfer.

Investment by way of fixed deposit in a public sector company or scheduled bank can be treated as a new asset acquired with the net consideration in terms of section 11(1A). Further, the option, to apply part of the capital gain in the next year, exercised under the Explanation to sub-section (1) to section 11 requesting the Assessing Officer to treat the part of the capital gain as deemed application of the current year is also permissible [CIT vs. East India Charitable Trust (1994) 206 ITR 152 (Cal)].

The brief facts of the case were as under:

During the relevant previous year ended on 31-12-1981, the assessee-trust sold shares of various companies which formed the corpus of the trust fund for a net consideration of ₹3,778,640. On this transaction, the capital gains shown amounted to ₹2,379,538. The assessee claimed that the net consideration of the sale was utilised for acquiring new capital assets as under:

Date of utilisation in 1981	Amount INR(₹)	Particulars
29-12-1981	12,50,000	Fixed deposit with Hindusthan Petroleum Corporation Ltd
29-12-1981	7,50,000	Fixed deposit with Bharat Petroleum Corporation Ltd
29-12-1981	5,00,000	Fixed deposit with Bharat Heavy Electrical Ltd
30-12-1981	5,88,149	48,130 units of the Unit Trust of India
	30,88,149	
In 1982:		
13-01-1982	4,00,000	Fixed deposit with Bharat Petroleum Corporation Ltd
08-02-1982	3,00,000	Fixed deposit with Bharat Heavy Electricals Ltd
	7,00,000	

Out of the above, a sum of ₹7,00,000 was invested in the next previous year after December 31, 1981, and an option was exercised under the Explanation to section 11(1) requesting the Income-tax Officer to treat the above sum as deemed application during the year ended on December 31, 1981. It was urged that the capital gains of ₹23,79,538 was, therefore, exempt from tax under section 11(1) of the Income-tax Act, 1961.

The Income-tax Officer found that the assessee made fixed deposits with Central Government undertakings and further purchased 48,130 units of the Unit Trust of India. The Income-tax Officer was of the view that the investment in public sector undertakings was nothing but loans floated by these companies under their schemes and did not amount to the acquisition of capital assets. As regards unit trust investment, he found that the shares were not issued during the relevant year. The units were not marketable and the assessee did not become a registered holder of the units in the year under reference. He also found that the sum of ₹5,69,151 was included by the assessee in 'loans and advances' and had not been spent during the calendar year 1981.

The Income-tax Officer observed that the assessee could not get the benefit of deemed application under section 11(1) by utilising the net consideration in the subsequent year. The Income-tax Officer did not accept the assessee's contention that the net consideration for the sale of shares was utilised by it in acquiring new capital assets. He, therefore, did not allow exemption in respect of capital gains of ₹2,379,538 under section 11(1) of the Income-tax Act.

In this reference under section 256(1) of the Income-tax Act, 1961, for the assessment year 1982-83, the following questions of law have been referred to this court:

(1) Whether, on the facts and in the circumstances of the case, the Income-tax Officer was correct in law in holding that the investment in public sector undertakings was a capital asset within the meaning of section 2(14) of the Income-tax Act, 1961?

(2) Whether the finding of the Tribunal that the assessee-trust had invested in the units of the Unit Trust of India during the relevant previous year was based on proper evidence and materials?

(3) Whether, on the facts and in the circumstances of the case, the Income-tax Appellate Tribunal was correct in law in holding that the entire sale proceeds from shares were invested in the acquisition of other capital assets within the meaning of section 11(1A) of the Income-tax Act, 1961?

(4) Whether the Income-tax Appellate Tribunal was justified in holding that the assessee-trust was entitled to exemption under section 11(1A) of the Income-tax Act, 1961, in respect of the capital gains of ₹2,379,538 on the sale of shares?

In was held that—

(a) As per section 2(14), capital asset includes property of any kind held by an assessee. 'Deposits or investments' are a kind of property and they do not fall in the exclusionary limb of the said definition.

What reinforces the assessee's case is the special mention in subsection (5) of section 11 of deposits with public sector companies. This only shows that an investment or deposit in a public sector company is firstly an asset and secondly a capital asset and thirdly a permitted capital asset under the special law relating to the assessment of charitable or public religious trusts. Therefore, the contention of the Revenue that the investment by way of deposit in a public sector company cannot be treated investment by way of deposit in a public sector company cannot be treated as a new asset acquired with the net consideration in terms of section 11(1A) is not tenable.

(b) In our view, by reason of the option exercised under the Explanation to section 11(1), the assessee is entitled to the benefit under section 11(1A) in as much as the definition of income as contained in section 2(24) of the Act includes capital gains as one of the species of income. That being so, the option as exercisable with regard to income should also avail to capital gains provided such option is exercised in writing before the expiry of the time allowed under subsection (1) of section 139 for furnishing the return. Therefore, the amount of ₹7 lakh utilised in acquiring fixed deposits with the Bharat Petroleum Corporation Ltd and the Bharat Electronics Ltd should also be allowed exemption under the said provision for the assessment year 1982-83.

For the reasons aforesaid, we answer the first and the third questions in R.A. No. 1475/(Cal) of 1986 in the affirmative and against the Revenue.

(c) So long as the investments were actually made during the accounting period, the issue of the units after the expiry of the accounting year is immaterial. The same shall relate back to the date when the payments were made to the unit trust for the purchase of the units.

There can be no cause for the Revenue to agitate that the utilisation in acquisition of fresh capital assets by way of units of the Unit Trust of India did not take place during the relevant previous year. The Revenue has not brought any evidence to prove that the money for the units had not been tendered on December 30, 1981. Nor is the finding of fact by the lower authorities on that aspect in any manner questioned. Therefore, we answer question No. 2 in the affirmative and in favour of the assessee.

[Director of Income Tax (Exemption) vs. DLF Qutub Enclave Complex Medical Charitable Trust (2001) 115 Taxman 520 (Del)].

Net consideration invested in a fixed deposit is an investment for acquiring another capital asset [Hindustan Welfare Trust vs. ITO (1988) 26 ITD 1 (AT) (SB) (Cal)].

Where an assessee trust had used the consideration on sale of a capital asset for redeeming a pledge, it was held that the assessee trust had merely discharged its obligation to pay the creditor and had not thereby acquired any capital asset so as to be entitled to the exemption under this section [CIT vs. Avkash Nidhi (1986) 160 ITR 729 (Guj)].

Where an assessee sold some shares and a part of the net consideration was deposited in a bank and the balance was left with the purchaser of shares as fixed deposit on interest and in its Balance Sheet this amount was shown as investment, it was held that the provisions of section 11(1A) were fully satisfied [CIT vs. Ambalal Sarabhai Trust (1988) 173 ITR 683 (Guj)].

Investment of the net consideration in fixed deposit with a bank for a period of six months or above would be regarded as utilization of the net consideration for acquiring another capital asset within the meaning of section 11(1A) of the Income-tax Act, 1961 [Instruction No. 883, dated 24-9-1975].

Where the net consideration was utilised during the accounting year for acquiring units of Unit Trust of India but the certificates of the units were received after the expiry of the accounting year, it was held that if the investments were actually made during the accounting year, the issue of the units by the Unit Trust of India after the expiry of the accounting year is immaterial for the purpose of claiming exemption under section 11(1A) [CIT vs. East India Charitable Trust (1994) 206 ITR 152 (Cal)].

Section 11(1A) is not meant for calculation of capital gains tax but is to operate after capital gains are worked in accordance with the provisions of sections 45 to 55 [Akhara Ghamanda Dass vs. Asstt. CIT (2000) 68 TTJ (Asr) 244].

Donation received in kind

Certain funds, trusts and institutions running hospitals, creches orphanages, school, etc, often receive donation in kind from various sources for application towards their charitable purposes. These contributions may be in the shape of books, clothes for the poor, grains to feed the poor, drugs, hospital equipments, etc.

Since, the donation in kind, of a nature referred to above, received by a fund, trust or institution would be income within the meaning of section 2(24)(vi) of the Act, it is clarified that the use of these towards object for which the fund, trust or institutions is established would be regarded as application of the income of the fund, trust or institution [Circular No. 580, dated 14-9-1990].

Where a trust received donation in kind and the same could not be used towards objects for which the trust, fund, etc is established, it should convert the asset in the form or mode specified in section 11(5) before the expiry of one year from the end of the previous year in which asset is acquired.

Business Income of a Trust

Trust can earn the following two types of business income:—

(a) Profits and gains from a business undertaking held under a trust [Section 11(4)].

(b) Profits and gains from a business provided such business is incidental to the attainment of the objectives of the trust/institution and separate books of account are maintained in respect of such business [Section 11(4A)].

(a) Profits and gains from a business undertaking held under a trust [Section 11(4)]: According to section 11(4), for the purpose of section 11 'property held under trust' includes a business undertaking so held and where a claim is made that the income of any such undertaking shall not be included in the total income of the trust, etc. in receipt thereof, the Assessing Officer shall have the power to determine the income of such undertaking in accordance with the provision of the Income-tax Act relating to the assessment and where the income determined by the Assessing Officer exceeds the income as shown in the books of account of the undertaking, such excess shall be deemed to be applied to purposes other than charitable or religious purposes and hence would not be exempt.

Section 11(4) is merely intended to tax income which is not accounted for in the books: It does not operate to charge a disclosed amount which is admittedly expended, for a purpose either charitable or non-charitable, but is disclosed as business expenditure and consequently added back in computing the business income [CIT vs. Birla Education Trust (1985) 153 ITR 579 (Cal)].

(b) Profits and gains from incidental business [Section 11(4A)]: Where a trust or an institution is also carrying on any business activity, the provisions of section 11(1), (2), (3) and (3A) regarding exemption etc. shall not apply in respect of income earned from such business activity. However, if such business is incidental to the attainment of the objects of the trust/institution and separate books of account are maintained by such trust/institution in respect of such business, the exemption shall be available to trust in respect of income earned from such business activity.

Consequent to substitution of sub-section (4A), w.e.f. assessment year 1992-93, all that is required for business income of a trust or institution to be exempt is that business should be incidental to attainment of objectives of trust or institution [Asstt. CIT vs. Thanthi Trust (2001) 247 ITR 785 (SC)]. Thus, a business whose income is utilised by the trust or the institution for the purpose of achieving the objective of the trust or the institution is, surely, a business which is incidental to the attainment of the objectives of the trust.

(1) Income of any other business which is not incidental to the attainment of the objectives of the trust or institution will not be exempt from tax [Circular No. 642, dated 15-12-1992].

(2) It is relevant to note that the provisions of section 11(4A) do not override the provisions of section 10 of the Income-tax Act, and as such, profits derived by any trust, institution, association etc referred to in clauses (21), (23A), (23B), (23BB), (23C), etc. will continue to be exempted from income tax.

(3) W.e.f. A.Y. 2009-10, where a trust or institution is registered under the category of 'advancement of any other object of general public utility', and it is carrying on any activity in the nature of trade, commence or business or it is carrying on any activity of rendering of any service in relation to any trade, commerce or business, such advancement of any other object of general public utility shall not be a charitable purpose. However, this provision shall not be applicable if the gross receipts of such trust or institution from such activity during the previous year does not exceed ₹25,00,000 (₹10,00,000 for assessment years 2010-11 and 2011-12).

Where a charitable institution after acquiring an old building demolished the same and constructed marriage halls and auditoria and with a part of it run as a hostel it was held that such activity of letting is not business. Further, the property is one of the permitted investments under section 11(5) and if it is treated as investment in property, the question of application under section 11(4A) could not arise and the Assessing Officer has not to decide as to whether such business income was used for attainment of its objects [DIT (Exemption) vs. Willington Charitable Trust (2011) 330 ITR 24 (Mad)].

Registration of a Trust

For claiming exemption under sections 11 and 12, the trust must be registered under the Income-tax Act.

The application for registration of a charitable or religious trust has to be made in Form 10A. However, w.e.f. 1-6-2007, section 12A was amended as under:

(1) For application for registration made on or before 30-5-2007, registration was granted under section 12A.

(2) For application for registration made on or after 1-6-2007, registration is to be granted under section 12AA.

(1) Law applicable up to 30-5-2007 [Section 12A(1)(a)]: The person in receipt of income was to make an application for registration of the trust/institution in the prescribed form (Form No. 10A) and in the prescribed manner to the Commissioner of Income-tax before the expiry of a period of one year from the date of creation of the trust or the establishment of the institution. If the application for registration was made within the prescribed time and the registration was granted under section 12A, the provisions of sections 11 and 12 were applicable from the date of creation of trust.

Condonation of delay in making application [Proviso to section 12A(1)(a)]: Where such application was made after the expiry of the aforesaid period, the provisions of sections 11 and 12 were to apply in relation to the income from the date of creation of the trust only if the Commissioner was, for reasons to be recorded in writing, satisfied that the person in receipt of the income was prevented from making the application before the expiry of the period aforesaid for sufficient reasons.

If the Commissioner was not so satisfied, the provisions of sections 11 and 12 were to apply only from the first day of the financial year, in which such application was made.

(2) Law applicable w.e.f. 1-6-2007 [Sections 12A and 12AA]: Power of condonation of delay in making application for registration of charitable or religious trust has been withdrawn by the Finance Act, 2007.

Hence, as per section 12A(1)(aa) if the application for registration is made on or after 1-6-2007 the registration shall be granted under section 12AA.

Further, as per section 12A(2), the provision of sections 11 and 12 shall apply in relation to the income of such trust or institution from assessment year immediately following the financial year in which such application is made.

Documents to be attached along with application in Form 10A:

According to rule 17A, application for registration of a trust or institution shall be made in Form 10A, in duplicate and it shall be accompanied by the following documents, namely:—

(a) (i) Where the trust is created, or the institution is established, under an instrument — The instrument in original, together with one copy thereof.

(ii) Where the trust is created, or the institution is established, otherwise than under an instrument — The document evidencing the creation of the trust or the establishment of the institution, together with one copy thereof.

However, if the instrument or document in original cannot conveniently be produced, it shall be open to the Chief Commissioner or Commissioner to accept a certified copy in lieu of the original;

(b) where the trust or institution has been in existence during any year or years, prior to the financial year in which the application for registration is made, two copies of the accounts of the trust or institution relating to such prior year or years (not being more than three years immediately preceding the year in which the said application is made) for which such accounts have been made up.

Where a trust is in existence for past several decades and no evidence or any document creating a trust is available, a declaration by existing trustees indicating the trust property and its objects as ascertained from all available evidence and other evidences as revenue records, house tax receipts, etc. shall form a logical base for inferring a creation of trust and these should be adequate for registration of trust [Laxminarayan Maharaj and Anr vs. CIT (1984) 150 ITR 465 (MP)].

Procedure for Registration of trusts under Income-tax Act

As per section 12AA, the Commissioner, on receipt of an application for registration of a trust or institution made under section 12A, shall—

(a) call for such documents or information from the trust or institution as he thinks necessary in order to satisfy himself about the genuineness of activities of the trust or institution and may also make such inquiries as he may deem necessary in this behalf; and

(b) after satisfying himself about the objects of the trust or institution and the genuineness of its activities, he—

(i) shall pass an order in writing registering the trust or institution;

(ii) shall, if he is not so satisfied, pass an order in writing refusing to register the trust or institution,

and a copy of such order shall be sent to the applicant:

However, no order refusing to register the trust shall be passed unless the applicant has been given a reasonable opportunity of being heard.

Order granting or refusing registration should be passed within 6 months [Section 12AA(2)]: Every order granting or refusing registration shall be passed before the expiry of six months from the end of the month in which the application was received under section 12A.

While considering the application for registration under section 12A, the Commissioner is not to examine the application of income. All that he is required to examine is whether the application form for registration is made in accordance with requirements of section 12A read with rule 17A i.e. whether the society has actually made an application in time, whether the accounts of the society have been maintained in the manner as suggested by such section and whether Form No. 10A has been properly filled up. He may also see whether the objects of trusts are charitable or not but at this stage it is not necessary or proper to examine whether the society would be able to claim the exemption under section 11 or 12. The only purpose for which the registration is required is for establishing its identity as an institution for being able to claim benefit under sections 11 and 12 of the Act [New Life In Christ Evangelistic Association vs. CIT (2000) 246 ITR 532 (Mad)].

For the purpose of registration of a trust under section 12AA, authorities have to ascertain only genuineness of activities of trust and how income derived from trust property is applied for charitable or religious purposes and not nature of activity by which income is derived by trust [Sanjeevamma Hanumanthe Gowda Charitable Trust vs. Director of Income Tax (Exemption) (2006) 155 Taxman 466 (Karn)].

Where, on an application filed under section 12A(a), a trust or institution is registered as a charitable or religious one, the registration itself would be sufficient proof of the fact that the trust or institution concerned is created or established for charitable or religious purposes. In such a case, it would not be possible for the Assessing Officer, in the course of the assessment proceedings, to come to a different finding that the trust or institution is not one for charitable or religious purposes. However, the Assessing Officer would be entitled to forfeit the exemption to the trust or institution for non-fulfilment of any other statutory requirement and/or contravention of any other provision of law [CIT vs. Ootacamund Gymkhana Club (1977) 110 ITR 392 (Mad)].

The application of income to charitable purposes outside India is relevant for determining the question of exemption and not for deciding the eligibility for registration under section 12AA [CIT vs. Shri Ram Memorial Foundation (2004) 269 ITR 35 (Del)].

Further, if the objects of the trust are charitable, the fact that no activity has been carried out by the trust does not entitle the Commissioner to hold that trust is not entitled to registration even though its objects are charitable [S.L. Oberai Memorial Charitable Trust vs. ITO (2005) 3 SOT 229 (Del)].

University, incorporated under Haryana Private Universities Act, 2006, is an artificial juristic person within the meaning of term "person" under section 2(31)(vii), hence, it is entitled to make an application for registration under section 12AA. The object of the university were granting fellowship, freeship, scholarship, etc to students belonging to weaker sections of society, it could be concluded that assessee was a charitable institution [O. P. Jindal Global University vs. CIT (2010) 127 ITD 164 (Del)].

Only because no charitable activity is carried on for the relevant year, registration cannot be refused. The Tribunal directed the CIT to grant approval under section 80G(5)(vi) [Jasoda Devi Charitable Trust vs. CIT (2010) 4 ITR 457 (Jaipur)(Trib)].

While granting registration to a Charitable Trust or institution, the powers of the CIT are limited to examination as to whether or not the objects of the trust are charitable in nature and examination about the genuineness of the activities, when genuineness of the activities is not in doubt, the CIT was not justified in refusing the registration under section 12AA, on irrelevant grounds [Saint Kabir Educational Trust vs. CIT (2010) 41 DTR 267 (Asr)(Trib)].

Where a truck operators association was formed for the welfare of the truck operators who were its members and it applied for registration under section 12AA as an association for charitable purpose under the category of advancement of general public utility, it was held that the assessee is not entitled to benefit of registration as it is not formed for advancement of general public utility [CIT vs. Truck Operator Association (2010) 328 ITR 636 (P&H)].

Denial of registration should be in a speaking order: Registration is an executive process, which involves exercise of quasi judicial powers. Where the commission declines registration, it could only be in a speaking order recording reasons for denial. The commissioner not having given any reasons in the order cannot support his denial by adducing reasons in the counter affidavit filed before the High Court [Adarsha Vidyanidhi Trust vs. CIT (2007) 292 ITR 465 (Ker)].

Where after examining the Income and Expenditure Account for the relevant assessment years, the Commissioner concluded that assessee was not carrying on any charitable activity within the meaning of section 2(15) and its dominant object was to earn profits under the garb of education and accordingly the application for registration was rejected, it was held that in expression 'charitable purpose', charity is soul of expression and mere trade and commerce in education cannot be said to be a charitable purpose entitling a society to grant of registration under section 12AA [CIT vs. National Institute of Aeronautical Engineering Education Society (2009) 181 Taxman 205 (Uttakhand)].

Where a truck operators association was formed for the welfare of the truck operators who were its members and it applied for registration under section 12AA as an association for charitable purpose under the category of advancement of general public utility, it was held that the assessee is not entitled to benefit of registration as it is not formed for advancement of general public utility [CIT vs. Truck Operator Association (2010) 328 ITR 636 (P&H)].

If the Commissioner does not pass any order granting/refusing registration within the time limit set under section 12AA, then the Commissioner is deemed to have allowed the registration [Society for the Promotion of Education, Adventure Sport & Conservation of Environment vs. CIT (2008) 171 Taxman 113 (All). See also Bhagwad Swamp Shri Shri Devraha Baba Memorial Shri Hari Parmarth Dham Trust vs. CIT (2008) 299 ITR (AT) 161 (Del)(SB)].

Once the period of limitation prescribed under section 12AA(2) has expired, the subsequent impugned order refusing registration is nothing but a nullity. The expression used in the section is "shall". This "shall" cannot be expressed to mean 'may'. The unequivocal purport of the section is mandatory. There is no escape for the department. Once the limitation period has expired, the Commissioner becomes functus officio as regards the application under consideration before him. At the very moment of expiry of limitation, the application is deemed to have been accepted, in case no order thereon is passed by him.

Wherever application for registration is made, the authorities must act within the time frame. Failure on the part of the authority concerned to pass order within the statutorily laid down period of limitation will give rise to a presumption that registration, as applied for by the assessee, has been granted [Karnataka Golf Association vs. Director of Income Tax (2004) 91 ITD 1 (Bang)].

If the Commissioner does not grant or refuse to grant registration to a trust under section 12AA within the stipulated period of 6 months the registration shall be deemed to have been granted [Rev Father Trust Oscar Colasco Memorial Medical Association vs. Commissioner of Income-tax III, Thane (2009) 31 SOT 1 (Mum)].

Further, if the objects of the trust are charitable, the fact that no activity has been carried out by the trust does not entitle the commissioner to hold that trust is not entitled to registration even though its objects are charitable [S.L. Oberai Memorial Charitable Trust vs. ITO (2005) 3 SOT 229 (Del)].

If the application is made on or after 1-6-2007, the provision of sections 11 and 12 shall apply in relation to the income of such trust or institution from assessment year immediately following the financial year in which such application is made.

Prior to 1-6-2007, the registration would become effective from the date of creation of the trust if the application was made before the expiry of a period of one year from the date of creation of the trust or establishment of the institution. Further, prior to 1-6-2007, the Commissioner had a power to condone the delay in making an application for registration and the registration could be granted by the Commissioner from the date of creation of trust even if application was made after the expiry of the aforesaid one year.

Where a trust or an institution has been granted registration under section 12AA(1)(b) and subsequently, the Commissioner of Income-tax is satisfied that the activities of any trust or institution are not genuine or are not being carried out in accordance with the objects of the trust or institution, he shall, after giving reasonable opportunity of being heard to the concerned trust or institution, pass an order in writing cancelling the registration granted under the said section.

Amendment made by the Finance Act, 2010

Cancellation of registration obtained under section 12A [Section 12AA] [W.e.f. 1-6-2010]

Judicial rulings in Sri Chaitanya Educational Committee vs. CIT (2007) 106 ITD 256 (Hyd) and other cases have held that the Commissioner does not have the power to cancel the registration which was obtained earlier by any trust or institution under provisions of section 12A as it is not specifically mentioned in section 12AA(3).

The Act has therefore amended section 12AA(3) so as to provide that the Commissioner can cancel the registration even if it was obtained under section 12A.

As per section 12AA(3), registration granted to any trust or society under section 12AA(1)(b) can be cancelled only if the CIT is satisfied that the activities of such trust or institution are not genuine or are not being earned out in accordance with the objects thereof; registration could not be cancelled under section 12AA(3) by merely re-examining the objects of the trust or society [Chaturvedi Har Prasad Education Society vs. CIT (2010) 134 TTI 781 (Luck)].

Power to cancel registration under section 12AA(3) is prospective: Insertion of new clause in section 12AA(3) with effect from 1-6-2010, by which Commissioner has got power to cancel registration granted earlier to assessee-trust under section 12A, is not applicable retrospectively and its operation has to be effective from date it was introduced and onwards. Merely by granting a registration under section 12A/12AA, a trust ipso facto is not entitled to exemption prescribed under sections 11 and 12 [Ajit Education Trust v CIT (2010) 42 SOT 415 (Ahd); Bharati Vidyapeeth vs. ITO (2008) 14 DTR 454; Oxford Academy for Career Development vs. CCIT(2009) 315 ITR 382 (All)].

The Finance Act, 2012 has made the following amendments w.r.e.f. A.Y. 2009-10 for this situation:

The second proviso to section 2(15) provides that in case where the activity of any trust or institution is the nature of advancement of any other object of general public utility, and it involves carrying on of any activity in the nature of trade, commerce or business; but the aggregate value of receipts from the commercial activities does not exceed ₹25,00,000 in the previous year, then the purpose of such institution shall be considered as charitable, and accordingly, the benefits of exemption shall be available to it.

Thus, a charitable trust or institution pursuing advancement of object of general public utility may be charitable trust in one year and not a charitable trust in another year depending on whether its aggregate commercial receipts exceed ₹25,00,000 or not.

There is need to ensure that if the purpose of a trust or institution does not remain charitable due to application of first proviso on account of commercial receipts exceeding ₹25,00,000 in a previous year, then, such trust or institution would not be entitled to get benefit of exemption in respect of its income for that previous year for which such proviso is applicable. Such denial of exemption shall be mandatory by operation of law and would not be dependent on any withdrawal of approval or cancellation of registration or a notification being rescinded. Hence, sub-section (8) has been inserted in section 13 to provide that exemption under sections 11 and 12 shall not be allowed for the previous year in which commercial receipts of such trust exceed ₹25,00,000 whether or not registration is cancelled in respect of that trust.

Where fund or institution had been notified or approved by the Central Government or the prescribed authority under section 10(23C), as the case may be, and subsequently that Government or the prescribed authority is satisfied that—

(i) such fund or institution or trust or any university or other educational institution or any hospital or other medical institution has not,—

   (a) applied its income in accordance with the provisions applicable; or

   (b) invested or deposited its funds in accordance with the provisions; or

(ii) the activities of such fund or trust or institution or any university or other educational institution or any hospital or other medical institution,—

   (a) are not genuine; or

   (b) are not being carried out in accordance with all or any of the conditions subject to which such association was notified or approved,

it may, at any time after giving a reasonable opportunity of showing cause against the proposed action to the concerned fund or institution or trust or any university or other educational institution or any hospital or other medical institution, rescind the notification or, by order, withdraw the approval, as the case may be, and forward a copy of the order rescinding the notification or withdrawing the approval to such fund or institution or trust or any university or other educational institution or any hospital or other medical institution and to the Assessing Officer.

The following incomes of charitable or religious trusts/institutions shall not be eligible for exemption under sections 11 and 12.

(1) Any part of the income from the property held under a trust for private religious purposes which does not enure for the benefit of the public [Section 13(1)(a)].

(2) Any income of trust/institution created/established for charitable purposes on or after 1-4-1962, if such trust or institution is created or established for the benefit of any particular religious community or caste [Section 13(1)(b)]. The exemption is however, available to a charitable trust or institution created or established before 1-4-1962 even if it is for the benefit of any particular religious community or caste.

    A trust or institution created or established for the benefit of Scheduled Castes, backward classes, Scheduled Tribes or women and children shall not be deemed to be a trust or institution created or established for the benefit of a religious community or caste within the meaning of clause (b) of sub-section (1).

(3) Any income of charitable or religious trust or institution created or established after 1-4-1962, if under the terms of the trust or rules governing the institution, any part of the income enures directly or indirectly for the benefit of any person referred to in sub-section 13(3) [Section 13(1)(c)].

(4) Any income of a trust for charitable or religious purposes or a charitable or religious institution (whenever created or established) if any part of such income or any property of the trust or the institution during the previous year is used or applied directly or indirectly for the benefit of any person referred to in section 13(3) [Section 13(1)(c)]. However, exemption is not denied where the trust, etc. is created before 1-4-1962 and such use or application of income is in compliance with a mandatory term of the trust or a mandatory rule governing the institution.

    The above restriction is obviously intended to ensure that, despite the ostensibly charitable objects of such trust or institution, its income is not diverted away to benefit persons who are closely connected with the creation, establishment and conduct of the trust or institution.

    Charitable Trusts not to lose exemption if educational or medical facilities provided to specified persons [Section 13(6)]: A trust running an educational institution or a medical institution or a hospital shall not lose the benefit of exemption of any income under section 11 other than the value of benefits of educational or medical facilities provided to the specified persons referred to in section 13(3), solely on the ground that such benefits have been provided to such persons.

    However, the value of such facilities provided to such specified persons either free of cost or at concessional rate shall be deemed to be income of such trust and shall not be eligible for exemption under section 11.

    The expression ‘value’ shall be the value of any benefit or facility granted or provided free of cost or at concessional rate to any person referred to in clause (a) to clause (e) mentioned in section 13(3).

(5) Any income of a trust/institution, if its funds are invested/deposited otherwise than as specified under section 11(5) [Section 13(1)(d)]. However, the provisions of section 13(1)(d) shall not apply to the under mentioned:

    (i) any asset forming part of the corpus of the trust as on 1-6-1973;

    (ii) any accretion to the corpus shares by way of bonus shares allotted to the trust;

(iii) debentures issued by or on behalf of any company or corporation and acquired by the trust before March 1, 1983;

(iv) any asset not covered under section 11(5) where such asset is held for not more than 1 year from the end of the previous year in which such asset is acquired;

(v) any fund representing the profits and gains of business, being profits and gains of any previous year relevant to the assessment year 1984-85 or any subsequent assessment year. But such relaxation of the restriction will be denied unless the trust keeps separate accounts for the business. As already noted, subject to certain exceptions, such business profits no longer enjoy exemption under section 11.

(6) As per the new section 115BBC, anonymous donation shall now be taxable at the maximum marginal rate of 30%. Consequently, a new sub-section (7) has been inserted in section 13 to provide that nothing contained in section 11 or section 12 shall operate so as to exclude from the total income of the previous year of the person in receipt thereof, any anonymous donation referred to in the new section 115BBC on which tax is payable in accordance with the provisions of that section. In other words anonymous donation shall not be excluded from the total income of the assessee.

A perusal of section 13 of the Income-tax Act, 1961, makes it clear that it carves out an exception to section 11 or 12 by providing that in those cases which are covered by clauses (a), (b), (c) and (d), the provision of section 11 or 12 shall not operate. Broadly speaking, it is divided into three categories and an exception is carved out in the case of private religious trusts, charitable trusts and charitable or religious trusts if the conditions mentioned in clauses (a), (b), (c) and (d) are satisfied. Firstly, any part of the income from the property held under a trust for private religious purposes which does not enure for the benefit of the public is not to be excluded as provided under section 11 of the Act. Secondly, where a trust for charitable purposes or a charitable institution is created or established after the commencement of the Income-tax Act, the authority is required to find out whether the trust for charitable purposes is established for the benefit of a particular religious community or caste. If it is so established, then the provisions of section 11 would not be applicable. Thirdly, clauses (c) and (d) carve out an exception in the case of a trust for charitable or religious purposes or a charitable or religious institution. It provides certain cases in which any income thereof enures, used or applied, directly or indirectly, for the benefit of any person referred to in section 11(3) [now section 13(3)]. In the three different clauses, namely, (a), (b) and (c) of section 13(1) the Legislature has used different phrases. Clause (a) deals with a trust for private religious purposes or a charitable or religious institution. From this different phraseology used by the Legislature in clauses (a), (b) and (c), it can be inferred that the Legislature intended to cover only trusts for charitable purposes under clause (b). That means, if a trust is composite, that is, for religious and charitable purposes, then it would not be covered. It is also apparent that if the trust is only for religious purposes, clause (b) would not be applicable [CIT vs. Barkate Saifiyah Society (1995) 213 ITR 492 (Guj)].

Section 13(1)(c) provides that where a part of the income of a charitable or religious trust or institution enures or is used or applied, directly or indirectly, for the benefit of those persons specified in section 13(3), such a trust or institution shall forfeit the exclusion under section 11. Even if only a small portion of the income enures or is used or applied for the benefit of a person mentioned in section 13(3), the entire income of the trust is denied the exclusion, except in the case provided in section 13(4) [CIT vs. Jamnalal Bajaj Sewa Trust (1988) 171 ITR 568 (Bom)]. However, w.e.f. assessment year 2002-03, as per section 13(6), if the charitable or religious trust is running an educational institution or a medical institution or a hospital, the exemption shall not be denied if the benefit of educational or medical facility is provided to the persons specified under section 13(3). In this case, only the value of such facility provided to such specified person shall be taxable.

Bonds are like debentures and therefore exemption under section 11 could not be denied: Bond is covered by the expression "debenture" and therefore, investment in bonds of certain companies by the assessee, a Charitable Trust did not amount to infringement of the provision of section 13(1)(d) and therefore, exemption under section 11 could not be denied on that ground [DIT vs. Shree Visheswar Nath Memorial Public Charitable Trust (2010) 46 DTR 49 (Del)(Trib)].

Advance paid by assessee an educational institution registered under 12A, to a club towards membership fee for providing certain amenities to the staff and students of the assessee did not attract the provisions of section 13(1)(c) read with section 13(2)(a) as the said club is not a prohibited person as specified in section 13(3). Provisions of section 13(1)(d) were also not attracted as the said advance was neither a deposit nor an investment and therefore, exemption under section 11 is allowable to the assessee more so when the AO has allowed assessee's claim of exemption under section 11 on the same set of facts in the preceding year [Vidya Pratishthan vs. Dy CIT (2010) 44 DTR 145 (Pune)(Trib)].

Once there is a violation of provision of section 13(3) read with section 13(1)(c), the provisions of sections 11 and 12 of the Act shall not operate so as to exclude the income of the trust from the total income of the previous year. According to sections 11 and 12 of the Act, the voluntary contribution made with specific direction that they shall form part of the corpus of the trust or institution, shall not be included in the total income of the previous year of the trust. But once the exemption under sections 11 and 12 is denied, the assessee would not get any protection from sections 11 and 12 and the voluntary contribution would be treated as income, as per the definition of income given in section 2(24) of the Act, according to which income includes the voluntary contribution receipts by a trust credited wholly or partly for charitable or religious purposes or by an institution established wholly or partly for such purposes meaning thereby once the exemption under sections 11 and 12 of the Act is withdrawn all the receipts of the trust either by voluntary contribution or income derived from its property would be an income of the trust in a normal course and is chargeable to tax [Kanahya Lai Punj Charitable Trust vs. DIT (2008) 171 Taxman 134 (Del)].

Persons referred to in section 13(3) are as follows:

(a) The author of the trust or the founder of the institution.

(b) Any person who has made a substantial contribution to the trust or institution, that is to say, any person whose total contribution at the end of the relevant previous year exceeds fifty thousand rupees.

(c) Where such author, founder or person is a Hindu undivided family a member of the family.

(d) Any trustee of the trust or manager (by whatever name called) of the institution.

(e) Any relative of any such author, founder, person, member, trustee or manager as aforesaid.

(f) Any concern in which any of the persons referred to in clauses (a), (b), (c) (d) and (e) has a substantial interest.

Every signatory to the memorandum of association has to be treated as founder: In the case of a charitable institution formed as a company, every signatory to the memorandum of association has to be treated as founder, so that money lent to such a person without adequate security constitutes a benefit, which would deprive the exemption for the company [CIT vs. Charat Ram Foundation (2001) 250 ITR 64 (Del)].

Further, the Supreme Court decided upon who is a founder. It held that the expression 'founder of the institution' used in section 13(3)(a) means that the person concerned should be the originator of the institution, or at least one of the persons responsible for the coming into existence of the institution. Contribution of money is not an inexorable test of a person being a 'founder', though it might happen often that the person who originates an institution may often also fund it [Director of Income-tax vs. Bharat Diamond Bourse (2003) 259 ITR 280 (SC)].

The Board have considered a representation that while filing the Form 10B and is annexure, an auditor can accept as correct the list of persons covered by section 13(3) as given by the managing trustee, etc. The Board agree that an auditor can accept as correct the list of specified persons, till given further instruction, by the managing trustee and base their report on the strength of the certificate [Circular No. 143, dated 20-8-1974].

The income or the property of the trust or institution or any part of such income or property is to be deemed to have been used or applied for the benefit of a person referred to in section 13(3) in the following cases:

(a) Interest free loan or loan without security: If any part of the income or the property of the trust or institution is or continues to be lent to any person referred to in Section 13(3) for any period during the previous year without either adequate security or adequate interest or both [Section 13(2)(a)].

(b) Use of properties without charging adequate rent: If any land, building or other property of the trust or institution is or continues to be, made available, for the use of any person referred to in section 13(3) for any period during the previous year without charging adequate rent or other compensation [Section 13(2)(b)].

Letting out of trust property to an interested person is violation of section 13(2): Where the trust property is let out to a partnership in which the trustee was a partner for a meagre rent, there is clear violation of the requirements of section 13(2)(b), so that the trust has to lose its exemption [Ram Bhawan Dharamshala vs. State of Rajasthan (2002) 258 ITR 725 (Raj)].

(c) Excessive payment for services: If any amount is paid out of the resources of the trust or institution to any of the persons referred to in section 13(3) for services rendered to the trust or institution but such amount is in excess of a reasonable sum payable for such services [Section 13(2)(c)].

(d) Services of trust without adequate remuneration: If the services of the trust or institution are made available to any person referred to Section 13(3) without adequate remuneration or other compensation [Section 13(2)(d)].

(e) Purchase of property for trust for excessive consideration: If any share, security or other property is purchased by or on behalf of the trust or institution from any person referred to in section 13(3) during the previous year for a consideration which is more than adequate [Section 13(2)(e)].

(f) Sale of trust property for inadequate consideration: If any share, security or other property is sold by or on behalf of the trust or institution to any person referred to in section 13(3) during the previous year for a consideration which is less than adequate [Section 13(2)(f)].

(g) Diversion of income or property exceeding ₹1,000: If any income or property of the trust or institution is diverted during the previous year in favour of any person referred to in section 13(3) provided the aggregate value of such income and property diverted exceeds ₹1,000 [Section 13(2)(g)].

(h) Investment in substantial interest concerns: If any funds of the trust or institution are or continue to remain, invested for any period during the previous year (not being a period before the 1-6-1971) in any concern in which any person referred to in section 13(3) has a substantial interest [Section 13(2)(h)].

However, section 13(4) provides that where the aggregate of the funds invested in the said concern does not exceed 5% of the capital of that concern, the exemption under section 11 will be denied only in relation to such income as arises out of the said investment.

Section 13(1)(d) requires that payment for goods or services to interested persons should be commensurate with their value and not excessive: Section 13(1)(d) bars benefit to interested persons but it does not bar any transaction with such interested person. It requires that the payment for such goods or services should be commensurate with their value and not excessive. Thus where an advance was paid to an interested person, being a company in which the trustees were directors, for the purpose of construction of a hospital without security and without interest with the money lying idle throughout the year with the company, it was found to be violation of section 11(5) which bars investments other than those listed therein and section 13(1)(d) which bars benefit to interested person [CIT vs. V.G.P. Foundation (2003) 262 ITR 187 (Mad)].

Assessee a registered society under section 12A, advanced certain sum without any security to its treasurer. It could not furnish any detail about rate of interest and mode of recovery of loan and same was also not reflected in its books as well as audit report except resolution which could not be relied upon. It was a clear case of violation of section 13 and exemption had been rightly denied to it [CIT vs. Audh Educational Society (2011) 203 Taxman 166 (All)].

Return of Income

Every person who is in receipt of the following income, if such income (computed before allowing any exemption under sections 11 and 12) exceeds the maximum amount not chargeable to tax, must file a return of income in respect of:

(a) income derived from property held under trust or other legal obligation wholly or partly for religious or charitable purposes, or

(b) income by way of voluntary contribution on behalf of such trust or institution.

The return of income must be furnished in Form ITR-7 and verified in the prescribed manner containing all the prescribed particulars. Such return of income must be furnished by the representative assessee within the time prescribed under section 139(1).

The funds under section 10(23C) whose income is exempt from income tax

Any income received by any person on behalf of the following is exempt from tax:

(a) The Prime Minister's National Relief Fund; or

(b) The Prime Minister's Fund (Promotion of Folk Art); or

(c) The Prime Minister's Aid to Students Fund; or

(d) The National Foundation for Communal Harmony; or

(e) The Swachh Bharat Kosh, set up by the Central Government; or

(f) The clean Gange Fund, set up by the Central Government; or

(g) Any university or other educational institution existing solely by for educational purposes and not for purpose of profit and which is wholly or substantially finance by the Government [Sub-clause (iiiab)]; or

(h) Any hospital or other institution for the reception and treatment of persons (i) suffering from illness or (ii) mental defectiveness or (iii) during convalescence or (iv) requiring medical attention or rehabilitation, existing solely for philanthropic purpose and not for purpose of profit and which is wholly or substantially financed by the Government [Sub-clause (iiiac)]; or

(i) Any university or other education institution existing, solely for educational purposes and not for purpose of profit if the aggregate annual receipts of such university or education institution do not exceed ₹1,00,00,000 [Sub-clause (iiiad)]; or

(j) Any hospital or other medical institution for the purpose mentioned in clause (f) above where aggregate annual receipts do not exceed ₹1,00,00,000 [Sub-clause (iiiae)]; or

(k) Any other fund or institution established for charitable purposes which may be approved by the prescribed authority having regards to its object and its importance throughout India or throughout any State or States [Sub-clause (iv)]; or

(l) Any trust (including any other legal obligation) or institution wholly for public religious purposes or wholly for public religious and charitable purposes which may be approved by the prescribed authority having regard to the manner in which the affairs of the trust or institution are administered, and supervised for ensuring that the income accruing thereto is properly applied for the objects thereof [Sub-clause (v)]; or

(m) Any university or other educational institution existing solely for educational purposes and not for purpose of profit other than those mentioned in clause (e) and (g) above i.e. whose aggregate annual gross receipts exceed ₹1,00,00,000 [Sub-clause (vi)]; or

(n) Any hospital or other institution for the purpose mentioned in clause (f) above but other than those mentioned in clause (f) and (h) above i.e. whose aggregate annual receipts exceed ₹1,00,00,000 [Sub-clause (via)].

Conditions to be satisfied for claiming exemption under section 10(23C)

The conditions for claiming exemption under section 10(23C) are as under:

	University or educational institution or hospital or medical institution who are substantially financed by the Government [Section 10(25C)(iiiab) and (iiiac)]	University or educational institution or hospital or medical institution whose aggregate annual gross receipts do not exceed ₹1crore [Section 10(23C) (iiiad)and (iiiae)]	University or educational institution or hospital or medical institution whose aggregate annual gross receipts exceed ₹1 crore [Section 10(23C)(vi) or (via)]	Charitable or religious institution covered under section 10(23C)(iv) or (v)
Whether application for grant for exemption necessary	No	No	Yes, approval is necessary	Yes, approval is required
Form in which application is to be made and to whom it should be made	NA	NA	Form No. 56D to the jurisdictional Chief Commissioner of Income Tax or Director General of Income Tax	Form No. 56 to the Director General of income Tax (Exemption)
Time period within which application is to be made	NA	NA	If application is made on or after 1.4.2009, it shall be made on or before 30th September of the relevant assessment year from which exemption is sought. Prior to this it was required to be made before the end of the relevant assessment year.	If application is made on or after 1.4.2009, it shall be made on or before 30th September of the relevant assessment year from which exemption is sought. Prior to this it was required to be made before the end of the relevant assessment year.
Period of the validity of exemption	NA	NA	If application has been made on or after 13.7.2006, it is a permanent exemption unless withdrawn. However, if application has been made before 13.7.2006, the exemption will be for a period of three years and fresh application shall have to be made after the expiry of un-expired period of 3 years which shall also be permanent exemption unless withdrawn	If application has been made on or after 13.7.2006, it is a permanent exemption unless withdrawn. However, if application has been made before 13.7.2006, the exemption will be for a period of 3 years and fresh application hall have to be made after the expiry of un- expired period of 3 years which shall also be permanent exemption unless withdrawn

Time period within which exemption has to be granted or rejected	NA	NA	If application is made on or after 13-7-2006, its approval is to be granted or rejected within a period of 2 months from the end of the month in which application as received by the authorities	If application is made on or after 13-7-2006, its approval is to be granted or rejected within a period of 12 months from the end of the month in which application was received by the authorities
Whether Audit of Accounts is compulsory	No	No	Yes	Yes
Whether it is mandatory to file return of income	No	Yes	Yes	Yes

Where an assessee was already registered under section 12A and was also exempt under section 10(23C)(iv), the audit report filed in Form 10B instead of Form 10BB could not by itself lose exemption for the institution, since the mistake is a technical one. The difference in the Forms also did not make a difference in the spirit or the requirements of law [National Horticulture Board vs. CCIT (2009) 319 ITR 74 (P&H)].

Where the assessee society was having multiple objects of which education was one of them, and the Director of Exemption had denied registration to the society under section 10(23C)(vi) merely on the suspicion that the society might deviate from its objective of education in future. It was held that the assessee could be given benefit of exemption under section 10(23C)(vi) subject to an affidavit of undertaking given by the assessee-society that it would not breach any of condition or stipulations imposed by the section and further that surplus fund would be utilized only for educational purpose and would not be diverted to other non educational objectives [Digamber Jain Society for Child Welfare vs. DGIT (Exemption) (2009) 185 Taxman 255 (Del)].

Merely because surplus had arisen to the assessee whose total receipt did not exceed 1 crore by running two scheme it was not required to get any approval from prescribed authority and hence Assessing Officer was not justified in refusing the exemption under section 10(23)(iiiad) [Gagan Education Society vs. Addl CIT(2011) 56 DTR 199 (Agra) (Trib)].

Where the petitioners application seeking exemption under section 10(23C)(vi) was rejected on the ground that the object of the petitioner does not exist solely for educational purpose. It was held that, the 'education' means process of training and developing, knowledge, skill, mind and character of students. Activities such as maintaining, library, conducting classes of stitching, weaving, embroidery and adult education, fall within 'education'. Sports and recreational activities also fall with in modern concept of education. Educational society running school having such other objects cannot be denied approval under section 10(23C)(vi) on ground that society is not existing solely for educational purpose [Little Angles Shiksha Samiti Dal Bazaar, Gwalior & Anr. vs. UOI (2011) Tax L.R 941 (MP)].

Where Petitioner University was created under section 3 of Haryana Private University Act, 2006 and it obtained recognition from the Bar Council of India as well as University Grants Commission and also set up infrastructure for starting law courses, it was held that it is an existing educational institution and therefore entitled to approval. Rejection on the ground that petitioner is yet to commence educational activities is set aside and the Commissioner was directed to pass an order granting approval under section 10(23C)(vi) [O. P. Jindal Global University vs. CCIT (Exemption) (2011) 64 DTK 22 (P&H)].

Where assessee society which is teaching and promoting all forms of music and dance, western, Indian or any other form and is run like school or educational institution in a systematic manner with regular classes, vacations, attendance requirements, enforcement of discipline and so on meets the requirement of educational institution within the meaning of section 10(23C)(vi), the High Court quashed the order of prescribed authority and directed to pass the order by giving a reasonable opportunity [Delhi Music Society vs. DIG (2012) 65 DTK 337/246 CTR 327 (Del)].

Other conditions for claiming exemption:

The fund, trust or institution covered under section 10(23C)(iv), (v), (vi) and (via) should satisfy the following additional conditions to claim exemption under this section:

(1) At the time of making application in Form No. 56 or 56D, it should furnish such documents (including Audited Annual Accounts) or information which the Central Government or the prescribed authority as the case may be, may consider necessary in order to satisfy itself about the genuineness of the activities of the fund or trust or institution/university/hospital, etc. and the Central Government or the prescribed authority, as the case may be, may also make such enquiries as it deems necessary in this behalf.

(2) (a) it should apply its income, or accumulate it for application, wholly and exclusively to the objects for which it is established and in a case where more than 15% of its income is accumulated, the period of the accumulation of the amount exceeding 15% of its income shall in no case exceed 5 years; and

(b) it should not invest or deposit its funds for any period during the previous year otherwise than in any one or more of forms or mode specified in section 11(5).

However the following are the exceptions to the above requirement of funds to be invested as per provisions of section 11(5).

(i) Where assets held form part of the corpus of the fund, trust or institution or any university or other educational institution or any hospital or other medical institution as on 1-6-1973;

(ii) Where asset, being equity shares of a public company, held by any university or other educational institution or any hospital or other medical institution which form part of its corpus as on 1-6-1998.

(iii) Where assets (being debentures issued by, or on behalf of, any company or corporation), were acquired by the fund, trust of institution or any university or other medical institution before 1-3-1983;

(iv) Where there is any accretion to the shares, forming part of the corpus mentioned in sub-clause (i) and (ii) above, by way of bonus shares allotted it;

(v) Where voluntary contributions are received and maintained in the form of jewellery, furniture or any other article as the Board may, by notification in the official gazette, specify;

(vi) Where voluntary contribution is received in kind, it has not been held in a mode other than 11(5) after the expiry of one year from the end of the previous year in which such asset is acquired.

1. The grant of exemption from income tax will not apply to any income in the nature of profits and gains of business unless the business is incidental to the attainment of its objectives and separate books of account are maintained by it in respect of such business.

2. Certain funds, trusts and institutions running hospitals, creches orphanages, school, etc. often receive donation in kind from various sources for application towards their charitable purposes. These contributions may be in the shape of books, clothes for the poor, grains to feed the poor, drugs, hospital equipments, etc.

Since the donation in kind, of a nature referred to above, received by a fund, trust or institution would be income within the meaning of section 2(24) of the Act, it is clarified that the use of these towards object for which the fund, trust or institutions is established would be regarded as application of the income of the fund, trust or institution [Circular No. 580, dated 14-9-1990].

(I) An educational trust or other similar body running an educational institution solely for educational purposes and not for purposes of profit would be regarded as other educational institutions [Aditanar Educational Institution vs. Addl. CIT (1997) 224 ITR 310 (SC)].

(II) Even if an educational institution made profit and such profits were applied only for the spread of education, it was entitled to exemption under section 10(22) of the Act [CIT vs. Delhi Kannada Education Society (2000) 246 ITR 731 (Del). Also see CIT vs. Lagan Kala Upvan (2003) 259 ITR 489 (Del)].

(III) The assessee running several schools employing more than one thousand teachers and nuns and imparting education to several thousand students is entitled to exemption under section 10(22) [now 10(23C)]. Activity of running a dispensary for the benefit of students and teachers, running a church for the benefit of nuns and running an orphanage for the benefit of abandoned children did not detract from the educational activities earned on by the assessee [DIT vs. Institute of The Franciscan Clarist Sister of the Most Blessed Sacrament (2005) 196 CTR 582 (Del)].

(IV) Merely because the assessee has undertaken research projects at instance of Government or local bodies and has taken remuneration for such projects, the character of assessee foundation could not be said to have been converted into one which carried on commerce or business or activity or rendering any service in relation to trades, commerce or business. Such foundation is an educational institution and eligible for grant of exemption under section 10(23C)(iv).

(V) The conditions precedent for availing of exemption to an educational institution under section 10(23C) or section 11 of the Income-tax Act, 1961, are as follows:

 (a) the educational institution must actually exist for application of the said provision and mere taking of steps would not be sufficient to attract the exemption;

 (b) the educational institution need not be affiliated to any university or Board and in fact it need not itself be imparting education and it is enough if it runs some schools or colleges;

 (c) the educational institution must exist solely for educational purposes and not for purposes of profit. But merely because there is a surplus, that is to say a surplus of receipts over expenditure it cannot be said that the educational institution exists for profit;

 (d) an entity may be having income from different sources, but if a particular income is from an educational institution which exists solely for educational purposes and not for purposes of profit, then that income would be entitled to exemption and further the income

 (e) should be directly relatable to educational activity [CIT vs. Delhi Kannada Education Society (2000) 246 ITR 731 (Del)].

(VI) The term "other educational institutions" is a narrower concept: Where a trust conducted english improvement classes for standards X, XI, and XII and also conducted guidance classes for C.A. entrance examinations, it also held refresher courses for english language teachers and guidance courses for banking service recruitment and similar activities, it was held that although the activities of the assessee were connected with formal education being given by other educational institutions running schools or colleges, the assessee did not run any composite or integrated course of organized and systematic training. The assessee was not affiliated to or registered by, any authority. Such a trust can certainly be considered as qualifying, for exemption under section 11(1)(a) read with section 2(15) but the term "other educational institutions" contemplated by section 10(23C), is a narrower concept. Though educational institution and educational activities are closely interconnected, in section 11(1)(a) read with section 2(15), it is the activities which are in focus, whereas in section

10(23C) both the institution and the activities are in focus. Therefore, an educational institution under section 10(23C) is more than a body carrying on charitable activities in the field of education as contemplated by section 2(15). The expression "other educational institution" in the section would mean an institution imparting formal education in an organized and systematic manner. Where the institution would be accountable to some authority and where there would be teachers and the taught, the former having some degree of control over the later. Although, the expression other education institution may not be confined to schools or colleges, the expression does contemplate an institution imparting formal education or training [Saurashtra Education Foundation vs. CIT (2005) 273 ITR 139 (Guj)].

(VII) Where applicant had earlier obtained exemption under section 10(22) and after omission of said section applies for first time for initial approval in terms of section 10(23C)(vi), prescribed authority must give an opportunity to applicant-institute to comply with monitoring conditions which have been stipulated for first by third proviso to section 10(23C) [American Hotel & Lodging Association, Educational Institute vs. CBDT (2008) 170 Taxman 306 (SC)].

Donation to other trust/institutions, etc out of accumulated income shall not be treated as application of income: Where the above fund or trust or institutions (i.e. covered under section 10(23C)(iv), (v), (vi) and (via) do not apply its income during the year of receipt and accumulates it, any payment or credit out of such accumulation to any trust or institution registered under section 12AA or to similar type of fund or trust or institution or any university or other educational institution shall not be treated as application of income to the objects for which it was established.

Anonymous donation received by the trust or institution covered under section 10(23C)(iiiad), (iiiae), (iv), (v), (vi) and (via) shall also be taxable under section 115BBC.

Where such fund or institution had been notified or approved by the Central Government or the prescribed authority, as the case may be, and subsequently that Government or the prescribed authority is satisfied that—

(i) such fund or institution or trust or any university or other educational institution or any hospital or other medical institution has not applied its income in accordance with the provisions or invested or deposited its funds in accordance with the provisions

(ii) the activities of such fund or trust or institution or any university or other educational institution or any hospital or other medical institution,—

(A) are not genuine; or

(B) are not being carried out in accordance with all or any of the conditions subject to which such association was notified or approved,

it may, at any time after giving a reasonable opportunity of showing cause against the proposed action to the concerned fund or institution or trust or any university or other educational institution or any hospital or other medical institution, rescind the notification or, by order, withdraw the approval, as the case may be, and forward a copy of the order rescinding the notification or withdrawing the approval to such fund or institution or trust or any university or other educational institution or any hospital or other medical institution and to the Assessing Officer.

A charitable trust or institution pursuing advancement of object of general public utility may be charitable trust in one year and not a charitable trust in another year depending on whether its aggregate commercial receipts exceed ₹25,00,000 or not.

Hence, seventeenth proviso has been inserted to section 10(23C) to provide that exemption shall not be allowed for the previous year in which commercial receipts of charitable trust or institution referred to section 10(23C)(iv) or (v) exceed ₹25,00,000 whether or not approval has been withdrawn or rescinded in respect of such trust. Further, 3rd proviso has been inserted in section 143(3) to provide that first and second proviso to section 143(3) shall not be applicable where in any previous year commercial receipt of such trust exceed ₹25,00,000. In other words, Assessing Officer shall not give exemption to such trust covered under section 10(23C)(iv) or (v) even if approval has not been withdrawn or rescinded.

9.9 ASSESSMENT OF MUTUAL ASSOCIATION

Assessment of Mutual Association

To constitute a mutual association, a number of persons associate together to subscribe money for a fund for the purpose of its being spent upon a particular object, and the balance, if any, being returned to the subscribers and proportionately distributed among them. This balance is that part of the fund which is not absorbed by the particular object of the subscriptions. Those transactions are mutual dealings and the unrequired balance is the surplus. This surplus is not assessable to income-tax since it arises out of the mutual dealings. [General Family Pension Fund vs. CIT (1946) 14 ITR 488 (Cal)].

No person can trade with himself and make an assessable profit. If, instead of one person, more than one combine themselves into a distinct and separate legal entity for rendering services to themselves by only charging themselves, the resulting surplus is not assessable to tax, [CIT vs. Merchant Navy Club (1974) 96 ITR 261 (AP)].

The basis for exemption of the income of the mutual association are as follows:

(1) common identity of contributors and participators,

(2) the treatment of the assessee, though incorporated, as a mere entity for the convenience of the members, and

(3) the impossibility of the contributors deriving profit from the contribution made by themselves to a fund which could only be expended or returned to themselves.

(1) Common identity of contributors and participators

The essence of mutuality lies in the return of what one has contributed to a common fund, and, unless there is complete identity between the contributors and the participators in a common fund, the principle of mutuality would not be attracted. If some of the contributors to the common fund are not participators in the surplus or if some of the participators in the surplus are not contributors to the common fund, the profits of the association would be assessable to tax.

However, the criterion that the contributors to the common fund and participators in the surplus must be an identical body does not mean that each member should participate in the surplus or get back from the surplus precisely what he has paid. What is required is that the members as a class should contribute to the common fund and as a class they must be able to participate in the surplus. [CIT vs. Merchant Navy Club (1974) 96 ITR 261 (AP)].

(2) The treatment of the assessee, though incorporated, as a mere entity for the convenience of the members

If there is a common identity of contributors and participators, the particular form which the association takes is immaterial.

Incorporation as a company or as a registered society is a convenient medium for enabling the members to conduct a mutual concern. The property of the incorporated company or registered society, for all practical purposes, in the case of a mutual enterprise, is considered as the property of the members.

The incorporation of any company to carry on the activities of a club does not result in the deprivation of the admissibility of the claim for exemption based on the concept of mutuality. [CIT vs. Madras Race Club (1976) 105 ITR 433 (Mad)].

Even a company assessee can claim exemption on the basis of mutuality principle where its memorandum and articles of association provided that the funds of the company should be utilised solely for the promotion of its objects and that no portion of the income or property shall be paid or transferred directly or indirectly, by way of dividends, bonus to any member or former member. [CIT vs. Escorts Dealers Development Association Ltd. (2002) 253 ITR 305 (P&H)].

(3) The impossibility of the contributors deriving profit from the contribution made by themselves to a fund which could only be expended or returned to themselves

A mutual association is an association of persons who agree to contribute funds for some common purpose mutually beneficial and receive back the surplus left out of these funds in the same capacity in which they have made the contributions. This capacity as contributors and recipients remains the same. They contribute not with an idea to trade but with an idea of rendering mutual help. They receive back the surplus, which is left after meeting the expenditure which they have incurred for this common purpose, in the same capacity in which they have contributed. Thus, they receive back what was already their own. The receipt which thus comes in their hands, is not profit, because no man can make a profit out of himself, just as he cannot trade with himself. [CIT vs. Shree Jari Merchants Association (1977) 106 ITR 542 (Guj)].

The participation in the surplus need not be immediate as soon as the surplus is discerned, but may be on the winding up or dissolution, the surplus for the time being carried to a reserve.

The surplus may be handed back, it may be kept for some future contingency; the test is whether it is the members' money.

The mutuality principle which is true in the case of an individual is equally true in respect of bodies of individuals, such as, (A) a members' club, (B) a co-operative society, (C) a mutual benefit fund, (D) a thrift fund, or (E) a pooling association.

Members' club — Members' club are, without doubt, cent per cent mutual associations. They are co-operative bodies whereby the members raise funds by way of entrance fees and periodical subscriptions in order to provide themselves with social, sporting or similar other amenities.

One among the popular activities of such a club is the providing of refreshments to the members for a charge to cover the cost of preparation, overheads and service. If such refreshments be served to non-members, it would only be on the basis of such non-members being guests of the member who pays for himself and his guest.

Another popular activity of a club is the providing of residential rooms to nonresident members and mofussil members and supplying them with board for a charge to cover the rent of the rooms and the cost of the food and overhead.

Amenities are also provided for sports, such as, billiards, tennis, golf or cards, at a charge to compensate the maintenance of the tennis-court, or golf-course, or the cost of the playing of cards or the wear and tear of the billiard table.

The above are all activities of any social club and there is no element of buying and selling in the providing of these amenities for a certain fee. It is a fallacy to say that where a member of a club orders for dinner and consumes it, there is any sale to him.

In the case of CIT vs. Bankipur Club Ltd. (1997) 226 ITR 97 (SC) the Supreme Court has held that the receipt for various facilities extended by the club to members as part of the usual privileges, advantages and conveniences, attached to the membership of the club, could not be said to be a trading activity. The surplus of excess of receipts over the expenditure as a result of mutual arrangement could not be said to be "Income" for the purpose of Income Tax Act.

The fact that the members are also allowed to entertain their guests shall not be considered to be a disqualification [CIT vs. Darjeeling Club Ltd. (1985) 153 ITR 676 (Cal)].

The fact that there is some diversion to non-members as it happened when some of the rooms were let out to non-members need not vitiate the principle of mutuality as long as there is substantial compliance with the principle. [CIT vs. Delhi Gymkhana Club Ltd. (1985) 155 ITR 373 (Del)]. It may be pointed out that if the amount involved is substantial, the decision could have been otherwise.

In case the business of the assessee was governed by doctrine of mutuality, not only the surplus from the activity of the club but even the annual value of the club house would be outside the purview of the levy of income-tax. [Chelmsford Club vs. CIT (2000) 243 ITR 89 (SC)].

If the society had a convention centre with catering facilities primarily meant for the use of its member, but derived rental income from others, when it was free. Interest was also derived from funds meant for gratuity of its secretariat office. It was for this reason that the exemption was denied. The High Court while endorsing the decisions of the Tribunal pointed out that there was no commercial activity and the income from non-members was merely incidental to its service to members. [CIT vs. Standing Conference of Public Enterprises (SCOPE) (2009) 319 ITR 179 (Del)].

Interest income of a sports club derived from deposits with bank is not exempt on the ground of mutuality. [Rajpath Club Ltd. vs. CIT (1995) 211 ITR 379 Guj].

In order to get the benefit of the principle of mutuality, the association should confine its activities only as between members. Where such an association banks its surplus funds in fixed deposits it was held that such income from bank interest could not be exempt as banks are not the members of such association. [CIT vs. Bangalore Club (2006) 287 ITR 263 (Karn)].

Investment of surplus fund with some of member banks and other institutions in form of fixed deposit and securities which, in turn resulted in earning of huge interest could not be held to satisfy mutuality concept and, therefore, such interest income was liable to be taxed. [Madras Gymkhana Club vs. DCIT (2009) 183 Taxman 333 (Mad)].

If assessee-company is running a recreation club for its members, the income earned from the members is exempt on the principle of mutuality. Income of the club from FDR's in banks and Government securities, dividend income and profit on sale of investment is also covered by the doctrine of mutuality and is not taxable. [CIT vs. Delhi Gymkhana Club Ltd. (2011) 53 DTR 330 (Del)].

Interest income on investments with banks is not exempt on the principle of mutuality even though the concerned banks are members of the club. [CIT vs. Wellington Gymkhana Club (2010) 46 DTR 22 (Mad)].

Interest income earned on bank deposits made by a club was not income arising out of mutual activities/arrangement among members of club and hence taxable. [Amur Singh Club vs. Union of India (2009) 184 Taxman 481 (J&K)].

However, in CIT vs. Saraswati Kunj Co-operative House Building Society (2006) 287 ITR 22 (Del) it was held that the interest on money kept in saving bank account would be a capital receipt not liable to tax.

Interest on investment and dividend on shares earned by a mutual association, though a co-operative society, will be governed by the principle of mutuality and therefore will not be taxable. [Canara Bank Golden Jubilee Staff Welfare Fund vs. DCIT (2009) 308 ITR 202 (Kar)].

Further, where the trade or activity is mutual, the fact that, as regards certain activities, only certain members of the association take advantage of the facilities which it offers, does not affect the mutuality of the enterprise. But if the object of the assessee-company claiming to be a mutual concern or club, is to carry on a particular business and the money is realised both from the members and the non-members, for the same consideration by giving the same or similar facilities to all alike in respect of the one and the same business carried on by it, the dealings as a whole, disclose the same profit earning motive and are alike tainted with commerciality and the resultant surplus is profit-income liable to tax.

In the case of Joint Commercial Tax Officer vs. Young Men's Indian Association (1970) 26 STC 241, 247 (SC), the Supreme Court observed that if the club even though a distinct legal entity is only acting as an agent for its members in the supply of various preparations to them, no sale would be involved as the element of transfer would be completely absent.

A club is taxable on the profit derived from subscriptions and charges paid by non-members and on the income derived from its capital assets and investment. [Rajpath Club Ltd. vs. CIT (1995) 211 ITR 379 (Guj)].

An enterprise annexed by a club to its activities by way of extending its amenities to members of the public, the sums realised on such extensions would be outside the surplus attributable to mutual activities. Consequently, the receipts from the public or non-members would be income of the club in the eyes of law.

Likewise, rent received from members by a club for providing temporary accommodation to them as part of the amenities provided to them cannot constitute income. Where the income of the club from house property was not the outcome of any mutuality, even though the said income was utilised for the benefit of members, it could not be excluded from the arena of taxation.

If the services of the club are open to non-members then the identity of the contributors and that of the recipients would be lost. In such case the assessee may not be eligible for the exemption. [CIT vs. Royal Western India Turf Club Ltd. (1953) 24 ITR 551 (SC)].

In case the real contributors of income who availed of the facilities of the marriage hall were not the members and in order to enable them to avail of the facilities of the club, non-members were to be given temporary membership only for the purpose of availing of this benefit, it was held that the marriage hall was admittedly being rented out to non-members making them temporary members only for the purpose of letting out the marriage hall to non-members, the principle of mutuality would not apply and the rental income received from non-members was taxable. [CIT vs. Trivandrum Club (2006)282 ITR 505 (Ker)].

The assessee, a club, running on mutuality basis, had collected amounts from non-members for use of the assessee's premises as floor charges for trading in shares and stocks, it was held that the principle of mutuality could have no application to receipts of such charges. [Investors Club Trichur vs. CIT (2009) 318 ITR 427 (Ker)].

Trade associations as Mutual Associations— Many trade associations which were also undertaking activities of distribution of goods or services were held not assessable as a mutual association. [Mill Owners Mutual Insurance Association Ltd vs. CIT 6 ITC (Bom) 7; CIT vs. Bombay Oil Seeds and Oil Exchange Ltd (1993) 202 ITR 198 (Bom.) and CIT vs. West Godavari District Rice Millers' Association (1984) 150 ITR 394 (AP)].

Where the profits of such association did not go to a common fund, exemption on grounds of mutuality was held inadmissible. [Jaipur Slock Exchange Ltd vs. ITO (1995) 54 ITD 589 (Jaipur-Trib)]. In this case, Special Leave Petition was dismissed. In the case CIT vs. Northern India Motion Pictures Association (1994) 207 ITR (St.) 10, exemption was allowed and SLP was dismissed.

It is also possible that, some of the items like subscriptions and entrance fees may qualify for exemption on principle of mutuality, while other receipts like service charges may not so qualify, where such charges are collected from non-members or where disparity between the contributors and the participants is marked. But it is equally established that there need be no identity in the sense of complete quid pro quo as between the contributors and participants. In other words, there is no stipulation that every contributor must also be a participant.

However, where a hire purchase company claimed exemption of receipts on account of subscription charges of hirer member on account of principle of mutually, the claim was disallowed since such hirer members have no right to vote and no right to decide the destiny of the surplus on winding up. Further, their membership is temporary as it ceases as soon as the hiring is over Upper India Hire Purchase Co. vs. CIT (2001) 251 ITR 642 (Del).

Co-operative societies — A co-operative society is defined in section 2(19) of the Income Tax Act as a co-operative society registered under the Co-operative Societies Act, 1912, or under any other law for the time being in force in any State for the registration of co-operative societies. Turning to the Co-operative Societies Act, 1912, some of its important provisions may be noticed:

(1) Section 4 of the said Act provides that a society which has as its object the promotion of the economic interest of its members in accordance with co-operative principles (emphasis supplied), or a society established with the object of facilitating the operations of such a society, may be registered under this Act;

(2) Section 29(1) further provides that 'a registered society' shall not make a loan to any person other than a member provided that with the general or special sanction of the Registrar, a registered society may make loans to another registered society;

(3) Section 30 restricts the powers of the society in respect of its receiving any deposits or loans from persons who are not members of the society;

(4) Section 31 restricts the transactions of societies with non-members;

(5) Finally, section 33 provides that no part of the funds of a registered society shall be divided by way of bonus or dividend or otherwise among its members; provided that after at least one-fourth of the net profits in any year have been carried to a reserve fund, payments from the remainder of such profits and from any profits of past years available for distribution may be made among the members to such extent and under such conditions as may be prescribed by rules.

Section 34 further enacts that out of the balance left u/s 33, an amount not exceeding ten per cent thereof may be contributed to a charitable purpose with the sanction of the Registrar.

The above provisions show that a co-operative society is a mutual society and, on mutual principles, would not be earning any income in the eye of law. Transfer fee received by a co-operative housing society is not assessable since the co-operative housing society is a mutual concern and the persons became members of the society before they were entitled to get the flat transferred in their names or were liable to pay the transfer fees. There is an element of mutuality in respect of the transfer fees and therefore the same are not taxable. [CIT vs. Apsara Co-op Housing Society Ltd (1993) 204 ITR 662 (Cal). See also Director of Income-tax vs. All India Oriental Bank of Commerce Welfare Society (2003) 130 Taxman 573 (Del); Ludhiana Agganval Co-operative House Building Society Ltd vs. ITO (1995) 55 ITD 423 (Chd); ITO vs. Mumbai Hindi Shikshak Sayahak Nidhi (1985) 22 TTJ (Bom) 133].

Transfer fee received by a co-operative housing society whether from outgoing or from incoming members is not liable to tax on ground of principle of mutuality where predominant activity of such co-operative society is maintenance of property of society. [SIND Co-op Housing Society vs. ITO Pune (2009) 182 Taxman 346 (Bom)].

Transfer fee and non-occupancy charges received by assessee are not taxable in the hands of the assessee as being governed by principle of mutuality. [Mittal Court Premises Co-operative Society Ltd. vs. ITO (2009) 184 Taxman 292 (Bom)].

The assessee was a Co-operative Housing Building Society established with the specific objective of purchasing agricultural land for development as plots which were to be allotted to its own members. The assessee entered into an agreement with the State Government, which stipulated that the assessee would keep 30% amount realized from plot holders in bank deposit for being utilized by the assessee towards meeting the cost of internal development work in the colony and it would not derive any profit out of sale of plots to its members. Assessing Officer treated the interest earned on said deposit as revenue income. It was held that the money kept in savings bank account had inextricable link with acquisition of land and interest earned on the said deposit would be a capital receipt. [CIT vs. Saruswati Kitnj Co-operative House Building Society (2006) 287 ITR 22 (Del)].

Interest income earned by an assessee on surplus fund of a mutual society deposited with a banking institution is covered by the principle of mutuality. [Shivalika Cooperative Group Housing Society Ltd. vs. ITO (2007) 289 ITR (AT) 105 (Del)].

If a co-operative housing society collects contributions from members for an amenity fund for repairs, besides collecting contributions for a welfare fund from new members in pursuance of bye-laws framed under the Maharashtra Co-operative Societies Act, there was no violation of the mutuality principle because of these collections. Further the collection of non-occupation charges would also have a similar character. [Mittal Court Premises Co-operative Society Ltd. vs. ITO (2010) 320 ITR 414 (Bom))].

Assessee, a co-operative housing society, was formed for the development and construction of residential houses/flats for its members and to provide them necessary common amenities and facilities, and therefore the principle of mutuality would apply to the income of the society, including the income from sale of shops. Principle of mutuality is attracted also to the interest derived from deposits made by the society out of contribution made by its members. [CIT vs. Talangang Co-operative Group Housing Society Ltd (2010) 44 DTR 58 (Del)].

Pooling associations — Pooling associations are formed to maintain prices, to open, up markets for goods, or to demarcate areas for trade operations. The activities of such associations cannot also be said to bring any profit which can be taxed under the Income Tax Act. An association of traders collecting subscriptions or donations from its members for construction of a building will be a mutual concern although its memorandum may enable its assets to be given to an association with allied objects in the event of its dissolution. [CIT vs. West Godavari District Rice Millers" Association (1984) 150 ITR 394 (AP)].

The aforesaid general observation that mutual activities of a mutual concern do not return taxable income is, however, subject to the following four exceptions expressly provided in the Act:

(1) Income accruing to a life or non-life mutual insurance concern from the business of such insurance is liable to tax [Section 2(24)(vii)].

(2) Income derived by a trade, professional or similar association from specific services performed for its members are chargeable to tax [Section 2(24)(v) read with section 28(iii)].

(3) Income of insurance business carried on by a co-operative society is taxable in all cases (even if it is a mutual concern) and is to be computed in accordance with the rules in the First Schedule [Section 2(24)(vii)].

(4) The profits and gains of any business of banking (including providing credit facilities) carried on by a co-operative society with its members [Section 2(24)(viia)].

Trade and professional association means an association of traders or professionals for the protection or advancement of their common interest.

Income arising to such trade or professional associations shall be taxable only when such income arises from performing specific services to members. If any entrance fee is taken by these associations, that fee shall not be taxable.

This is an exception to the general principle that a surplus arising to mutual association cannot be regarded as income chargeable to tax. Every trade, professional or similar association which renders specific services to its own members for remuneration related to those services would come within the purview of this sub-section. [Indian Tea Planter's Association Ltd. vs. CIT (1971) 82 ITR 322 (Cal)]. It may however be noted that income derived by a social club/resident welfare association, etc. shall be exempt even if the specific services are rendered by it to its members as these are not trade, professional or similar association. In order to bring an income within this clause two essential facts have to be established, namely that the association rendered specific services to its members and that remuneration was paid by the members for these services, and there must be a connection between remuneration and the service rendered. [Ismaillia Grain Merchants Association Ltd. vs. CIT (1957) 31 ITR 433 (Bom)].

Any income derived by a trade, professional or similar association for rendering specific services to its members is taxable under section 28(iii). But any surplus of other receipts over the expenses from mutual activities of such association is not chargeable to tax as it is of mutual character. Since excess of such surplus is not taxable, if there is any deficiency instead of the surplus, it should normally not be allowed to be set off against taxable income of such association. Section 44A provides a special advantage where such deficiency shall be allowed to be set off from the assessable income of such association subject to the following conditions being satisfied:

(i) The assessee is a trade, professional or similar association other than an association covered under section 10(23A). Section 10(23A) exempts the income of approved association or institutions established in India having its object — the control, supervision, regulation or encouragement of the profession of law, medicine, accountancy, engineering or architecture or such other notified profession. Provisions of section 44A shall not be applicable to these association or institutions.

(ii) Such association should not distribute any part of its income to its members except as grants to any association or institution affiliated to it.

If the above conditions are satisfied, the amount of any deficiency will be allowed from the assessable income of such association to the extent of 50% of the assessable income, as arrived at before allowing this deduction.

The aforesaid deduction will be allowed first from the income of such association chargeable under the head profits and gains from business or profession and the balance amount, if any, from the assessable income of the association under any other head.

The said deduction will be allowable from the net assessable income of the association as computed after giving effect to the provisions in the Income Tax Act for the carry forward of unabsorbed depreciation, and past business losses.

Deficiency means the excess of expenditure (other than capital expenditure or not being expenditure deductible in computing the income under any other provisions of the Act) incurred for the advancement of the common interest of the members of the association concerned, over receipts from its members. Such receipts will not include any remuneration for rendering any specific services to the members of such association.

In other words it will be computed as under:

Step 1 Take expenditure incurred by such association. Expenditure does not include capital expenditure or any expenditure deductible in computing the income under any other provisions of the Act.

Step 2 Deduct receipt from members. Such receipts will not include any remuneration for rendering any specific services to the members.

Step 3 Step 1 minus Step 2 is the deficiency which is allowed to be set off against taxable income of such association.

The expression expenditure shall include depreciation provided for in the books of account. The circumstances that such association is not normally entitled to claim depreciation u/s 32 is of no effect. [CIT vs. Indian Jute Mills Association (1982) 134 ITR 68 (Cal)]

9.10 ALTERNATE MINIMUM TAX

Where the regular Income Tax payable for a Previous Year by a person (other than a company) is less than the Alternate Minimum Tax payable for such Previous Year, the Adjusted Total Income shall be deemed to be the total income of such person and he shall be liable to pay Income-tax on such Total Income at the rate of 18.5% [Section115JC (1)]

To whom Alternate Minimum Tax shall be applicable [Section 115JEE (1)]

The provisions of Alternate Minimum Tax shall apply to a non-corporate assessee who has claimed any deduction under:

(a) Sections 80-IA to 80RRB other than section 80P; or

(b) Section 10AA; or

(c) Section 35AD

To whom Alternate Minimum Tax shall not be applicable [Section 115JEE (2)]

The provisions of Alternate Minimum Tax under Chapter XII-BA *shall not apply to-*

(a) an Individual; or

(b) a Hindu Undivided Family; or

(c) an Association of Persons or a Body of Individuals (whether incorporated or not) or

(d) an Artificial Juridical Person referred to in section 2(31) (vii),

if the Adjusted Total Income of such person does not exceed ₹20,00,000

Section 115JEE(3), Notwithstanding anything containe din sub-section (2) the credit for tax paid under Section 115JC shall be allowed in accordance with the provisions of Section 115JD.

Steps involving calculation of Tax where Alternate Minimum Tax provisions applies:

Step 1: Calculate the regular Income-tax liability of the non-corporate assessee ignoring the provisions of Sections 115JC to 115JF.

Step 2: Calculate Adjusted Total Income of the non-corporate assessee.

Step 3: Calculate Alternate Minimum Tax by applying 19.055 percent (18.5 % + 2% EC + 1% SHEC) or 20.9605 percent (i.e. 18.5% + 10% Surcharge + 2% EC + 1% SHEC) incase Adjusted Total Income exceeds ₹1 crore, on Adjusted Total Income computed under Step 2.

Step 4: Compare tax liability computed under Step 1 and Alternate Minimum Tax computed under Step 3. If amount computed under Step 1 is equal to or more than amount computed under Step 3, then the provisions of Alternate Minimum Tax will not apply.

Step 5: If amount computed under Step 1 is less than amount computed under Step 3, then amount computed under Step 3 will be deemed as tax liability of the non-corporate assessee for such Previous Years. In this case, the excess amount computed under Step 3 over the amount computed under Step 1 will be available as credit and can be carried forward and set off against regulars tax liability of the non-corporate assessee of the next year or subsequent years.

Report from an accountant [Section 115JC (3)]: Every non-corporate assessee to whom this section applies shall obtain a report, in such form as may prescribed, from an accountant, certifying that the Adjusted Total Income and the Alternate Minimum Tax have been computed in accordance with the provisions of this Chapter and furnish such report on or before the due date of furnishing of return of income under section 139(1).

Tax credit for AMT: Section 115JD provides the credit for tax (tax credit) paid by a non-corporate on account of AMT under Chapter XII-BA shall be allowed to the extent of the excess of *the AMT paid over the regular Income-tax*. This tax credit shall be allowed to be carried forward up to the tenth Assessment Year immediately succeeding the Assessment Year for which such credit becomes allowable. It shall be allowed to be set off for an Assessment Year in which the regular income-tax exceeds the AMT to the *extent of the excess of the regular Income-tax over the AMT.* No interest shall be payable on tax credit allowed under section 115JD.

For the purpose of the given sections:

"**Adjusted Total Income**" means the Total Income or Net Income of the non-corporate assessee as increased by –

(a) Amount claimed as deduction by the non-corporate assessee under sections 80H to 80RRB other than section 80P;

(b) Amount claimed as deduction by the non-corporate assessee under section 10AA.

"**Alternate Minimum Tax**" shall be the amount of tax computed on Adjusted Total Income at a rate of eighteen and one-half per cent.

Application of other provisions of this Act [Section 115JE]: Save as otherwise provided in this Chapter, all other provisions of this Act shall apply to a non-corporate referred to in this Chapter. Hence, all other provisions relating to Advance tax, interest under sections 234A, 234B and 234C penalty, etc. shall apply to such non-corporate also.

Rates of Income-Tax for Assessment Year 2014-15

Normal Rates of Income Tax

I. Rate of Tax applicable to any Resident Senior Citizen (who attains 60 years age or more during any time of the Previous Year but less than 80 years of age)

Net Income Range	Rate of Income Tax	Education Cess	Secondary and Higher Education Cess
Upto ₹ 3,00,000	Nil	Nil	Nil
₹ 3,00,001 to ₹ 5,00,000	@10% on total income minus ₹ 3,00,000	@2% of Income Tax	@1% of Income Tax
₹ 5,00,001 to ₹ 10,00,000	₹ 20,000 + @20% on total income minus ₹ 5,00,000	@2% of Income Tax	@1% of Income Tax
₹ 10,00,000 onwards	₹ 1,20,000 + @30% on total income minus ₹ 10,00,000	@2% of Income Tax	@1% of Income Tax

II. Rate of Tax applicable to any Resident Super Senior Citizen (who attains 80 years age or more during any time of the Previous Year)

Net Income Range	Rate of Income Tax	Education Cess	Secondary and Higher Education Cess
Upto ₹ 5,00,000	Nil	Nil	Nil
₹ 5,00,001 to ₹ 10,00,000	@20% on total income minus ₹ 5,00,000	@ 2% of Income Tax	@ 1% of Income Tax
₹ 10,00,000 onwards	₹ 1,00,000 + @ 30% on total income minus ₹ 10,00,000	@ 2% of Income Tax	@ 1% of Income Tax

III. In the case of any other Individual or Hindu Undivided Family or AOP/BOI (other than a co-operative society) whether incorporated or not, or every Artificial Judicial Person

Net Income Range	Rate of Income Tax	Education Cess	Secondary and Higher Education Cess
Upto ₹ 2,50,000	Nil	Nil	Nil
₹ 2,50,001 to ₹ 5,00,000	@10% on total income minus ₹ 2,00,000	@ 2% of Income Tax	@ 1% of Income Tax
₹ 5,00,001 to ₹ 10,00,000	₹ 25,000 + @ 20% on total income minus ₹ 5,00,000	@ 2% of Income Tax	@ 1% of Income Tax
₹ 10,00,000 onwards	₹ 1,25,000 + @ 30% on total income minus ₹ 10,00,000	@ 2% of Income Tax	@ 1% of Income Tax

Note : The above rate is applicable to any individual who is not a Senior Citizen. No Addl / special benefit is awarded to Women tax payers. Here, the other individual includes Non-resident individual also irrespective of their age.

The amount of tax computed in accordance with the above rates and special rates u/s 111A (relating to STCG on shares through recognised stock exchange) and 112 (relating to LTCG) shall be increased by a surcharge at the rate of 12% of such income tax in case the total income exceeds ₹1 crore.

A resident individual, having total income not exceeding ₹5,00,000, can avail rebate of ₹2,000 or 100% of income tax, whichever is less, u/s 87A.

Other Assessees:

Assessee	**Rate of Tax**	**Surcharge**
For Firms (including Limited Liability Partnership)	Total Income × 30% + EC@ 2% + SHEC @ 1%.	Surcharge @ 12% if the total income exceeds ₹1 crore
Domestic Companies	Total Income × 30% + EC@ 2% + SHEC @ 1%.	Surcharge @ 7% if the total income exceeds ₹1 crore and @ 12% if the total income exceeds ₹10 crore
Foreign Companies :		
Royalty received from Indian Government or an Indian concern in pursuance of an agreement made by it with the Indian concern after March 31, 1961, but before April 1, 1976, or fees for rendering technical services in pursuance of an agreement made by it after February 29, 1964 and where such agreement has, in either case been approved by the Central Government	Total Income x 50%+ EC@ 2% + SHEC @ 1%	Surcharge @ 2% if the total income exceeds ₹1 crore and @ 5% if the total income exceeds ₹10 crore
Other Income	Total Income x 40%+ EC@ 2% + SHEC @ 1%	Surcharge @ 2% if the total income exceeds ₹1 crore and @ 5% if the total income exceeds ₹10 crore
For Local Authorities	Total Income × 30% + EC@ 2% + SHEC @ 1%.	Surcharge @ 12% if the total income exceeds ₹1 crore
For Co-operative Societies	For First ₹ 10,000 @ 10% For Next ₹ 10,000 @ 20% For the Balance @ 30% EC @ 2% and SHEC @ 1% are applicable.	Surcharge @ 12% if the total income exceeds ₹1 crore
MAT = Minimum Alternate Tax	18.5% of Book Profit + EC @ 2% + SHEC 1%	Surcharge as applicable if Book Profits exceed ₹1 crore or ₹ 10 crore.
AMT = Alternate Minimum Tax	18.5% of Book Profit + EC @ 2% + SHEC 1%	Surcharge if Adjusted Total Income exceed ₹1 crore.

Marginal Relief: The total amount payable as income tax and surcharge on total income exceeding ₹ 1 crore but not exceeding ₹ 10 crore, shall not exceed the total amount payable as income tax on a total income of ₹ 1 crore, by more than the amount of income that exceeds ₹ 1 crore.

In case of a company having a net income exceeding ₹ 10 crores, the amount payable as income tax and surcharge on total income of ₹ 10 crore by more than amount of income that exceeds ₹ 10 crore.

ILLUSTRATIONS ON ASSESSMENT OF AOP / BOI

Illustration 1. A & B are members of AOP, sharing profit and losses in the ratio of 5 : 3 and they are allowed the following payments:

	A ₹	B ₹
(i) Salary	40,000	60,000
(ii) Interest on capital or loan	20,000	10,000

You are required to compute taxable business profits of AOP and share of each member for the Previous Year 2015-2016 in the following cases:

(a) AOP has earned profit of ₹ 3,00,000 after making the above payments;

(b) AOP has earned profit of ₹ 3,00,000 before making the above payments;

(c) AOP has suffered loss of ₹ 3,00,000 after making the above payments; and

(d) AOP has suffered loss of ₹ 3,00,000 before making the above payments.

Solution:

Computation of income of AOP for the A.Y. 2016-2017 :

Particulars	Case (a) ₹	Case(b) ₹	Case (c) ₹	Case (d) ₹
Profit/ loss	(+) 3,00,000	(+) 3,00,000	(-) 3,00,000	(-) 3,00,000
Add: Inadmissible payments [Sec. 40 (ba)]:				
(i) Salary to members (40,000+60,000)	(+) 1,00,000	—	(+) 1,00,000	—
(ii) Interest on capital/loan to members: (20,000 + 10,000)	(+) 30,000	—	(+) 30,000	—
Profit/Loss as per Income Tax Law	(+) 4,30,000	(+) 3,00,000	(-) 1,70,000	(-) 3,00,000

Computation of member's share in the income/loss of the AOP

Particulars	Case (a)		Case (b)		Case (c)		Case (d)	
	A ₹	B ₹	A ₹	B ₹	A ₹	B ₹	A ₹	B ₹
Salary	40,000	60,000	40,000	60,000	40,000	60,000	40,000	60,000
Interest	20,000	10,000	20,000	10,000	20,000	10,000	20,000	10,000
Divisible profit:								
(a) 4,30,000–1,30,000	1,87,500	1,12,500	X	X	X	X	X	X
(b) 3,00,000–1,30,000	X	X	1,06,250	63,750	X	X	X	X
(c) (–) 1,70,000 +(–)1,30,000	X	X	X	X				
=(-)3,00,000	X		X		(1,87,500)	(1,12,500)	X	X
(d) (-) 3,00,000 +		X		X				
(-) 1,30,000= (-) 4,30,000					X	X	(2,68,750)	(1,61,250)
Share of profit/loss	2,47,500	1,82,500	1,66,250	1,33,750	(1,27,500)	(42,500)	(2,08,750)	(91,250)

(i) Where assessed business income is a profit: Beneficial payments (i.e. salary, bonus, commission and interest) made to partners should be deducted from assessed profit to arrive at divisible profit, which is to be apportioned among members.

(ii) Where assessed business income is a loss: Beneficial payments made to partners should be added to assess loss to arrive at the divisible loss which is to be apportioned among members.

Illustration 2. Anand and Aniket are equal members in AA & Associates. The Profit and Loss Account of the AOP for the year ended 31st March 2016 is as follows:

Particulars	₹	Particulars	₹
Selling and administrative Expenses	8,00,000	Gross Profit	20,00,000
Interest to Anand @ 15%	60,000	Income from House Property	3,60,000
Remuneration:			
Anand	1,50,000		
Aniket	1,50,000		
Net Profit:			
Anand	6,00,000		
Aniket	6,00,000		
	23,60,000		**23,60,000**

Other information :

1. Selling and administrative expenses include ₹ 60,000 paid to a consultant in cash.
2. The other income/investment details of the members are given as below:

Members	Income	Source of income	Investments
Anand	3,90,000	Interest on fixed deposit from bank	Purchase of NSC VIII ₹ 30,000
Aniket	5,00,000	Interest on Govt. securities	Contribution to PPF ₹ 50,000

Compute the tax liability of the AOP and it members.

Solution:

Computation of total income of AOP: AY 2016-2017

Particulars	₹
Net Profit	12,00,000
Add: Inadmissible payments.	
1. Fees paid to consultants in cash Sec. 40A (3)	60,000
2. Interest paid to members [Sec. 40(ba)]	60,000
3. Remuneration paid to members Sec. 40(ba)	3,00,000
	16,20,000
Less: Income from House Property	3,60,000
Business Profits	**12,60,000**
Add: Income from House Property	3,60,000
Total Income	**16,20,000**
Tax Liability of AOP on Total Income	
Tax on slabs rates	3,11,000
Add:	
Education cess 2%	6,220
SHEC @ 1%	3,100
Tax Payable	**3,20,330**

Allocation of income amongst the members:

Particulars	Anand ₹	Aniket ₹	Total ₹
Interest	60,000	—	60,000
Remuneration	1,50,000	1,50,000	3,00,000
Share of divisible profit (12,60,000-60,000-3,00,000)	4,50,000	4,50,000	9,00,000
Share of profit	6,60,000	6,00,000	12,60,000
Share of income from House Property	1,80,000	1,80,000	3,60,000
	8,40,000	7,80,000	16,20,000

Computation of total income of members:

Particulars	Anand ₹	Aniket ₹
Share income from AOP	8,40,000	7,80,000
Income from Other Sources:		
Interest on bank deposits	3,90,000	—
Interest on Government securities	—	5,00,000
Gross Total Income	12,30,000	12,80,000
Less: Deduction under Sec. 80C	30,000	50,000
Total Income	12,00,000	12,30,000
Tax liability of members : Tax on slab rates	1,85,000	1,94,000
Add: Education cess @ 2% on income tax	3,700	3,880
Add : SHEC @ 1%	1,850	1,940
	1,90,550	1,99,820
Less: Rebate on share of profit at the average: (See Note below)	1,33,385	1,26,715
Tax Payable	57,165	73,105
Tax Payable rounded off to the nearest multiple of ₹ 10 (See. 288B)	57,170	73,110
Note: Anand: 1,90,550/12,00,000x 8,40,000 Aniket : 1,99,820/12,30,000× 7,80,000		

Note: Assumed that the provisions of Alternate Minimum Tax are not applicable in the above case.

Illustration 3. A, B and C Ltd. are three members of an AOP, sharing profit and losses in the ratio 2:2:1. The AOP discloses its income for the PY 2015-2016 as below:

Particulars	₹
(i) Long-term Capital Gains	4,00,000
(ii) Business Profits	6,00,000

Determine tax liability of AOP in the following cases:

(i) C Ltd. is an Indian company

(ii) C Ltd. is a foreign company

Solution: Allocation of income of AOP among partners

Particulars of income	A ₹	B ₹	C Ltd ₹
Long-term Capital Gains	1,60,000	1,60,000	80,000
Business Profits	2,40,000	2,40,000	1,20,000
Share income of the members	4,00,000	4,00,000	2,00,000

Tax liability of AOP

Particulars	Case – I C Ltd. an Indian company ₹	Case – II C Ltd. as foreign company ₹
Tax on the share of C Ltd.		
Case I : 1,20,000 x 30.90%	37,080	—
Case II: 1,20,000 x 41.20%	—	49,440
Tax on balance income at AOP:		
(i) Long-term Capital Gain		
4,00,000 x 20.60%	82,400	82,400
(ii) Business Profits		
4,80,000 x 30.90%	1,48,320	1,48,320
Total Tax Payable	2,67,800	2,80,160
Total Tax (Rounded off u/s 288B)	2,67,800	2,80,160

Note : Assumed that the provisions of AMT are not applicable in the above case.

Illustration 4. R, S and T Ltd. (a widely held domestic company) are members in an AOP for the Previous Year 2015-2016. They share profit and losses in the ratio 30%, 40% and 30%. Taxable business income of AOP is determined at ₹ 8,00,000. Personal incomes of the partners are given below:

	(₹)
R - House Property	90,000
S – Short-term Capital Gain	1,00,000

R deposits ₹ 20,000 in CTDS-15-year account in Post Office in February 2016. S purchases NSC VIII-Issue for ₹ 25,000 in December 2015.

Determine the tax liability of the AOP and its partners

Solution : (a) Computation of tax liability of AOP for the Previous Year 2015-2016. Allocation of AOP income among members:

Particulars	R ₹	S ₹	T Ltd. ₹
Business Profit	2,40,000	320000	240000

Tax liability of AOP: 8,00,000 × 30.90% = 2,47,200

(b) Tax liability of members:

Particulars	R ₹	S ₹	T Ltd. ₹
Share income from AOP	2,40,000	320000	240000
AOP charged at maximum marginal rate	Exempt	Exempt	Exempt
Personal income of members after deduction under Chapter VIA	70,000	75,000	Nil
Personal income below taxable limit	Exempt	Exempt	X

Note : Assumed that AMT is not applicable in the above case.

Illustration 5. GMK are partners in a firm assessed as an association of persons. They share profit and losses in the ratio of 4:3:3. The abridged profit and loss for the Previous Year 2015-2016 is as follows:

Particulars	₹	Particulars	₹
Business expenses	5,00,000	Gross Profits	6,85,000
Salaries to partners		Short-term Capital Gain	2,80,000
G	60,000	Interest on drawings	
M	40,000	G	5,000
K	50,000	M	20,000
Bonus to partners:		K	10,000
G	30,000		
M	20,000		
Commission to K	40,000		
Interest to partners:			
G	20,000		
M	15,000		
K	25,000		
Net Profit			
G	80,000		
M	60,000		
K	60,000		
	10,00,000		**10,00,000**

Business expenses include donation to Nalanda University ₹ 50,000.

Compute the taxable income of AOP, its tax liability and tax liability of its members in the following cases:

Personal income of members	Case-I ₹	Case-II ₹
G: Interest on bank deposits	2,40,000	1,00,000
M: Interest on Government securities	2,65,000	1,20,100
K: Income from House Property	2,50,000	1,10,000
LIP paid by every member on a policy of ₹ 1,00,000.	20,000	20,000

Solution :

Computation of Taxable Business Profits

Particulars	₹
Net Profit as per Profit & Loss A/c	2,00,000
Add: (i) Donation to Nalanda University	50,000
(ii) Salaries to partners [Sec. 40(ba)] (60,000 + 40,000 + 50,000)	1,50,000
(iii) Bonus to partners (30,000 + 20,000)	50,000
(iv) Interest on capital (Net of Interest on Drawings)	
G (20,000 – 5,000)	15,000
K (25,000 – 10,000)	15,000
(v) Commission to K	40,000
	5,20,000
	2,80,000
Less: Short-term Capital Gain	
Taxable Business Profits	**2,40,000**
Computation of Total Income	
Add: (i) Business Profits	2,40,000
(ii) Short-term Capital Gain	2,80,000
Gross Total Income	**5,20,000**
Less: Deduction for charitable donation (Sec. 80G)	
(a) Actual donation ₹ 50,000 or,	
(b) 10% of gross total income: $\frac{10}{100} \times 5{,}20{,}000 = 52{,}000$	
whichever is less, is qualifying amount. i.e. ₹ 50,000.	
Amount of deduction 50% of ₹ 50,000, qualifying amount	25,000
Total Income	**4,95,000**

Tax liability of AOP :

Particulars	Case I	Case II
(a) Tax on Total Income at slab rates including Education Cess and SHEC	25,235	—
(b) Tax on Total Income at maximum marginal rates including surcharge plus education cess plus SHEC	—	1,52,955
Tax Payable	25,235	1,52,955
Tax Payable rounded off (u/s 288B)	25,240	1,52,960

Tax liability of members:

Share of income from AOP:	G (₹)	M (₹)	K (₹)	Total (₹)
(i) Salary	60,000	40,000	50,000	1,50,000
(ii) Bonus	30,000	20,000	—	50,000
(iii) Commission	—	—	40,000	40,000
(iv) Interest	15,000	—	15,000	30,000
	1,05,000	60,000	1,05,000	2,70,000
(v) Divisible loss : (2,40,000-25,000)-270,000 = (-) 55,000	(-) 22,000	(-) 16,500	(-) 16,500	(-) 55,000
Share of Business Profit	83,000	43,500	88,500	2,15,000
Share of Short-term Capital Gain	1,12,000	84,000	84,000	2,80,000
Share of income from AOP	**1,95,000**	**1,27,500**	**1,72,500**	**4,95,000**

Total Income and Tax Liability of members :

Case:(a) where AOP is taxed at slab rates:

Particulars	G	M	K
Income from House Property	—	—	2,50,000
Income from Other Sources	2,40,000	2,65,000	—
Share income from AOP	1,95,000	1,27,500	1,72,500
Gross Total Income	**4,35,000**	**3,92,500**	**4,22,500**
Less: Deduction under Sec. 80C: LIP restricted to 20% of policy [Assumed the policy is issued before 1.4.2012]	20,000	20,000	20,000
Total Income	**4,15,000**	**3,72,500**	**4,02,500**
Gross income tax at slab rate	16,500	12,250	15,250
Less: Rebate u/s 87A	2,000	2,000	2,000
	14,500	10,250	13,250
Add: Surcharge	Nil	Nil	Nil
Add: Education Cess @ 2%	290	205	265
Add : SHEC @ 1%	145	103	133
	14,935	10,558	13,648
Less: Rebate on share of profit from firm at the average rate	7,018	3,619	5,849
Tax Payable	7,917	6,939	7,799
Tax Payable rounded off (u/s 288B)	**7,920**	**6,940**	**7,800**
Note 1: 14,935 ÷ 4,15,000 × 1,95,000 = 7,018 Note 2: 10,558 ÷ 3,72,500 × 1,27,500 = 3,619 Note 3: 13,648 ÷ 4,02,500 × 1,72,500 = 5,849			

Case (b) where AOP is taxed at maximum marginal rate:

Particulars	G	M	K
1. Share of profit from AOP; Since the AOP was assessed at the maximum marginal rate, share of income from AOP is exempt (Sec. 86)	—	—	—
2. Personal income:			
Income from House Property	–	–	1,10,000
Income from Other Sources	1,00,000	1,20,100	–
Less: Deduction u/s 80C	(-) 20,000	(-) 20,000	(-) 20,000
Total Income	80,000	1,00,100	90,000
Tax Payable	Nil	Nil	Nil

Note : Provisions of AMT are not applicable in the above case.

Illustration 6. T and Q are individuals, who constitute an Association of Persons, sharing profit and losses in the ratio of 2:1. For the accounting year ended 31st March 2016, the Profit and Loss Account of the business was as under:

Particulars	₹ in '000	Particulars	₹ in '000
Cost of goods sold	6,250.00	Sales	9,900.00
Remuneration to:		Dividend from companies	25.00
T	130.00		
Q	170.00	Long-term Capital Gains	1,640.00
Employees	256.00		
Interest to :			
T	48.30		
Q	35.70		
Other expenses	111.70		
Sales-tax penalty due	39.00		
Net Profit	4,524.30		
	11,565.00		11,565.00

Additional information furnished:

(i) Other expenses included:

(a) entertainment expenses of ₹ 35,000;

(b) wristwatches costing ₹ 2,500 each were given to 12 dealers, who had exceeded the sales quota prescribed under a sales promotion scheme;

(c) employer's contribution of ₹ 6,000 to the Provident Fund was paid on 14th January 2016.

(d) ₹ 30,000 was paid in cash to an advertising agency for publicity.

(ii) Outstanding sales tax penalty was paid on 15th April 2016. The penalty was imposed by the sales tax officer for non-filing of returns and statements by the due dates.

(iii) T and Q had, for this year, income from other sources of ₹ 3,50,000 and ₹ 2,60,000, respectively.

Required to :

(i) Compute the total income of the AOP for the Previous Year 2015-2016.

(ii) Ascertain the tax liability of the Association for that year; and

(iii) Ascertain the tax liability for that year of the individual members.

[Ignore the application of Alternate Minimum Tax]

Solution : (i) Computation of total income of the AOP for PY 2015-2016

Particulars	₹	₹
Profit and Gains of Business (see Working Note below)		33,12,300
Long Term Capital Gain		16,40,000
Income from Other Sources [dividend is exempt u/s 10(34), assuming it is from domestic companies]		NIL
Total Income		**49,52,300**
Working Note:		
Computation of profits and gains of business:		
Net profit as per Profit and Loss Account		45,24,300
Add: Inadmissible payments:		
Interest to members T & Q (₹ 48,300 + ₹ 35,700)	84,000	
Advertising [disallowance u/s 40A(3)	30,000	
Remuneration to members T & Q (₹ 1,30,000 + ₹ 1,70,000)	3,00,000	
Sales tax penalty due (See Note 3 below)	39,000	4,53,000
		49,77,300
Less : Income not taxable under this head		
Dividend from companies	25,000	
Long term Capital Gain	16,40,000	16,65,000
Profits and Gains of Business		**33,12,300**

(ii) Computation of tax liability of the AOP for PY 2015-2016

Particulars	₹	₹
Long-term Capital Gain (₹ 16,40,000 × 20%)		3,28,000
Other Income (₹ 33,12,300 × 30%)		9,93,690
Tax on Total Income		13,21,690
Add : Education cess @ 2%		26,434
Add : SHEC @ 1%		13,217
Total Tax due		**13,61,341**
Total Tax Rounded off (u/s 288B)		**13,61,340**

Note :

1. Since one of the members has individual income more than the basic exemption limit, the AOP will be assessed at the maximum marginal rate.
2. Since the employer's contribution to PF has been paid during the Previous Year 2015-2016 itself, it is allowable as deduction.
3. Penalty imposed for delay in filing sales tax return is not deductible since it is on account of infraction of the law requiring filing of the return within the specified period.
4. Gift paid to dealers are solely for business purpose and hence, fully deductible item.

(iii) Computation of Tax Liability of members T & Q for the PY 2015-2016

Particulars	₹	Particulars	₹
Tax on ₹ 3,50,000	10,000	Tax on ₹ 2,60,000	1,000
Less: Rebate u/s 87A	2,000	Less: Rebate u/s 87A	1,000
	8,000		Nil
Add : Surcharge	Nil	Add : Surcharge	Nil
	8,000		Nil
Add : Education cess @ 2%	160	Add : Education cess @ 2%	Nil
Add : SHEC @ 1%	80	Add : SHEC @ 1%	Nil
Net Tax Payable	**8,240**	**Net Tax Payable**	**Nil**

ILLUSTRATIONS ON ASSESSMENT OF CHARITABLE TRUSTS

Illustration 7. Shri Dubbawala Charitable Trust (Regd.) submits the particulars of its income / outgoing for the Previous Year 2015-2016 as below :

		₹
(i)	Income from property held under trust for charitable purposes:	10,00,000
	(₹ 2,20,000 out of ₹ 10,00,000 is received in PY 2016-2017)	
(ii)	Voluntary contributions (out of which ₹ 50,000 will form part of the corpus)	2,00,000

The trust spends ₹ 1,77,500 during the Previous Year 2015-2016 for charitable purposes. In respect of ₹ 2,20,000, it has exercised its option to spend it within the permissible time-limit in the year of receipt or in the year, immediately following the year of receipt.

The trust spends ₹ 2,00,000 during the Previous Year 2014-2015 and ₹ 1,00,000 during the Previous Year 2016-2017. Compute and discuss the chargeabiliry of the income of the trust.

Solution : (a) Computation of taxable income and tax liability of the charitable trust for the PY 2015-2016 / AY 2016-2017

Particulars			₹
(i) Income from property held under trust for charitable purposes			10,00,000
(ii) Voluntary contributions (₹ 2,00,000 - ₹ 50,000)			1,50,000
			11,50,000
Less: 15% set apart for future application			1,72,500
Balance			9,77,500
Less: Amount spent during the Previous Year for charitable purposes			1,77,500
Balance			8,00,000
Less: Income not received during the Previous Year 2015-2016			2,20,000
Taxable Income			5,80,000
Tax payable:	Rate of tax		
2,50,000	Nil		
2,50,000	10%		25,000
80,000	20%		16,000
			41,000
Add: Education Cess @ 2%			820
Add: SHEC @ 1%			410
Tax Payable			**42,230**
(b) Previous Year 2016-2017 /AY 2017-2018			
Income received during the Previous Year 2016-2017		2,20,000	
Amount spent for charitable purposes during 2015-2016		1,00,000	
Taxable Income		**1,20,000**	

Illustration 8. Shri Mungeri Ram Temple Trust (Regd.) derived ₹ 6,00,000 income from the property held under charitable trust during the Previous Year 2015-2016. About 40% of the income has been received by the end of the financial year. The trust could spend ₹ 60,000 for charitable purposes during the year 2015-2016 and 40% receipts, received by the year end in 2015-2016, are being planned to be applied for charitable purposes during the Previous Year 2016-2017. Compute its income for the said two years if the amount planned to be spent during Previous Year 2016-2017 for charitable purposes is ₹ 1,00,000.

Solution : (a) Computation of Taxable Income of Charitable Trust: PY 2015-2016/AY 2016-2017

Particulars		₹
Income from property held under Trust		6,00,000
Less: 15% set apart for future application for charitable purposes		90,000
Balance		5,10,000
Less : Income applied for charitable purposes during the year 2015-2016		60,000
Balance		4,50,000
Less: Income realised by the close of the Previous Year—40% of ₹ 6,00,000		2,40,000
Taxable Income		**2,10,000**
(b) Previous Year : 2016-2017/**A.Y.** 2017-2018		
Amount set apart in 2015-2016 to be applied for charitable purposes in 2016-2017	= 2,40,000	
Less: Amount applied for charitable purposes	= 1,00,000	
Taxable Income	**1,40,000**	

Illustration 9. Devdas Charitable Trust submits the particulars of its receipts and outgoing during the Previous Year 2015-2016 as below :

(i)	Income from property held under trust for charitable purposes	₹ 20,00,000
(ii)	Voluntary contribution (out of which ₹ 5,00,000 will form part of the corpus)	₹ 15,00,000
(iii)	Donations paid to blind charitable school	₹ 6,00,000
(iv)	Scholarship paid to poor students	₹ 4,00,000
(v)	Amount spent on holding free eye camps in urban slums	₹ 3,00,000
(vi)	Amount set apart for setting up an old age home by March 2018	₹ 10,00,000

Compute the total income of the trust for the Previous Years 2015-2016 and 2018-2019 if it spends ₹ 3,00,000 during the Previous Year 2017-2018 and ₹ 5,00,000 during the Previous Year 2018-2019 in setting up the old age home.

Solution : (a) Computation of the Taxable Income of the trust for Previous Year 2015-2016/AY 2016-2017.

Particulars		₹
(i) Income from property held under charitable trust		20,00,000
(ii) Income from voluntary contributions (₹ 15,00,000 - ₹ 5,00,000)		10,00,000
Total		**30,00,000**
Less : 15% set apart for future application		4,50,000
Balance		**25,50,000**
Less: Income applied for charitable purposes:		
(i) Donations to blind charitable school	6,00,000	
(ii) Scholarship to poor students	4,00,000	
(iii) Free eye camps in urban slums	3,00,000	
Total	**13,00,000**	
Amount set apart for old age home	10,00,000	(23,00,000)
Taxable Income		**2,50,000**
(b) Previous Year 2018-2019 /AY 2019-2020:		
Amount set apart for old age home	10,00,000	
Less : 1. Amount spent during 2017-2018	(3,00,000)	
2. Amount spent during 2018-2019	(5,00,000)	
Taxable Income	**2,00,000**	

Illustration 10. CD Charitable Trust furnishes the following particulars, for the year 2015-2016:

(₹)

(i)	Sale price of capital assets	15,30,000
(ii)	Expenses incurred in connection with sale of the asset	30,000
(iii)	Cost of the asset sold (purchased in 2014-2015)	5,00,000
(iv)	Compute Capital Gain in the following cases:	
	(a) Cost of the new asset to be acquired	15,00,000
	(b) Cost of the new asset to be acquired	8,00,000
	(c) Cost of the new asset to be acquired	4,00,000

Solution: Computation of Capital Gain: PY 2015-2016/AY 2016-2017

Particulars	**Case-I** ₹	**Case-II** ₹	**Case-III** ₹
Sale price	15,30,000	15,30,000	15,30,000
Less: (i) Selling expenses	(-) 30,000	(-) 30,000	(-) 30,000
(ii) Cost of the asset	(-) 5,00,000	(-) 5,00,000	(-) 5,00,000
Short-term Capital Gain	10,00,000	10,00,000	10,00,000
Less: Exemption in respect of Capital Gain	10,00,000	3,00,000	Nil
Taxable Capital Gain	Nil	7,00,000	10,00,000

Note : 1. Cost of new asset - cost of asset sold: 8,00,000 - 5,00,000 = 3,00,000

2. Cost of new asset - cost of asset sold: 4,00,000 - 5,00,000 = Nil

Illustration 11. Where the private trust is charged at the maximum marginal rate u/s 164(1), whether basic exemption is to be allowed?

Solution: No. The tax should be levied at the maximum marginal rate as laid down in the Act itself, without allowing the basic exemption as laid down in the Finance Act. [Surendranath Gangopadhyay Trust vs. CIT (1983) 142 ITR 149 (Cal.)].

Illustration 12. Whether, while computing the income of a private trust, deduction under section 80C is allowable?

Solution: Yes. Section 164(1) comes into play only after the income has been computed in accordance with the provisions of the Act. Where the trustees of a discretionary trust are assessed on behalf of a beneficiary, who is an individual, deduction under section 80C or rebate under section 88 is allowable [CIT vs. Shri Krishna Bandar Trust (1993) 201 ITR 989 (Cal.) and Amy F. Cama vs. CIT (1999) 237 ITR 82 (Bom.)]

It is available against beneficiary's share of income from the trust, even where assessment is made in the hands of the trustee [CIT vs. Saurin S. Zaveri (2002) 257 ITR 160 (Mad.) and CIT vs. Venu Suresh Sanjay Trust (1996) 221 ITR 649 (Mad.)]. The Supreme Court refused special leave to revenue on the question of deduction under section 80C on income assessable in the hands of the trust [CIT vs. Pradeep J. Kinariwala (1999) 237 ITR (St.) 129].

Illustration 13. The Assessing Officer made an assessment for A.Y. 2015-16, in the name of the trust. But, during the assessment proceedings of A.Y. 2016-17 the Assessing Officer found that the assessment in the hands of the beneficiaries would be more beneficial to the revenue than the assessment in the hands of the trust. Accordingly, he made the assessment for A.Y. 2016-17 in the hands of the beneficiaries. Was the Assessing Officer justified in doing so?

Solution: No. In Board's Circular No.157 dated 26.12.1974, it is clarified that at the initial assessment, the Assessing Officer should opt to assess either the trust or the beneficiaries, and that, once the option is exercised, the same income cannot be taxed in the other persons' hands (the beneficiary or the trustee, as the case may be).

Illustration 14. Should the maximum rate of tax prescribed for discretionary trust, where such discretion does not extend to the entire trust's income, be applicable for entire income?

Solution: No. In a similar situation relating to a charitable institution where there was violation in respect of some investments not permitted under section 13(1)(d), it was found in Director of Income Tax (Exemptions) vs. Shaik Mohd. Jan Foundation Trust ITA Nos. 267 & 272 (Bom.), where it was held that maximum rate should be limited only to that part of the income, where there is a violation, attracting such maximum rate and not to the entire income. The decision was rendered in the context of the language of the proviso to section 164(2), which refers to the forfeiture of exemption for breach of section 13(1)(d). It was pointed out that there is a factual difference between eligibility for exemption and withdrawal/forfeiture of exemption. Once there is eligibility, the withdrawal or forfeiture could only be limited to that part of the income which attracts maximum rate. Since the decision was rendered in the context of section 164(2) applicable to discretionary trust, the principle should have application for all private trusts.

Illustration 15. Where a trust is created, for carrying on the business hitherto carried on by joint family, after its partition, could such trust be treated as one liable to be assessed as AOP constituted by the beneficiaries?

Solution: Such a situation arose in CIT vs. Ashok Match Industries B-Unit (2000) 244 ITR 1047 (Mad.). The argument on behalf of the assessee was that, since the consent of members is necessary for treatment as AOP and since the business was carried on by the trustees and not by the beneficiaries, who incidentally were minors, there could be no AOP. The High Court found the consent of the guardian of the minors was good enough to create an AOP. The fact that the titular owner of the business was a trust was not a bar to the treatment of the beneficiaries collectively as AOP. Such a decision was rendered after review of the case law on the subject with reference to the principles laid down by the Supreme Court in N.V. Shanmugham and Co. vs. CIT(1971) 81 ITR 310 (SC). In the result, the concept of trust could not avoid collective assessment of AOP.

In CIT vs. Shabandari Family Trust (2000) 246 ITR 57 (Ker.,) a similar issue was remitted back to the Tribunal by the High Court for consideration of the activities of the trust, mode of income derived and beneficiaries of the trust.

Illustration 16. Can a trust be created by the legal guardian of the minor in respect of minor's property on behalf of the minor?

Solution: In T.A.V. Trust vs. CIT (1999) 236 ITR 788 (SC), it was found that as section 7 of the Indian Trusts Act, 1882 provides that a trust can be created only by persons competent to contract and that in the case of a minor, it can be so done only with the permission of the civil court of original jurisdiction, otherwise, such trust is invalid.

Illustration 17. Where there is a sole beneficiary with the trustee having only the power to determine the time when benefit can be availed by the beneficiary, will such trust attract maximum rate of tax under section 164?

Solution: Where the beneficiary is one and is known, it cannot be said that it is a discretionary trust within the meaning of section 164. It is not a case where maximum rate of tax would have application. It was so held in CIT vs. Saroja Raman (1999) 238 ITR 34 (Mad.), Where the High Court pointed out that the object of the provision is directed against trusts, where the benefits could be manipulated and not to deny the normal rate of tax in such cases where there is no choice as between different beneficiaries is left to the trustee.

Illustration 18. Where a trust is created by Will by which the executor has to act as a trustee, when does the executor cease to be an executor and becomes a trustee?

Solution: This issue was decided in K.R. Patel (Deceased) vs. CIT (1999) 239 ITR 738 (SC) where the Will was probated and an application for registration of public trust was also made by the executors. It is neither the date of probate of grant of the Will or the date of application for registration of public trust which is relevant. Till all payments required to be made under the Will are made, the executor continues to be an executor and the income of the estate is required to be assessed only in his hands in that capacity.

Illustration 19. Where there is more than one trustee, is it permissible to adopt the status of the trust as AOP?

Solution: Since the income of a trust has to be allocated to the beneficiaries the status of the beneficiary will be that of the trust in respect of income of each beneficiary.

Illustration 20. Where the sole beneficiary is another trust, can the first trust be treated as a representative assessee so as to be entitled to exemption for which beneficiary is eligible?

Solution: Yes. It has been held that there is no reason why the role of representative assessee should be different merely because the beneficiary is another trust [Honesty Engineers and Contractors Trust vs. CIT (2003) 262 ITR 266 (Mad.)].

Illustration 21. Where a trust has both business income and has also other incomes and section 164 is applicable, should maximum rate be applicable for the total income?

Solution: No. Only the business income will attract the maximum marginal rate [CIT vs. T.A.V. Trust (2003) 264 ITR 52 (Ker.)].

Illustration 22. A trustee made distribution of income to the beneficiaries, in a manner contrary to the terms of the deed. Does it attract maximum marginal rate?

Solution: No. Where the shares are specified, a distribution contrary to specifications does not make it a discretionary trust, so that maximum rate is not applicable [CIT vs. Smt. Gurmail Kaur Trust (2004) 268 ITR 124 (P&H)] .

Illustration 23. Is a trustee, as a representative assessee, where minor is a beneficiary, liable for penalty?

Solution: The fact that beneficiary is a minor does not offer immunity, so that the issue has to be decided on merits. In a case, where under-statement of income in the return filed by legal representative was alleged, the matter was remanded by the High Court for a finding in this regard in a departmental appeal [CIT vs. Master Sunil R. Kalro (2007) 292 ITR 86 (Kar)]. The reasoning appears to be that the representative, responsible for the default, cannot be excused.

Illustration 24. Where a trust attracted maximum marginal rate, can rectification be made to the trust deed, so as to specify shares and avoid such higher rate?

Solution: A trust deed can be rectified in the manner permissible under the terms of trust deed and trust law, but it can have effect only from the date on which rectification is made [Ranga Rao Lottery Agencies Vs. CIT (2006) 287 ITR 542 (Mad)].

Illustration 25. Where the income of a beneficiary has been assessed in the hands of the trust, is such income includible in the direct assessment of the beneficiary for rate purposes?

Solution: No. Assessing Officer's reliance on section 86 which permits inclusion of share income from Association of Persons, where it has no assessable income, was found to be unjustified, since section 86 can have no application where such income has been assessed in the hands of a representative assessee [CIT vs. P.N. Bajaj (2003) 262 ITR 593 (Mad)].

Illustration 26. Where grandparents had created 45 trusts for 12 grandchildren at the same time, what is tax treatment?

Solution: Creation of multiple trusts at the same time for similar benefit was held to be not genuine. The entire income was held to be assessable in the hands of an Association of Persons. The better solution was to assess the settlors on the finding that the trusts were not genuine.

ILLUSTRATIONS ON ASSESSMENT OF COOPERATIVE SOCIETIES

Illustration 27. Dinesh Pally Cooperative Society Ltd. furnishes the following particulars of its income for the Previous Year ended on 31st March 2016:

(i)	Interest on Government securities	40,000
(ii)	Profits from banking business	3,50,000
(iii)	Income from purchase and sale of agricultural implement and seeds to its members	2,50,000
(iv)	Income from marketing of agricultural produce of its members	4,00,000
(v)	Profits and gains of business	2,20,000
(vi)	Income from cottage industry	3,50,000
(vii)	Interest and dividends (gross) from other cooperative societies	30,000

Compute Total Income of the society and calculate the Tax Payable by it for the Assessment Year 2016-2017.

Solution :

Dinesh Pally Cooperative Society Ltd.

Computation of income of the for the Previous Year 2015-2016 relating to the Assessment Year 2016-2017 :

Particulars	₹	₹
1. Profits and Gains of Business or Profession:		
(a) Banking business	3,50,000	
(b) Income from purchase and sale of agricultural implements and seeds to its members	2,50,000	
(c) Income from marketing of agricultural produce of its members	4,00,000	
(d) Profits and gains of business	2,20,000	
(e) Income from cottage industry	3,50,000	15,70,000
2. Income from Other Sources:		
(a) Interest on Government securities	40,000	
(b) Interest and dividends from other cooperatives	30,000	70,000
Gross Total Income		**16,40,000**
Less: Deduction allowable from gross total income under Sec. 8OP		
1. Banking business [Assumed it is a Rural Development Bank]	3,50,000	
2. Income from purchase and sale of agricultural implement and seeds to its members	2,50,000	
3. Income from marketing of agricultural produce of its members	4,00,000	
4. Income from cottage industry	3,50,000	
5. Interest on Government securities(not eligible for deduction)	Nil	
6. Interest and dividends from other co-operative societies	30,000	13,80,000
Total Income		**2,60,000**

Computation of Tax Liability :

Particulars	Rate	₹
On first ₹ 10,000	10%	1,000
On next ₹ 10,000	20%	2,000
On balance ₹ 2,40,000	30%	72,000
Income Tax Payable		75,000
Add: Education cess @ 2%		1,500
Add: SHEC @ 1%		750
Tax Payable		**77,250**

Note: It is assumed that the provisions of Alternate Minimum Tax are not applicable.

Illustration 28. A co-operative society, engaged in the business of banking, seeks your opinion by the matter of eligibility of deduction under Sec. 8OP on the following items of income earned by it during the year ended 31-3-2016.

(i) Interest on investment in Government securities made out of statutory reserves

(ii) Hire charges of safe deposit lockers.

Solution :

From the Assessment Year 2008-2009 and onward, no deduction is allowed under Sec. 80P to any cooperative bank. However, a primary agricultural credit society or primary co-operative agricultural and rural development bank is outside the purview of this provision [Sec. 80P(4)].

Illustration 29. A co-operative society was engaged in the business of banking or providing credit facilities to its members. It sold goods on credit to its members. Is the co-operative society entitled to special deduction under Sec. 80P(2)(a)(i) in respect of income derived from such an activity?

Solution :

Society is not entitled to the special deduction under Sec. 80P(2)(a)(i).

ILLUSTRATIONS ON ASSESSMENT OF INDIVIDUAL

Illustration 30. Salil was running a business. He died on 20th December, 2015, leaving behind his wife Sruti and two minor sons - Sampat and Samar. He did not have any will. Sruti is running the business for and on behalf of herself and the minor children. Salil owned two house properties. Discuss how the rental income and the business income of the financial year 31st March, 2016 will be assessed and in whose hands.

Solution:

Section 159 provides that if an assessee dies during the Previous Year, the income of the period beginning from the commencement of Previous Year and ending with the date of death is taxable in the hands of the legal representative as if the assessee had not died. Therefore, the business profits and the rental income accruing from 1st April, 2015 to 20th December, 2015 will be assessable in the hands of the legal representatives. Sruti represents the estate and hence is liable to be assessed as the legal representative of Salil.

Business profits and rental income arise from 21st December, 2015 to 31st March, 2016: As far as rental income is concerned, it will be assessed as income of Sruti, Sampat and Samar according to their shares.

According to provisions of Hindu Succession Act, when a male Hindu dies intestate, his estate will devolve on the heirs mentioned in the Schedule by succession and not by survivorship. Hence, the widow and minor children became co-owners and Section 26 will apply since the respective shares are definite and ascertainable. The rental income will be divided into three parts. However, income of Sampat and Samar will be clubbed with income of Sruti by virtue of section 64(1A).

As far as business profit is concerned, the Andhra Pradesh High Court in Deccan Wine and General Stores vs. CIT [1977] 106 ITR 111 has held on similar facts that it is to be assessed in the status of Body of Individuals.

Illustration 31 : Ria, Gia and Ira are persons ,aged 30 years, 34 years and 35 years respectively, of Indian origin, though their residential status is non-resident. During the Previous Year relevant for the Assessment Year 2016-17, their income from investment in India is as follows:

Particulars	Ria ₹	Gia ₹	Ira ₹
a. Interest on deposits with public limited companies received on March 31, 2016	35,000	80,000	1,50,000
b. Interest on Government securities received on December 31, 2015	2,25,000	2,20,000	2,70,000
c. Interest on deposits with private limited companies on September 30, 2015	Nil	1,00,000	8,80,000
Tax deducted at source, i.e., @ 20.6 per cent in respect of foreign exchange assets (a) and (b); and @ 30.9 per cent in respect of (c)	53,560	92,700	3,58,440

Determine the amount of tax liability/refund for the Assessment Year 2016-17. Also discuss whether the assessee should opt under section 115-I, i.e., not to be governed by provisions of sections 115C to 115-I.

Solution:

Tax liability if the assessee opts under section 115-I, not to be governed under the provisions of sections 115C to 115-I:

Particulars	Ria ₹	Gia ₹	Ira ₹
Gross Total Income [(a) + (b) + (c)]	2,60,000	4,00,000	13,00,000
Less: Deduction	Nil	Nil	Nil
Net Income	2,60,000	4,00,000	13,00,000
Tax	1,000	15,000	2,15,000
Add: Education Cess	20	300	4,300
Add: Secondary and Higher Secondary Education Cess	10	150	2,150
	1,030	15,450	2,21,450
Less: Tax Deduction at Source	53,560	92,700	3,58,440
Final tax liability/(-)refund	(-)52,530	(-)77,250	(-)1,36,990
Tax liability if provisions of sections 115C to 115-I are applicable:			
Income from foreign exchange assets eligible for provisions of sections 115C to 115-I [i.e., (a) + (b)]	2,60,000	3,00,000	4,20,000
Tax on income from foreign exchange assets [i.e., @ 20.6% in the case of Ria, Gia and Ira] (1)	53,560	61,800	86,520
Other Income [i.e., (c)]	Nil	1,00,000	8,80,000
Less: Deduction	Nil	Nil	Nil
Taxable Income	Nil	1,00,000	8,80,000
Tax	Nil	Nil	1,06,000
Add: Education Cess	Nil	Nil	2,120
Add: Secondary and Higher Secondary Education Cess	Nil	Nil	1,060
Tax on Other Income (2)	Nil	Nil	1,09,180
Tax liability [i.e., (1) + (2)]	53,560	61,800	1,95,700
Less: Tax Deducted at Source	53,560	92,700	3,58,440
Final tax liability/(-)refund	Nil	(-)30,900	(-)1,62,740

Note: in the problem given above, Ria and Gia should opt under section 115-I (i.e., not to be governed by special provisions of sections 115C to 115-I) by furnishing return of income under section 139. Ira should take the benefit of special provisions of sections 115C to 115-I.

Illustration 32 : From the Profit and Loss Account of Ms. Alo of 36 years old for the year ended March 31, 2016, ascertain her Total Income and Tax liability for the Assessment Year 2016-17:

Particulars	₹	Particulars	₹
General Expenses	13,500	Gross Profits	3,17,000
Bad debts	22,000	Commission	8,800
Advance Tax	3,000	Brokerage	37,000
Insurance	800	Sundry receipts	2,500
Printing & Stationery	1,200	Bad debt recovered (earlier allowed as deduction)	11,000
Salary to Staff	27,000		
Salary to Alo	51,000	Interest on debentures (i.e., net amount ₹18,000 + tax deducted at source : ₹ 2,000)	20,000
Interest on Overdraft	4,000		
Interest on loan to Chandra	41,000	Interest on deposit with a company (non – trade) (net interest : ₹ 13,500 + tax deducted at source : ₹ 1,500)	15,000
Interest on capital of Alo	22,000		
Depreciation	48,000		
Advertisement expenditure	7,000		
Contribution to employees' Recognized Provident Fund	7,800		
Net Profit	1,63,000		
	4,11,300		4,11,300

Other Information:

1. The amount of depreciation allowable is ₹ 45,000 as per the Income Tax Rules. It includes depreciation on permanent sing board.
2. Advertisement expenditure includes ₹ 2000, being cost of permanent sing board fixed on office premises.
3. Income of ₹ 2500, accrued during the Previous Year, is not recorded in the Profit and Loss Account.
4. Alo pays ₹ 9000 as premium on own life insurance policy of ₹ 1,00,000.
5. General expenses include:

   (a) ₹ 1,500 given to sister for arranging a party in her birthday party

   (b) ₹ 1,000 being contribution to a political party.
6. Loan was taken from Chandra for payment of arrears of Income – tax.

Solution :

Assessee : Ms. Alo **Previous Year : 2015-2016** **Assessment Year : 2016-2017**

Particulars	₹	₹
Net profit as per Profit & Loss Account		1,63,000
Add: Inadmissible expenses:		
Expenses for arranging personal party	1,500	
Contribution to a political party	1,000	
Advance tax	3,000	
Salary to Alo	51,000	
Interest on capital to Alo	22,000	
Interest on loan taken for payment of Income-tax	41,000	
Capital expenditure on advertisement	2,000	
Depreciation debited to the Profit & Loss A/c	48,000	1,69,500
		3,32,500
Add: Income not recorded in the Profit and Loss Account		2,500
		3,35,000
Less: Income credited to the Profit and Loss Account but not chargeable under the head "Profits and gains of business or profession".		
Interest on debentures	20,000	
Interest on company deposit	15,000	35,000
		3,00,000
Less: Depreciation allowable Income Tax Rules		45,000
Business Income		2,55,000
Computation of Net Income		
Profits and Gains of Business or Profession		2,55,000
Income from Other Sources (interest on debentures and company deposit)		35,000
Gross Total Income		2,90,000
Less: Deductions		
Under section 80C (payment of insurance premium)	9,000	
Deduction under section 80GGC (being contribution to a political party)	1,000	10,000
Net Income		2,80,000
Tax on Net Income		3,000
Less: Rebate u/s 87A		2,000
		1,000
Add: Surcharge		Nil
Tax and Surcharge		1,000
Add: Education cess (2% of tax and Surcharge)		20
Add: Secondary and higher education cess [1% of tax and Surcharge]		10
Tax		1,030
Less: Pre-paid tax (i.e., advance tax + tax deducted at source)		6,500
Tax Refundable (rounded off)		5,470

Note :

Provisions of Alternate Minimum Tax are not applicable.

Illustration 33. The total income of Mina for the assessment year 2016-17 is ₹1,01,30,000. Compute the tax payable by Mina for the assessment year 2016-17.

Solution:

Particulars		₹
Tax on ₹1 crore		
On first ₹2,50,000		Nil
Next ₹2,50,000 — 10%		25,000
Next ₹5,00,000 — 20%		1,00,000
Balance ₹90,00,000 — 30%		27,00,000
		28,25,000
Tax on ₹ 1,30,000 which is above ₹1 crore		39,000
₹ 1,30,000 @ 30%		
Total tax		28,64,000
Additional income above ₹ 1 crore	1,30,000	
Tax payable	39,000	
Balance income	91,000	
Surcharge on ₹28,64,000 @ 12% — ₹3,43,680		
∴ surcharge in this case shall be ₹91,000 or ₹3,43,680 whichever is less due to marginal relief		91,000
Tax including surcharge		29,55,000
Add: Education cess & SHEC @ 3%		88,650
Tax Payable		30,43,650

Alternatively:

Particulars	₹
Tax on ₹1,01,30,000	
On first ₹2,50,000	Nil
Next ₹2,50,000 — 10%	25,000
Next ₹5,00,000 — 20%	1,00,000
Balance ₹91,30,000 — 30%	27,39,000
	28,64,000
Add : Surcharge @ 12%	3,43,680
(a)	32,07,680
Tax on ₹ 1,00,00,000	28,25,000
Add : Income over ₹ 1 crore	1,30,000
(b)	29,55,000
Tax [(a) or (b) whichever is lower]	29,55,000
Add : Education Cess is SHEC @ 3%	88,650
Tax Payable	30,43,650

ILLUSTRATIONS ON ASSESSMENT OF HUF

Illustration 34. The following details have been supplied by the Karta, of an HUF aged 62 years. You are required to compute its total income and tax liability for the Assessment Year 2016-2017.

Particulars	₹
(i) Profits from business (after charging ₹ 1,00,000 salary to Karta for managing the business)	15,00,000
(ii) Salary received by the member of a family	60,000
(iii) Director's fee received by Karta from B Ltd where HUF holds 20% shares but he became director because of his qualifications,	40,000
(iv) Rental income from house property (after deduction of municipal taxes ₹12,000)	78,000
(v) Dividends (gross) from Indian companies	15,000
(vi) Long-term Capital Gain	80,000
(vii) Short-term Capital Gain	30,000
(viii) Donation to a school, which is an approved institution	1,00,000
(ix) Deposits in Public Provident Fund	20,000
(x) NSC-VIII issues purchased	40,000

Solution:

Computation of Total Income for the A.Y. 2016-17

Particulars	₹	₹
(i) Income from House Property:		
Gross annual value (₹ 78,000 + ₹ 12,000)	90,000	
Less: Municipal Taxes paid	12,000	
Annual value	78,000	
Less: Statutory deduction: 30% ×78,000	23,400	54,600
(ii) Profits and gains from business		15,00,000
(iii) Capital Gains (a) long-term + (b) short-term		1,10,000
(iv) Income from other sources—gross dividends from Indian companies: Exempt [Sec. 10(34)]		Nil
Gross Total Income		**16,64,600**
Less:		
1. Contribution to approved savings (Sec. 80C)		
(i) Deposits in Public Provident Fund	20,000	
(ii) NSC-VIII Issue	40,000	
2. Donation to recognised school:	60,000	
(a) Actual donation: ₹ 1,00,000 or		
(b) 10% of adjusted total income = (Gross Total Income – Long Term Capital Gains – All deductions under Chapter VIA excluding Sec. 80G) of ₹ 15,24,600 (16,64,600 - 80,000 - 60000) whichever is less, is qualifying amount.		
Amount of deduction: 50% of ₹ 1,00,000	50,000	1,10,000
Total Income		**15,54,600**

Computation of Tax Liability:

Particulars of total income	Rate of income tax		₹
	₹	₹	
(a) Long-term Capital Gain	80,000	20%	16,000
(b) Balance of total income: ₹ 14,74,600			
(i) First	2,50,000	Nil	—
(ii) Between 2,50,000 – 5,00,000	2,50,000	10%	25,000
(iii) Between 5,00,000 – 10,00,000	5,00,000	20%	1,00,000
(iv) Between 10,00,000 – 14,74,600	4,74,600	30%	1,42,380
Gross Income Tax			**2,83,380**
Add: Education cess @ 2% on income tax			5,668
SHEC @ 1% on income tax			2,834
Tax Payable			**2,91,882**
Rounded off u/s 288B			**2,91,880**

Note : Assumed applicability conditions of AMT are not satisfied and hence, AMT provisions are not applicable.

Illustration 35. Prem was the Karta of HUF. He died leaving behind his major son Anand, his widow, his grandmother and brother's wife. Can the HUF retain its status as such or the surviving persons become co-owners?

Solution:

Income-tax law does not require that there should be at least two male members to constitute an HUF [Gowli Buddanna vs. CIT (1966) 60ITR 293 (SC)]. The expression "Hindu Undivided Family" used in the Act should be understood in the sense in which it is understood under the Hindu personal law. The expression "Hindu Undivided Family" under the Income-tax Act is known as "Joint Hindu Family", under the Hindu personal law. A 'Joint Family' may consist of a single male member and the widows of the deceased male members. The property of the Hindu joint family does not cease to be an HUF property merely because that the HUF, consist of one male member at a given point of time, exercising the proprietary rights over the property of HUF property.

Illustration 36. J (HUF) was the owner of a house property, which was being used for the purposes of a business carried on by a partnership firm JC & Co. in which the Karta and other members of the HUF were partners in their individual capacity. The Assessing Officer proposes to assess the annual letting value of the said property as the HUF's income from house property. The HUF contends that the building was used for business purposes and, therefore, the annual letting value thereof was not taxable in its hands as income from house property under Sec. 22. Examine the rival contention.

Solution:

Section 22 directs not to tax the annual value of a house property which is used by the owner for his business profession, the profits of which are chargeable to tax. In the instant case, the HUF is not using its property for its business. The Karta of the Hindu undivided family and other members of the HUF are partners in the firm in their personal capacity. They have not joined the partnership on behalf of the HUF. Therefore, it cannot be said that the HUF property was being used by the HUF for its business. Hence, the Assessing Officer is justified to tax the income of the HUF property as income from "House Property".

Illustration 37. J.Hazra was the Karta of a Hindu Undivided Family which was assessed to income tax. He died in an air crash and his two sons received ₹ 8 lakhs as compensation and ₹6 lakhs from the insurance company. The said amount of ₹ 14 lakhs was invested in units. The assessee claims that the income from these units is assessable as income of the Hindu Undivided Family composed of his sons and their families. Discuss.

Solution:

The right to receive compensation and insurance claim did not vest in the assessee during his life-time. It came into existence only after his death. The income from investment and compensation would be personal income of the assessee [CIT vs. L. Bansi Dhar & Sons (1980) 123 ITR 58 (Del.)].

Illustration 38. C, the Karta of a Hindu Undivided Family, was appointed as the treasurer of a private sector bank on his furnishing security of the family property valued at ₹ 3,00,000, as required by the service rules of the bank. C does not own any self-acquired property.

(i) Discuss how the remuneration of C as the treasurer should be assessed.

(ii) Will your answer be different if C had joined a partnership firm as a partner by contributing family funds of ₹ 30,000.

Solution:

(i) Remuneration from bank cannot be treated a return on the security of family property, pledged with the bank to secure the continuity of service. It cannot be treated as income of the HUF.

Remuneration is a compensation for services rendered by C, in his personal capacity on account of personal qualifications. C is assessable on remuneration as income from "salary". He can claim standard deduction under Sec. 16.

(ii) Membership of partnership has been obtained because of HUF funds and not because of personal skill or qualification of C. Therefore, any income from partnership firm will be treated as income of the HUF.

Illustration 39. Ordinarily a partition means that a separated member ceases to belong to the joint family. Does a female member cease to be a member of the joint family because of the concept of the notional partition introduced by the Hindu Succession Act, 1956?

Solution:

No. There was such a misapprehension because of the decision of the Supreme Court in the case of G.K.Magdum vs. H.K. Magdum (1981) 129 ITR 440 (SC) holding that there is a deemed partition on the death of a coparcener, when there is a female heir with right to his share of the joint family property. But it was pointed out in State of Maharashtra vs. Narayan Rao Sham Rao Deshmukh (1987) 163 ITR 31 (SC) that unless it is given effect HUF will be deemed to continue with all the assets. The share is ascertained, but there is no partition unless there is exercise of such right on the part of the female member.

The Supreme Court judgment in State of Maharashtra vs. Narayan Rao Sham Rao Deshmukh (1987) 163 ITR 31 (SC) was followed in the context of capital gains in CIT vs. Vishwas D. Ranade (2004) 266 ITR 730 (Bom.).

Illustration 40. Can a partitioned family be reunited?

Solution:

Yes. It can be done as between the members who were parties to the original partition in respect of all the properties covered by it.

Illustration 41. In levying wealth tax on the family, can the share of the female heir be excluded?

Solution:

No. Following Gurupad Khandappa Magdum vs. Hirabhai Khadappa Magdum ((1981) 129 ITR 440 (SC) it was though that on the death of a coparcener, there is a notional partition, which could be given effect. But the subsequent decision in State of Maharashtra vs. Narayan Rao Sham Rao Deshmukh (1987) 163 ITR 31 (SC), it was clarified, that the share can be taken out only on actual partition by metes and bounds.

Illustration 42. Can voluntary foregoing be taken as partition?

Solution:

No. There should be a division by metes and bounds. Where an assessee agreed to have only a life interest with a charge to the son, and wife, it was held, that a voluntary charge will not amount to partition. Consequently, the charge was held to be not deductible in computing property income [CIT vs. Satyanarayana Sikaria (1999) 238 ITR 855 (Gau)].

Illustration 43. Can partition be oral?

Solution: The Supreme Court, no doubt, held that partition could be oral in Hans Raj Agarwal vs. Chief CIT (2003) 259 ITR 265 (SC). But in practice, it is reduced to writing, when it required registration. But a family arrangement entered into orally but later reduced to writing will not require registration CIT vs. R. Ponnammal (1987) 164 ITR 706 (Mad) following the Supreme Court decision in Kale vs. Dy. Director of Consolidation, AIR 1976 SC 807.

Illustration 44. Can the status be disturbed in reassessment proceedings, where it had been accepted in the original assessments?

Solution:

No. The status has been accepted after due enquiries in the original assessments. The status cannot be changed in the reassessment.

Illustration 45. X and Y, two brothers, constituted an HUF. Y died. X was an issueless widower. There were no other persons entitled to any claim upon the stage, nor were there any widows or other female members of the family with rights to maintenance. In his return of wealth, X claimed his status to be that of HUF. Is the claim correct?

Solution:

No. The property in the hands of a sole surviving coparcener of an HUF has to be assessed as the property of an individual [Ramachandra Rao (K.R.) vs. CWT (1963) 48 ITR 959 (Mad.)].

In view of the observations of the Supreme Court in Krishna Prasad vs. CIT (1974) 97 ITR 493 (SC) to the effect that a family signifies a group and it is essential therefore that there should be plurality of persons to constitute a family, a single male member cannot be treated as an HUF.

However, as pointed out by the Allahabad High Court in the case of Prem Kumar vs. CIT (1980) 121 ITR 347 (SC) HUF will come into existence when the sole surviving coparcener marries or even when he adopts a child.

Illustration 46. Does an inherited property always entail assessment as HUF?

Solution:

There is a distinction between a joint family and coparcenery. Coparceners in Mithakshara have a right in property by birth. Others, particularly females, have other rights like maintenance, etc., though these rights have been enhanced by successive legislation.

Though there is a single coparcener, there can be joint family with other members.

Illustration 47. Is it open to a female member to convert her property to that of a joint family of which she is a member?

Solution:

No. The Supreme Court has held in Pushpa Devi vs. CIT (1977) 109 ITR 730 (SC) that it is not possible under the Hindu Law. There is, however, no prohibition against her giving a gift to joint family as long as she makes her intention clear that the gift is to the Hindu Undivided Family.

Illustration 48. What is meant by "potential HUF"?

Solution:

An individual who receives family assets by partition or survivorship is an individual and assessable for income-tax purposes as an individual. Since it is generally accepted that he can assume the role of karta of a Hindu Undivided Family on his marriage in respect of such property, he is known as potential HUF, not assessable as HUF till marriage.

Illustration 49. When a Hindu throws his assets in common hotchpot, what is the tax incidence?

Solution:

The income of joint family arising out of blending will continue to be treated as belonging to him because of the clubbing provision under section 64. Even after partition of such family, the income from such converted assets to the extent to which it is allotted to wife will be treated as belonging to him. Gift tax having been abolished, there is no gift tax implication for transfers made on or after 1st October 1998.

Illustration 50. A Hindu Undivided Family, which was not earlier assessed had disrupted by severance of interests of coparceners without division by metes and bounds. Is it open to the Assessing Officer to treat the same as HUF?

Solution:

No. It is because an order recognising partition u/s 171 is not necessary for an HUF, which has not been "hitherto assessed". Since it had already disrupted within the meaning of Hindu Law, assessment can be made only in the hands of members of their respective shares.

Illustration 51. Is it open to the Assessing Officer to keep an application for partition under section 171 open without disposal and continue to make assessment on HUF on the ground that no order has been passed recognising partition so as to enable separate assessments?

Solution:

No. The Supreme Court in Kapurchand Shrimal vs. CIT (1981) 131 ITR 451 (SC) held that such assessment will not be valid and it has to be set aside so that assessment can be made in conformity with the order under section 171, which the Assessing Officer is bound to pass in accordance with law.

Illustration 52. Does a married daughter still remain a coparcener/member of the HUF of paternal side after she becomes a member of her husband's or father-in-laws HUF?

Solution:

A daughter on her marriage ceases to be a member of her father's family and becomes the member of the family of her husband. She cannot be a member of both the families. She had never been a coparcener in her father's family nor will she become one in her husband's family. Her right under Hindu Law is confined to maintenance but Hindu Succession Act, 1956 gives her a right equal to the share of her brother in respect of an individual property of father and the share of her father is the joint family property.

Illustration 53. Can there be multiple HUF besides individual status for a person?

Solution:

There can be more than one HUF. There can be even three families, for example, a person can be a member of a larger family of which the grandfather is the karta, while he may be a member of the smaller family with his father as karta, the smaller family having been formed by partial partition or by will or by gift or blending. He can be a karta of a third family with himself as karta, if he were married, with his wife and children, if any. At the same time, he can have individual status as well.

ILLUSTRATIONS ON ASSESSMENT OF FIRM / LLP

Illustration 54: R (29 years) and S (28 years) are two partners of R&S Co. (a firm of Cost Accountants). On March 31, 2015, there is no provision for payment of salary and interest to partners. On April 1, 2015, the deed of partnership has been amended to provide salary and interest as follows:

Particulars	R	S
Salary	₹ 21,000 per month	₹ 23,000 per month
Interest	14 per cent per annum	14 per cent per annum

The Income and Expenditure Account of R&S Co. for the year ended March 31, 2015 is as follows:

Particulars	₹	Particulars	₹
Office Expenses	2,59,000	Receipt from clients	10,57,000
Salary to employees	80,000	Interest recovered from R and S on drawings	3,000
Income tax	41,000		
Salary to R	2,52,000		
Salary to S	2,76,000		
Interest on capital to R @ 14% p.a.	14,000		
Interest on capital to S @ 14% p.a.	21,000		
Net Profit (shared by R and S equally as per the terms of partnership deed)	1,17,000		
	10,60,000		10,60,000

Other Information:

1. Out of office expenses, ₹ 19,000 is not deductible by virtue of sections 30 to 37.
2. During the year the firm sells a capital asset for ₹ 8,10,000 (indexed cost of acquisition being ₹ 1,88,865).
3. Personal income and investments of partners are as follows:

Particulars	R ₹	S ₹
Interest from Government securities	5,70,000	5,23,000
Fixed Deposit interest	2,00,000	1,08,000
Deposit in public provident fund	1,00,000	85,000
Mediclaim insurance premium	12,000	11,000

Find out the net income and tax liability of the firm as well as the partners for the Assessment Year 2016-17.

Solution :

Particulars	₹	₹
Computation of net income/tax liability of the firm		
Net profit as per Income and Expenditure Account		1,17,000
Add:		
Income tax		41,000
Office expenses		19,000
Salary to R and S (₹2,52,000 + ₹2,76,000)		5,28,000
Interest to R and S [to the extent not allowed as deduction, i.e., {(₹ 14,000 + ₹ 21,000)-12/14 of (₹ 14,000 + ₹ 21,000)}]		5,000
Book Profit		7,10,000
Less: Remuneration to partners [maximum deductible amount is 90% of ₹ 3,00,000 + 60% of ₹ 4,10,000]		5,16,000
Income from the Profession		1,94,000
Capital Gains		
Sale proceeds	8,10,000	
Less: Indexed cost of acquisition	1,88,865	6,21,135
Net income (rounded off)		8,15,135
Tax		
Income-tax on Long-term Capital Gain [20% of ₹ 6,21,135]		1,24,227
Income-tax on balancing amount [@30%]		58,200
Tax		1,82,427
Add: Surcharge		Nil
Tax and surcharge		1,82,427
Add: Education cess (2% of tax)		3,649
Add: Secondary and higher education cess (1% of income-tax)		1,824
Tax liability of the firm (rounded off)		1,87,900

Computation of net income and tax liability of partners	R	S
	₹	₹
Profits and gains of business or profession Interest from the firm(to the extent allowed as deduction, i.e., 12/14 of ₹ 14,000 and ₹ 21,000)	12,000	18,000
Salary received from the firm(to the extent allowed as deduction, i.e., ₹5,16,000 distributed in the ratio of 63:69)	2,46,273	2,69,727
Income from profession	2,58,273	2,87,727
Income from other sources	7,70,000	6,31,000
Gross total income	10,28,273	9,18,727
Less: Deduction under sections 80C to 80U		
Under section 80C	1,00,000	85,000
Under section 80D	12,000	11,000
Net Income (rounded off)	9,16,270	8,22,730
Tax on income		
Income-tax	1,08,254	89,546
Add: surcharge	Nil	Nil
Tax and surcharge	1,08,254	89,546
Add: Education Cess (2% of tax)	2,165	1,791
Add: Secondary and Higher Secondary Education Cess (1% of tax)	1,083	895
Tax liability (rounded off)	1,11,502	92,232

Note: Interest recovered from partners is fully taxable.
Provisions of Alternate Minimum Tax are not applicable in the above cases.

Illustration 55 : Bebo and Lolo are partners in a partnership firm, K & Co. They share profit at a ratio of 1:4. The firm is engaged in the business of civil construction. The Profit and Loss Account of the firm for the year ended March 31, 2016 is as follows:

Particulars	₹	Particulars	₹
Opening stock of raw material	1,12,200	Sales turnover	48,90,400
Depreciation	2,56,400	Rent of a godown	60,000
Salary to employees	1,65,000	Interest on company deposits	1,86,800
Purchase of raw material	33,12,000	Closing stock of raw material	6,12,600
Interest on loan taken for business purposes	76,400		
Travelling expense	27,200		
Entertainment expense	12,500		
Advertisement expenses	33,700		
Other expenses	4,15,000		
Municipal tax and insurance (₹ 8,000 + ₹ 1,600) of godown	9,600		
Salary to partners as per partnership deed			
Bebo	2,28,000		
Lolo	2,40,000		
Interest to partners as per partnership deed @ 20 per cent p.a.			
Bebo	20,000		
Lolo	60,000		
Net Profit	7,81,800		
	57,49,800		57,49,800

Other Information:

1. Out of other expenses debited to P&L A/c ₹ 15,700 is not deductible under section 37(1).
2. Out of travelling expenses ₹ 7,500 is not deductible under section 37(1).
3. On April 1, 2015, the firm owns the following depreciable assets:

   Block 1 – Plants 1 and 2, depreciated value: ₹ 4,70,000, rate of depreciation : 15%.

   Block 2 – Plants 3 and 4, depreciated value : ₹ 5,20,000, rate of depreciation : 30%.

   On January 1, 2016, the firm sells Plant 4 for ₹ 8,90,000 and purchases Plant 5 (rate of depreciation 15%) for ₹ 4,00,000.
4. The firm gives a donation of ₹ 1,50,000 to a notified charitable institute which is included in other expenses.

The firm wants to set off the following losses brought forward from earlier years:

Particulars	Assessment Years	
	2014-15 ₹	2013-14 ₹
Business	25,000	—
Capital Loss (short-term)	5,000	3,000

Income of partners Bebo and Lolo is as follows:

Particulars	Bebo ₹	Lolo ₹
Interest on Fixed Deposits	5,36,000	8,20,000
LIC Premium paid (Capital Sum Assured is more than 10% of Premium paid)	50,000	80,000

Firm wants to pay tax under section 44AD. Find out the net income and tax liability of the firm and partners for the Assessment Year 2016-16 on the assumption that –

a. Conditions of sections 184 and 40(b) are satisfied; and

b. Conditions of section 184 and/or section 40(b) are not satisfied.

Solution:

Particulars	Situation (a): When conditions of sections 184 and 40(b) are satisfied ₹	Situation (b): When conditions of Section 184 and/or 40(b) are not satisfied ₹
Computation of business income of the firm		
Income from civil construction business [i.e., 8% of ₹ 48,90,400]	3,91,232	3,91,232
Less: Interest on capital to partners @ 12% [i.e.12/20×(20,000+60,000)]	48,000	—
Book Profit	3,43,232	3,91,232
Less: Remuneration to partners [i.e., 90% of ₹ 3,00,000 and 60% of ₹ 43,232]	2,95,939	—
Income from the business of civil construction	47,293	3,91,232
Computation of income	36,400	36,400
Property income [i.e., ₹ 60,000 – ₹ 8,000 – 30% of ₹ 52,000]	22,293	3,66,232
Business income (minus brought forward business loss)		
Capital Gain on sale of Plant 4 under section 50 [i.e., ₹ 8,90,000 – ₹ 5,20,000 – ₹ 8,000 brought forward Short-term Capital Loss)	3,62,000	3,62,000
Income from Other Sources	1,86,800	1,86,800
Gross Total Income	6,07,493	9,51,432
Less: Deduction under section 80G [i.e., 50% of 10% of ₹ 6,07,493 or ₹ 9,51,432]	30,375	47,572
Net Income (rounded off)	5,77,120	9,03,860
Tax	1,73,136	2,71,158
Add: Surcharge	Nil	Nil
Tax and surcharge	1,73,136	2,71,158
Add: Education cess (2% on tax and surcharge)	3,463	5,423
Add: Secondary and higher education cess (1% on tax and surcharge)	1,731	2,712
Tax liability (rounded off)	1,78,330	2,79,290

Computation of net income and tax liability of partners	Situation (a)		Situation (b)	
	Bebo ₹	Lolo ₹	Bebo ₹	Lolo ₹
Business Income:				
Interest from firm	12,000	36,000	—	—
Salary from firm (₹2,95,939 shall be divided between Bebo and Lolo in the ratio of 228 : 240)	1,44,175	1,51,764	—	—
Business income under section 28	1,56,175	1,87,764	—	—
Bank interest (fixed deposits)	5,36,000	8,20,000	5,36,000	8,20,000
Gross total income	6,92,175	10,07,764	5,36,000	8,20,000
Less: Deduction under section 80C	50,000	80,000	50,000	80,000
Net Income (rounded off)	6,42,175	9,27,764	4,86,000	7,40,000
Tax	53,435	1,10,553	23,600	73,000
Less: Rebate u/s 87A	—	—	2,000	—
	53,435	1,10,553	21,600	73,000
Add: Surcharge	—	—	—	—
Tax and surcharge	53,435	1,10,553	21,600	73,000
Add: Education Cess (2% of tax)	1,069	2,211	432	1,460
Add: Secondary and Higher Secondary education Cess [1% of tax]	534	1,106	216	730
Tax liability (rounded off)	55,038	1,13,870	22,248	75,190

Note : (i) Provisions of Alternate Minimum Tax are not applicable in the above cases.

(ii) Bebo & Lolo are assumed to be resident during the previous year.

Illustration 56 : A, B and C are three partners (3: 3: 4) of ABC & Co., a LLP engaged in manufacturing leather goods and it has agencies of different companies. The Profit and Loss Account of the LLP for financial year ended March 31, 2016 is as follows:

Particulars	₹	Particulars	₹
Cost of goods sold	7,90,000	Sales	21,22,000
Salary to staff	7,80,000	Long-term Capital Gains	3,00,000
Depreciation	2,50,000		
Remuneration to Partners :			
A	1,92,000	Short-term Capital Gain under	
B	96,000	section 111A	55,000
C	1,80,000	Other Short-term Capital Gain	65,000
Interest on capital to partners		Fixed deposit interest	50,000
A	17,000	Other business receipts	2,000
B	30,000	Interest on drawings recovered	
C	40,000	from A	16,000
Other expenses	1,65,000		
Net Profit:			
A	21,000		
B	21,000		
C	28,000		
	26,10,000		26,10,000

Other information:

1. The LLP satisfies conditions of sections 184 and 40(b).
2. The LLP is not eligible for deduction under section 80-IA/80-IB.
3. The LLP has given donation of ₹ 70,000 to a notified public charitable trust which is not debited to the Profit and Loss Account.
4. Up to March 31, 2015, there is no provision in the partnership deed to pay remuneration to partners. The deed is amended on April 1, 2015 to pay remuneration/interest to partners as under:

Particulars	Remuneration ₹	Interest on capital ₹
A	16,000 per month	17 per cent simple interest
B	8,000 per month	15 per cent simple interest
C	15,000 per month	20 per cent simple interest

5. Depreciation as per section 32 comes to ₹ 95,000
6. Other expenses to the tune of ₹ 65,000 is not deductible under sections 30 to 43D.
7. For the Assessment Years 2014-15 and 2015-16, the firm has assessed business loss of ₹ 30,000 and Long-term Capital Loss of ₹ 15,000 (which has not been set off so far).

Solution :

Particulars	₹
Computation of remuneration deductible under section 40(b)	
Net Profit as per P&L A/c (₹ 21,000 + ₹21,000 + ₹28,000)	70,000
Add:	
Depreciation debited to P&L A/c	2,50,000
Remuneration to partners (i.e., ₹ 1,92,000 + ₹96,000 + ₹1,80,000)	4,68,000
Interest to partners (to the extent not deductible) (i.e., 5/17 of ₹ 17,000 + 3/15 of ₹30,000 + 8/20 of ₹ 40,000)	27,000
Other expenses (to the extent not deductible)	65,000
	8,80,000
Less:	
Capital Gain (₹ 3,00,000 + ₹55,000 + ₹65,000)	4,20,000
Interest on Bank Fixed Deposit	50,000
Depreciation as per Section 32	95,000
Book Profit	3,15,000
Remuneration deductible (90% of ₹ 3,00,000 + 60% of ₹15000)	2,79,000

Computation of income of the firm	₹	₹
Business Income		
Book Profit	3,15,000	
Less : Remuneration deductible	2,79,000	
Balance	36,000	
Less : Brought forward business loss	30,000	6,000
Long-term Capital Gain (minus brought forward Long-term Capital Loss of ₹15,000)	2,85,000	
Short-term Capital Gain under section 111A	55,000	
Other Short-term Capital Gain	65,000	4,05,000
Interest on Fixed Deposit		50,000
Gross total income		4,61,000
Less: Deduction under Section 80G [i.e., 50% of 10% of ₹(4,61,000-2,85,000-55,000)]		6,050
Net Income (rounded off)		4,54,950
Computation of tax of firm		
Long-term Capital Gain (20% of 2,85,000)		57,000
Short-term Capital Gain under section 111A (15% of ₹ 55,000)		8,250
Other Income (30% of ₹ 1,14,950)		34,485
Total		99,735
Add: Surcharge		Nil
Total		99,735
Add: Education Cess		1,995
Add: Secondary and Higher Education Cess		997
Tax liability of the firm (rounded off)		1,02,730

Note:

1. Interest recovered from partners is fully taxable.
2. Provisions of Alternate Minimum Tax are not applicable in the above cases.

Illustration 57 : The following is the Profit and Loss Account for the year ended 31.3.2016 of XYZ (LLP) having 3 partners :

Profit and Loss Account

Particulars		₹	Particulars	₹
Establishment & other expenses		45,50,000	Gross Profit	69,20,000
Interest to partner @ 15%			Rent from house property	1,60,000
X	90,000		Interest on Bank deposits	20,000
Y	1,20,000			
Z	60,000	2,70,000		
Salary to designated partners				
X	2,40,000			
Y	1,80,000	4,20,000		
Net Profit		18,60,000		
		71,00,000		71,00,000

The LLP is eligible for 100% deduction under section 80-IC as it is established in notified area in Himachal Pradesh.

Compute the tax payable by the Limited Liability Firm.

Solution :

Computation of Total Income of XYZ (LLP) for the A.Y. 2016-17

	₹	₹	₹
Income under the head House Property			
Actual Rent		1,60,000	
Less : Deduction 30%		48,000	1,12,000
Business Income			
Net Profit as per P&L A/c		18,60,000	
Less : Income credited but either exempt or taxable under other head			
Rent	1,60,000		
Interest on bank deposit	20,000	1,80,000	
		16,80,000	
Add : Expenses disallowed			
Interest to partners in excess of 12% [i.e. 3/15×2,70,000]	54,000		
Salary to partners	4,20,000	4,74,000	
Book Profit		21,54,000	
Less : Salary as per section *40(b)* *(See* working note)		4,20,000	17,34,000
Income from Other Sources			20,000
Gross Total Income			18,66,000
Less : Deduction under section 80-IC		17,34,000	
Deduction under section 80TTA [Assumed Savings Account]		10,000	17,44,000
Total Income			1,22,000

Regular income tax payable on Total Income

Total Income of ₹ 1,22,000 @ 30%	36,600

Adjusted Total Income

Total Income	1,22,000
Add : Deduction u/s 80-IC	17,34,000
	18,56,000

Alternate Minimum Tax (AMT) 18.5% on ₹ 18,56,000 = ₹ 3,43,360

Hence, adjusted total income shall be total income and the tax (payable shall be the Alternate Minimum Tax) i.e. on ₹ 18,56,000 @ 18.5% + 3% (EC + SHEC).

Tax Payable

	₹
Alternate Minimum Tax 18.5% on ₹ 18,56,000	3,43,360
Add : 3% Education Cess & SHEC	10,301
	3,53,661
Rounded off	3,53,660
Working Note:	
Book Profit	21,54,000
Maximum salary allowed	
First 3,00,000 of book profit — 90%	2,70,000
Balance ₹ 18,54,000 of book profit 60%	11,12,400
	13,82,400

Salary allowed shall be ₹ 13,82,400 or ₹ 4,20,000 whichever is lower i.e. ₹ 4,20,000.

AMT Credit of ₹ 3,15,963 (3,53,661 – 37,698) is available which can be carried forward for ten Assessment Years.

Illustration 58. At the time of becoming a partner in the firm of M/s. XYZ, X brings in his house property as his share of capital in the firm. Does such bringing in of immovable property to the stock require registration u/s 17(1)(b) of the Registration Act?

Solution:

Where the property is brought in as capital during formation of partnership deed, there is no transfer at all within the meaning of the Transfer of Property Act, 1882, but u/s 14 of the Partnership Act 1932. Therefore, even if a property brought in by one partner be an immovable property, no document registered or otherwise, is required for transferring the property to the partnership [CIT vs. Royal Amber Resorts (1987) 164 ITR 311 (Raj.)].

Illustration 59. A firm consisting of four partners purchased a plot of land. The plot was all through treated as the property of the firm. By an agreement between the partners, the said plot was taken out of the partnership by crediting the plot account at the book value and debiting the partner's capital account in equal proportion in the books of the account of the firm. The plot was subsequently sold and capital gains offered by tax in the hands of partners? Is it valid?

Solution:

The capital gains is rightly assessable in the hands of the firm as the entries made in the books of account, the partners had not legally and effectively taken out the immovable property of the firm from its ownership and vested the same in the partners. The transfer could not have been affected to partners without a registered document on 15.6.1976. Since the firm alone is liable to capital gains tax, assessment of partners is not valid [CIT vs. J.M. Mehta & Bros. (1995) 214 ITR 716 (Bom)].

Illustration 60. An assessee entered into a partnership with a company giving the company 50% interest in her business of purchase and sale of lands, though the company did not bring any capital. No business in sale and purchase of land was conducted by the firm. Within three months of its formation, the assessee retired from the firm with the lands taken over by the company with the assessee being given shares equivalent to the balance in her capital account. The Assessing Officer held that there was no genuine partnership, that the transaction had shown that the assessee had received the value of her land and the transaction of transfer of land was subject to capital-gains. Whether the decision of the Assessing Officer is valid in law?

Solution:

The decision of the Assessing Officer is valid in law. The true nature of the transaction was "transfer of land" and the various steps in the process of leaving the land with the company were nothing but a device to avoid capital gains tax leviable u/s 45 of the Act. Hence capital gains tax is leviable[Nayantara G. Agarwal vs. CIT (1994) 207 ITR 639 (Bom)].

If a firm is formed merely to dissolve it, so as to affect a transfer by adopting the procedure under partnership law, the transaction becomes colourable and is, therefore, liable to be discarded. As long as there was an intention of dissolving the firm at the time of its formation, such inference that the transaction is colourable may well follow.

Illustration 61. The purpose of constituting a firm was for construction and letting out godowns. The Assessing Officer had taken the view that since partnership can be only for carrying on a business, there is no business in deriving income from property and that therefore the firm is not entitled to be treated as a firm so as to require registration when registration procedure was in vogue. Even after the registration procedure has been dropped, is it possible to treat it as a firm and not required to be treated as association of persons?

Solution:

Business for the purpose of partnership law is different from the concept under Income Tax Law, which requires income from property even in the hands of a property dealer to be treated as property income and not business income. Kerala High Court in CIT vs. George Oommen & Co (2001) 247 ITR 574 (Ker) has pointed out that the heads of income for income-tax purposes have no relevance in deciding whether there is business under Partnership Law. But for purposes of General Law and Partnership Law, business has to be understood in wider sense to include every profit making activity. It was so held in Smith vs. Anderson (1880) 29 WR 21 (CA). This difference was pointed out in CIT vs. Veerabhadra Industries (1999) 240 ITR 5 (AP).

In case property is purchased jointly and the property income is shared, it may be difficult to treat the income as from business. But where they are let out to more than one person with intent to make profit by joint activity or to realise surplus on resale, business can well be inferred. Where the partners decide to construct godowns and then let them out, the inference of business would arise more readily. Leasing out a factory may or may not constitute business depending upon the circumstances.

Where the partnership acquired a cotton ginning mill to run it but leased it out, it was decided that there is business and that partnership has to be recognised, in Nauharchand Chananram vs. CIT (1971) 82 ITR 189 (P&H). It was pointed out that leasing is also a business. Similar view was taken in CIT vs. Admiralty Flats Motel(1982) 133 ITR 895 (Mad) and CIT vs. Tirumalai Traders (1999) 238 ITR 661 (AP). The Supreme Court's decision in S.G. Mercantile Corporation P. Ltd. vs. CIT (1972) 83 ITR 700 (SC) has laid down the criteria for holding a property to be treated as a business asset.

Where a property was taken on lease a vast piece of land and derived income by allowing film companies to shoot films and sale of dairy products, the High Court remanded the case for further examination observing that the activities in one single year were not sufficient to hold that the income was from property and other sources. But where a group of persons derived income from rent without any other activity, such group cannot be recognised as a firm even if there be a partnership deed, so as to be entitled to registration [CIT vs. Y. Narayana Murthy (Decd.) (2004) 270 ITR 275 (AP)].

The same view was repeated by the Kerala High Court in Mrs. Grace S. George vs. CIT (1988) 170 ITR 412 (Ker.) and CIT vs. Jacobs (1986) 160 ITR 570 (Ker.). The issue had come up in Thayyil Enterprises vs. CIT (2006) 287 ITR 414 (Ker). But then, the business has to be understood in a wider sense while considering the provisions of Partnership Law. Earning income from leasing out property has been understood to be business.

Illustration 62. Can a minor share loss? If the partnership deed provides for such share, can the firm be recognised as validly formed? Is a fresh deed necessary when the minor attains majority?

Solution:

A minor is not competent to contract. He cannot also be made liable for loss except to the limited extent of profits earlier made. Where a partnership deed makes a minor liable for share of loss, such partnership cannot be recognised as a firm for purposes of registration. This was followed in CIT vs. Badri Nath Ganga Ram (2005) 273 ITR 485 (All.). It is not necessary that a fresh partnership should be formed with the erstwhile minor, since he will continue as a partner unless he had expressed his intention otherwise.

Illustration 63. Is it advisable to form an association rather than a firm from tax point of view?

Solution:

An association of persons in General Law is not governed by either partnership law nor is it entitled to treatment available for partnership firms. Partnership Law regulates the relationship between the partners and their mutual rights and obligations, which are well-defined, while an association of persons is governed solely by the terms of agreement between them, all of which may not be anticipated and reduced to writing giving scope for differences. It is better to have an entity known to law. Those who deal with a firm or a company know the liability of the persons with whom they are dealing, so that AOP will find it difficult to borrow or obtain credit. It is because a person, who deals with such association, would feel uncertain of his rights, so that even from business point of view it is not advisable.

Illustration 64. Where there is dissolution of the firm during F.Y. 2014-2015, but distribution of assets in F.Y. 2015-2016, can the dissolved firm be made liable for the tax from A.Y. 2016-2017?

Solution:

Dissolution does not end the partnership. It only ends mutual agency. It was so pointed out in CIT vs. Pigot Chapman and Co (1982) 135 ITR 620 (SC). A dissolved firm continue till it is wound up under section 45 of the Partnership Act. Section 189 authorises such assessment.

Illustration 65. What is the liability of a non-working partner as regards liability of firm after dissolution?

Solution:

Every partner is jointly and severally liable for the debts of the firm. Intervening dissolution makes no difference. It was so held in Dhanpat Rai Verma vs. TRO (2004) 268 ITR 215 (All).

Illustration 66. Is it necessary to redraft the partnership deed for conversion of firm into Company?

Solution:

The need for having minimum of 7 partners in case of conversion cannot be dispensed with, if the object is to get registered as a limited company. Section 565(1)(b) requires that only a company consisting of 7 or more members has a right to get registered as a company under Part-IX of the Companies Act. In order to get registered as a company with limited liability it is necessary that the conditions which go with the requirement of limited liability are made part of the partnership deed itself, the main requirement being that there should be fixed capital for partners with proper sharing ratio corresponding to ratio of capital fixed for the partners. Any other clause which contradicts the concept of fixed capital, as for example, the usual clause that partners will bring in such additional capital as may be required for the purpose of business, may jeopardise registration, since capital is required to be fixed or companies with limited liability. It is in this context that a partnership firm may find it easier to first get registered as a company with unlimited liability and then take steps for converting such company with unlimited liability to one of limited lability by following the procedure u/s 32 of the Companies Act. It is, however, necessary that there should be positive share capital in either case.

Illustration 67. What is better, whether slump sale or severable itemised sale?

Solution:

In a slump sale from A.Y. 2000-2001, there is no benefit of indexation, the difference between book value and consideration is assessed. In a severable sale, the Capital Gain of asset has to be computed, so that in respect of long-term assets, benefit of indexation is available. But where the prospect of short-term capital gains is higher because of extent of depreciable assets comprised therein in severable sale, slump sale is preferable. Hence, what is preferable will be a matter to be considered with reference to facts in each case.

Illustration 68. If a slump sale is made by a firm to a company in a manner that the benefit of exemption u/s 47(xiii) is availed and thereafter the company amalgamates with another company, will there be forfeiture of exemption though 50% parity of ownership may not continue?

Solution:

It was once thought that amalgamation could not be transfer in view of the decision of the Supreme Court in CIT vs. Rasiklal Maneklal (HUF) (1989) 177 ITR 198 (SC) rendered in the context of Capital Gains Tax under the earlier law in which there was no exemption available for amalgamation. But then the

Supreme Court in a recent decision in CIT vs. Grace Collis (2001) 248 ITR 323 (SC) has held that the later extension of the definition of transfer to include extinguishment would mean that amalgamation is also transfer, so as to make the shareholder liable for tax. The fact that amalgamation is expected u/s 47(vi) and (vii) itself shows that it is otherwise a transfer, though not regarded as transfer for the limited purpose of the provision.

Hence, even if the condition of 50% parity is maintained it may still be construed as violation of condition u/s 47(xiii) of the Act and exemption may be lost.

Illustration 69. What are the tests for inferring business to be one as a going concern or a business as a whole in contrast with severable sale? Is it possible to reduce the incidence of tax in these transactions?

Solution:

In a sale of business as a whole, transferred as a going concern with all assets and liabilities, the seller will not be able to withdraw any asset while the buyer will not be able to reject any such assets of business. Similarly, the buyer cannot refuse to takeover any liability. Even if it is not so strictly complied with, it may still pass muster as a slump sale, because slump sale is defined in a wider sense, since Explanation-1 to section 2(19AA) would define an undertaking to include any part of an undertaking or a unit or division of an undertaking or a business activity taken as a whole, while ruling out only transfer of individual assets and liabilities or for combination thereof not constituting a business activity. What is implied is that the transferred entity must be a unit capable of being sold as such, though it may be a part of a larger undertaking. Hence a slump sale under Income Tax Law may be of a business activity, while for Sales Tax Law it may include a unit or a division but cannot possibly include a mere business activity. Where it is a unit or division, it may be capable of being considered as a separate business in some cases where all its assets and liabilities are transferred.

Illustration 70. Is it permissible for a company formed by conversion of firm under the Companies Act, 2013 to avail unabsorbed losses and depreciation of the firm against its profits? What is the position of relief under sections 10A, 10B, 80-IA and 80-IB, etc.?

Solution:

Where a firm had been converted into company by following the process of the Companies Act, 2013, there should be no difficulty for such company in getting the unabsorbed loss and depreciation even without satisfying the condition under section 47(xiii). It has been so held in Chetak Enterprises Pvt. Ltd. vs. Asst. CIT (2006) 281 ITR (AT) 162 (Jodh.) that relief u/s 80IA would continue to be available, notwithstanding such conversion under Part IX route. In CIT vs. Texspin Engineering and Manufacturing Works (2003) 263 ITR 345 (Bom), it was held that there was no liability for Capital Gains Tax, since there is no transfer. On the same reasoning, there is no hindrance in availing benefit of carried forward loss and depreciation by the company converted by Part IX route for availing firm's losses and depreciation. Similar view was also taken in CIT vs. Rita Mechanical Works (2012) 344 ITR 544 (P&H).

W.e.f. A.Y. 2002-2003, section 47(xiii) exempts from capital gains, transfer of assets of a firm, etc. to a company in the course of demutualization or corporatarisation of a recognised stock exchange as a result of which such firm or Association of Persons etc. is succeeded y a company.

Illustration 71. Is it possible for two firms to merge with each other without any tax consequence?

Solution:

The concept of merger or amalgamation is unknown to partnership law. Where a partnership business is taken over by another firm, there is a profit liable to Capital Gains Tax.

Illustration 72. Is it possible for two firms to convert themselves as companies under Part-IX of Companies Act and thereafter for both the companies to amalgamate so as to avoid capital gains on merger of the business of the two firms?

Solution:

The conversion and the later merger are two independent steps. Each should be justified by bona fide commercial considerations and not solely for saving tax. There is no liability at both stages, subject to conditions under the relevant provisions of law.

Illustration 73. Is it possible to avoid capital gains tax, where cost is not ascertainable?

Solution:

No. Cost has to be based on best estimate, where evaluation is not possible for lack of details. Law itself in some cases attributed nil cost for certain categories of assets listed u/s 55(2)(a). Written down value will be taken as cost in case of depreciable assets u/s 50. Net worth on the basis of book value will be taken in a slump sale under section 50B.

Illustration 74. Where a company has already been formed for takeover of the business of an existing firm, is it really necessary to get the benefit of Part IX conversion in a case where firm's business is taken over by company?

Solution:

The difference between conversion of firm to a company by registration under Part IX and takeover of a business by a company from a firm, was pointed out in Stewart & Co. Ltd. vs. C. Marshal AIR 1963 Cal 198 (DB). The incidence under property law and tax laws should be different. The liability to stamp duty is one difference. This can be avoided by registration under Chapter IX of the Companies Act.

Illustration 75. Is conversion of a private company to LLP exempt for purposes of capital gains? If the exemption is limited, what is the purpose of limitation?

Solution:

Exemption is limited only to companies with gross turnover not exceeding ₹60 lakh. The purpose apparently is that a big company does not avoid the incident of deemed dividend u/s 2(22)(e) and Minimum Alternate Tax by conversion to LLP.

Illustration 76. Are all companies eligible for conversion to LLPs?

Solution:

No. Only private limited companies and unlisted public companies are eligible for conversion under section 56 and 57 of the Limited Liability Partnership Act, 2008.

Illustration 77. What happens to partners/ shareholders of firm/ company, where the conversion to LLP does not satisfy the condition under section 47(xiiib)?

Solution:

Where the firm/ company does not qualify for exemption under section 47(xiiib), the conversion is still valid under Limited Liability Partnership Act, 2008. But the tax on capital gains arising on transfer will be the responsibility of LLP. The partners of the firm have no liability which has got converted to LLP on the transfer of shares consequent on conversion.

Illustration 78. Which is the regulatory authority of Limited Liability Partnership, whether Registrar of Firms or Registrar of Companies?

Solution:

Limited Liability Partnership Act, 2008 provides for administration of the Act with company law authorities with all powers for Registrar of Companies as are available to him under the Companies Act, 2013.

Illustration 79. Can an LLP be understood as body corporate independent of its partners?

Solution:

Yes. Section 2(d) of Limited Liability Partnership Act, 2008 understands the LLP as body corporate.

Illustration 80. Are all partners of LLP equally responsible for the acts of LLP?

Solution:

The LLP expects, at best, two of the partners to be "designated partners" whose responsibility will be on par with directors of the company.

Illustration 81. What are the formalities of conversion?

Solution:

Formalities are prescribed for conversion of firm, private companies and unlisted public companies under the Second, Third and Fourth Schedules respectively of the Limited Liability Partnership Act, 2008.

ILLUSTRATIONS ON ASSESSMENT OF COMPANIES

Illustration 82. RQ Ltd. has huge loss and depreciation to be carried forward. ST Ltd. is making profits. What should company RQ Ltd. do wipe off its losses within a reasonable time by taking the help of ST Ltd.?

Solution:

Amalgamation should not have been for mere tax saving like avoiding capital gains tax or merely for avoiding the benefit of set-off of losses and depreciation of a company, which is going defunct. It should satisfy the conditions u/s 72A, if profit making company is taking over a loss making company. Reverse merger, if genuine, will avoid the application of section 72A.

Illustration 83. Company A wants to amalgamate with B. The agreement is entered into on 1.7.2015 indicating the appointed day to be 1.4.2015. The Court however passes the order approving the merger on 15.4.2016. What is the date of amalgamation?

Solution:

The amalgamation will take effect from 1.4.2015, which is the appointed day, unless such date is varied by the High Court [Marshall Sons and Co. (India) Ltd. vs. ITO (1997) 223 ITR 809 (SC)].

Illustration 84. Amalgamation of companies X and Y has been approved by the BIFR. CBDT refuses to allow carry forward of losses u/s. 72A. Is the CBDT justified?

Solution:

No. According to the Supreme Court in Indian Shaving Products Ltd. vs. BIFR (1996) 218 ITR 140 (SC), once the approval has come from BIFR, Board cannot refuse carry forward of losses.

Illustration 85. A certain family has four companies with different members controlling the companies. There are differences. How could they affect a partition of their interest in the companies?

Solution:

They can shuffle their interest in the companies to ensure independence for each member/ group of members. But capital gains tax cannot be avoided. Demerger is an alternative. Demergers are exempt. It allows set-off of carried forward of past depreciation and unabsorbed loss subject to conditions prescribed under section 72A.

Illustration 86. Should the character of assets as between investments and stock-in-trade be the same both for amalgamating and amalgamated company?

Solution:

Answer will be in the affirmative, if the business is taken over as a going concern and earned on by the amalgamated company [Devare (L.M.) vs. CIT (1998) 234 ITR 813 (Bom.)].

Illustration 87. Since there is always a time lag between appointed date under the scheme and court's order, who should be liable for tax compliance during the interregnum?

Solution:

During the interregnum, the pre-existing management will be in charge. As soon as the amalgamation is approved, legal responsibility will be that of the amalgamated company following the decision of the Supreme Court in Marshall Sons and Company (India) Limited vs. ITO, (1997) 223 ITR 80 (SC).

Illustration 88. Is a slump sale an alternative to amalgamation and demerger?

Solution:

Yes. It is possible for a division or unit to be sold by slump sale or sell the asset in a severable sale to achieve the same object.

Illustration 89. Does the liability of shareholder get altered in amalgamation, demerger or slump sale?

Solution:

No. Amalgamation, demerger or slump sale by a company constitute a taxable event for company and not the shareholder.

Illustration 90. Where there is an acquisition by way of an industrial undertaking or business as a going concern by way of slump sale, can the successor avail the losses and depreciation of the transferred industrial undertaking or business?

Solution:

The law does not provide for benefit of set-off of losses and depreciation, where a business is transferred by way of slump sale.

Illustration 91. What is written down value to be adopted for the amalgamated company in cases, where the full eligible depreciation had not been availed by the amalgamating company?

Solution:

Explanation (2A) to section 43(1) provides that the written down value of the amalgamating company should be the actual cost for the amalgamated company. In CIT vs. Hindustan Petroleum Corporation Ltd. (1991) 187 ITR 1 (Bom.), it was held that the actual cost of the asset need be reduced only by the unabsorbed depreciation availed (absorbed) in the hands of the amalgamating company for purposes of "actual cost" of such transferred assets in the hands of amalgamated company, unless it satisfies the condition under section 72A. This decision was followed in CIT vs. Kothari Industrial Corporation Ltd. (2005) 274 ITR 600 (Mad.) and CIT vs. Silical Mettalurgic Ltd. (2010) 324 ITR 29 (Mad). If these decisions are correct, there will be double deduction in cases where assessee avails set-off of past unabsorbed depreciation under section 72A.

The decision has not taken into consideration Explanation 7 to section 43(1), which provides for determination of actual cost of assets taken over by amalgamated company on amalgamation to be the same as for amalgamating company as if the amalgamated company had continued to hold the asset. It follows that the written down value will have to be taken as that of the amalgamated company. Explanation 2, 2A and 2B to section 43(6) providing for computation of written down value for the amalgamated company is also in conformity with Explanation 7 to section 43(1). The decision, therefore, run counter to these statutory provisions. There is, however, no reaction from revenue to the decisions of the High Court, which should probably work in favour of the taxpayer.

Illustration 92. Where the amalgamated company sells the asset obtained from amalgamating company is the option of substituting the cost at market value on specified date available?

Solution:

It has been decided that such option is available in Harish Mahindra vs. CIT (1982) 135 ITR 191 (Bom.); H.F. Craig Harvey vs. CIT (2000) 244 ITR 578 (Mad.) and Madura Coats Ltd. vs. CIT (2005) 279 ITR 493 (Bom.). In all these cases, it was held that the amalgamated company steps into the shoes of amalgamating company, since amalgamation is not regarded as transfer. It follows, that the benefit of indexation should also be available for amalgamating company including the period of holding of the asset by the amalgamating company.

Illustration 93. What is the procedure for service of notice for assessment of amalgamating company, when it has ceased to exist on amalgamation?

Solution:

The amalgamated company cannot avoid the tax liability of the amalgamating company. Notice of reassessment can be issued on the amalgamated company as successor to amalgamating company to assess or reassess the income of the amalgamating company, subject to conditions therefor [Triveni Engineering and Industries Ltd. vs. Dy. CIT (2006) 280 ITR (AT) 210 (Del.)].

Illustration 94. Will incentive deductions available for amalgamating company continue for the remaining period to the amalgamated company?

Solution:

Yes, if the same conditions are continued to be complied with, it will be available. Amalgamation cannot be considered as reconstruction, so that the benefit of deduction is not lost [CIT vs. Silical Metallurgical Ltd. (2010) 324 ITR 29 (Mad)].

Illustration 95. How is the cost of an asset taken over in a slump sale ascertained?

Solution:

Where the asset having been taken over in a slump sale, there is no separate consideration paid for any asset unlike a severable sale. But purchase consideration for the amalgamating company will be available. It is such consideration, which will be the cost for purposes of section 41(2) or 50, as the case may be [CIT vs. Mahindra and Co. Ltd. (2010) 326 ITR 465 (Raj)].

Illustration 96. From the following information, determine the tax liability of Z Ltd., domestic company, for the Assessment Year 2015-2016 and 2016-2017.

S. No.	Assessment year	Book-profits (₹)	Total income (₹)
1.	2015-2016	2,80,000	1,30,000
2.	2016-2017	3,00,000	2,00,000

Solution :

Surcharge is not considered assuming, Net Income less than ₹ 1 crore

Assessment Year	**Book-profit (₹)**	**Total Income (₹)**	**Tax on Book-Profit (₹)**	**Tax on Total Income @ 30.9% rounded off u/s 288B (₹)**	**Tax Credit = Tax on Book Profits (–) Tax on Total Income (₹)**	**Tax Payable after tax credit set off, if any (₹)**	**Tax credit balance (₹)**
2015-2016	2,80,000	1,30,000	@ 19.055% on 2,80,000 = 53,354	@ 30.9% on 1,30,000 = 40,170	13,184	53,354	13,184
2016-2017	3,00,000	2,00,000	@ 19.055% on 3,00,000 = 57,165	@ 30.9% on 2,00,000 = 61,800	—	57,165 [restricted to ₹57,165]	8,549 [13,184 - 4,635]

Note : 1. Tax Payable is rounded off to the nearest multiple of ₹ 10 (Sec. 288B)

2. As per Section 115JD, the tax credit shall be allowed to be set-off to the extent of the excess of regular income-tax over the alternate minimum tax and the balance of the tax credit , if any, shall be carried forward.

Illustration 97. Fashion Ltd., a well-diversified group, given below its Profit and Loss Account for the Previous Year 2015-2016 :

Particulars	₹	Particulars	₹
Manufacturing expenses	9,00,000	Sale of manufactured goods	15,00,000
Salaries/wages	5,50,000	Sale of agriculture produce	10,00,000
Cultivation expenses	4,00,000	Receipt from generation / distribution of power	15,00,000
Power generation/distribution expenses	4,00,000	Receipt from I.U. set up in backward district in July 2005	10,00,000
Irrigation expenses	6,00,000	Transfer from Reserve & Provision A/c, debited to Profit and Loss Account in 2007-08 on account of free service under warranty period	9,50,000
Expenses of I.U., located in backward district	5,00,000	Sale of goods of I.U. (Sec. 10B)	2,00,000
Expenses of I.U., located in free trade zone(Sec. 10A)	1,50,000	Sale of goods of I.U, located in free trade zone (Sec. 10A)	2,00,000
Expenses of I.U. (Sec. 10B)	1,00,000	Receipt from water supply/irrigation project	1,00,000
Expenses of I.U. located in NRE	50,000	Income from UTI	50,000
Provision for losses of subsidiary	4,00,000	Sale of goods of I.U. located in Northern Eastern Region (NER) (Sec. 10C)	5,00,000
Sundry expenses	10,000	Long Term Capital Gain on sale of equity shares, transaction chargeable to Securities Transaction Tax	35,00,000
Provision for bad and doubtful debts	2,00,000		
Provision for bills under discount	50,000		
Provision for sales tax against demand notice	3,30,000		
Income tax provision against demand notice	3,00,000		
Dividend paid on preference shares	2,00,000		
Proposed dividend on equity shares	4,00,000		
Transfer to General Reserve	1,00,000		
Dividend Equalisation Reserve	2,00,000		
Penalties under direct tax laws	60,000		
Goodwill written off	50,000		
Depreciation	3,00,000		
Amortisation of patent rights	30,000		
Expenses on transfer of equity shares	20,000		
Net Profit	42,00,000		
	1,05,00,000		**1,05,00,000**

The following additional information is provided as below:

1. Depreciation includes, a sum of ₹ 1,00,000 on account of revaluation of building and plant and machinery.
2. Past year losses, before depreciation, are given below:

	Loss (₹)	Depreciation (₹)
2011-2012	(-) 5,00,000	(-) 6,00,000
2012-2013	Nil	(-) 5,00,000
2013-2014	(-) 7,00,000	(-) 4,00,000
2014-2015	(-) 5,00,000	Nil

Compute book-profits for the Previous Year 2015-2016/AY 2016-2017 for MAT under Sec. 115JB.

Solution :

Computation of Book Profit for the AY 2016-2017

Particulars	₹	₹
Net Profit as per Profit and Loss Account		42,00,000
Add:		
(i) Cultivation expenses	4,00,000	
(ii) Expenses of I.U. located in Free Trade Zone (Sec. 10A)	1,50,000	
(iii) Expenses of I.U. under Sec. 10B	1,00,000	
(iv) Provision of loss of subsidiary	4,00,000	
(v) Provision for bad and doubtful debts— an unascertained liability	2,00,000	
(vi) Provision for bills under discount— an unascertained liability	50,000	
(vii) Provision for sales- tax against demand notice — an ascertained liability	—	
(viii) Income-tax provision— an ascertained liability to be added back	3,00,000	
(ix) Dividend paid on preference shares	2,00,000	
(x) Proposed dividend on equity shares	4,00,000	
(xi) Transfer to General Reserve	1,00,000	
(xii) Dividend Equalisation Reserve	2,00,000	
(xiii) Depreciation [Sec. 115JB(2)(g) w.e.f. AY 2011-2012]	3,00,000	28,00,000
Adjusted Profits		**70,00,000**
Less:		
(i) Sales of agriculture produce [Sec. 10(1)]	10,00,000	
(ii) Receipt from I.U. in Free Trade Zone [Sec. 10A]	2,00,000	
(iii) Receipt from I.U. Sec. 10B	2,00,000	
(iv) Depreciation, excluding depreciation on account of revaluatio of assets	2,00,000	
(v) Withdrawals from Reserve & Provision for free sale service, under warranty scheme	9,50,000	
(vi) Long-term capital gain on transfer of equity shares [Sec. 10(38)] — see Note below	Nil	
(vii) Receipts from UTI [Sec. 10(35)]	50,000	
(viii) Brought forward loss or depreciation, whichever is less.	9,00,000	35,00,000
Book-profits		**35,00,000**

Note: 1. Calculation of brought forward losses or depreciation:

2011-2012	Loss	5,00,000
2012-2013	Loss/depreciation	Nil
2013-2014	Depreciation	4,00,000
2014-2015	Loss/depreciation	Nil
	Total	9,00,000

2. Transfer from provision for after sale service, free of cost, made during the year 2007-2008, debited to Profit and Loss A/c and now credited to Profit and Loss A/c and the amount so credited to Profit and Loss A/c is an allowable deduction [Sec. 115-JB(2)].

3. Long-term Capital Gain from the transfer of equity shares in a company is exempt is chargeable to Securities Transaction Tax (STT). However, for the purposes of computing Book-profits, it is not to be deducted [Sec.10(38)]. Accordingly, the expenditure incurred for the transfer of equity shares has not been added back in computing Book Profits.

Illustration 98. Classic Exporters Ltd, runs a new industrial undertaking set up in 2006-2007 which satisfies the conditions of Sec. 80-IB. Given below is the Profit and Loss Account for the Previous Year 2015-2016 :

Particulars	₹	**Particulars**	₹
Stock	4,00,000	Domestic sales	24,00,000
Purchases	23,00,000	Export sales	43,00,000
Salaries and wages	9,70,000	Export incentives Sec. 28(iiia)/(iiic)	50,000
Entertainment expenses	1,30,000	Profit of foreign branch	2,50,000
Freights and insurance attributable to exports	3,00,000	Brokerage/commission/interest/ rent, etc	50,000
Travelling expenses	2,20,000	Transfer from contingency reserve	10,00,000
Depreciation	1,50,000	Stock	3,50,000
Selling expenses	1,20,000		
Income tax paid	90,000		
Income-tax penalty	30,000		
Custom duty payable against demand notice	30,000		
Provision for unascertained liabilities	20,000		
Provision for ascertained liabilities	50,000		
Proposed dividend	3,00,000		
Loss of subsidiary company	50,000		
Net Profit	32,40,000		
	84,00,000		84,00,000

You are further informed:

(i) Excise duty for 2014-2015, amounting ₹ 1,20,000 was paid on 15th December 2015.

(ii) Depreciation under Sec. 32 is ₹ 2,20,000.

(iii) During the year 2011-2012, contingency reserve, amounting ₹ 10,00,000, debited to Profit and Loss A/c, was added back to the extent of ₹ 4,00,000 in the computation of Book-profits. The company has transferred the said reserve to the Profit and Loss A/c during the year.

(iv) Brought forward business loss/depreciation:

PY	Accounting purposes		Tax purposes	
	Loss	Depreciation	Loss	Depreciation
2011-2012	(-) 10,00,000	(-) 1,00,000	(-) 5,00,000	(-) 2,50,000
2012-2013	(-) 2,00,000	(-) 3,00,000	(-) 1,00,000	(-) 2,00,000

Compute the following: (a) Total Income, (b) Book-profits and (c) Tax Liability.

Solution :

(a) Computation of Total Income for the AY 2016-2017

Particulars	₹	₹
Net Profit as per Profit & Loss A/c		32,40,000
Add : Expenses debited to P&L A/c – disallowed		
(i) Income tax	90,000	
(ii) Custom duty payable	30,000	
(iii) Provision for unascertained liability	20,000	
(iv) Proposed dividend	3,00,000	
(v) Loss of subsidiary company	50,000	
(vi) Income-tax penalty	30,000	
(vii) Depreciation	1,50,000	6,70,000
		39,10,000
Less : Allowable Expenses and wrong credits in P&L A/c		
(i) Withdrawals from contingency reserve	10,00,000	
(ii) Excise duty	1,20,000	
(iii) Depreciation	2,20,000	
(iv) Brokerage, commission, interest and rent, etc.	50,000	13,90,000
Business Profits		**25,20,000**
Add: Income from Other Sources: Brokerage/ commission, etc.		50,000
Aggregate Income		**25,70,000**
Less:		
(i) Brought forward losses (Sec. 72)	6,00,000	
(ii) Brought forward depreciation [Sec. 32(2)]	4,50,000	10,50,000
Gross Total Income		**15,20,000**
Less: Profit from industrial undertaking Sec. 80IB: 30% of ₹ 15,20,000 as included in GTI		4,56,000
Total Income		**10,64,000**

(b) Computation of Book Profits for the AY 2016-2017

Particulars	₹	₹
Net profits as per Profit & Loss A/c		32,40,000
Add : Expenses disallowed		
(i) Income tax	90,000	
(ii) Provision for unascertained liability	20,000	
(iii) Proposed dividend	3,00,000	
(iv) Loss of subsidiary	50,000	4,60,000
		37,00,000
Less : Allowable expenses and wrong credit in P & L A/c		
(i) Withdrawals from contingency reserve	4,00,000	
(ii) Brought forward business loss or depreciation whichever is less		
2011-2012 Depreciation	1,00,000	
2012-2013 Loss	2,00,000	7,00,000
Book-profits		**30,00,000**

(c) Computation of Tax Liability for the AY 2016-2017

Particulars	₹
(a) Tax on Total Income (including Education Cess and SHEC) = 30.9% of 10,64,000	3,28,776
(b) Tax on Book Profits (including Education Cess and SHEC) = 19.055% on 30,00,000	5,71,650
Tax payable [Higher of (a) & (b)]	**5,71,650**

Note :

(i) No adjustment is required for depreciation debited to Profit and Loss A/c because it is not on account of revaluation of any asset.

(ii) MAT credit available ₹ (5,71,650 – 3,28,776) = ₹ 2,42,874

(iii) Any penalty, interest, etc. paid under any of the direct tax laws or for infraction of any other laws and debited to Profit & Loss Account will be allowed and hence, need not be added back.

Illustration 99. Z Ltd is a qualifying shipping company which has got two qualifying ships during the Previous Year 2015-2016 :

Ship	Tonnage weight	No. of operational days
Ship A	37,949 tonnes and 990 kg	300 days
Ship B	25,550 tonnes and 275 kg	366 days

Compute its tonnage income under Tonnage Tax Scheme for the Assessment Year 2016-2017.

Solution:

Ship A	**Ship B**
(i) Tonnage consisting of kilograms is ignored. (ii) If such tonnage is not a multiple of 100 tonnes and the last two digits are less than 50, the tonnage is reduced to the previous lower tonnage which is a multiple of 100. (iii) Tonnage rounded off = 37,900 tonnes	(i) Tonnage consisting of kilograms is ignored. (ii) If such tonnage is not a multiple of 100, and last two degits are 50 or more, the tonnage is increased to next higher tonnage which is a multiple of 100 (iii) Tonnage rounded off = 25,600 tonnes

Income— computation under TTS		**Income— computation under TTS**	
Daily TI:	₹	**Daily TI:**	₹
First 1,000 tonnes (₹ 46 × 10)	460	First 1,000 tonnes (₹ 46 × 10)	460
Next 9,000 tonnes (₹ 35 × 90)	3,150	Next 9,000 tonnes (₹ 35 × 90)	3,150
Next 15,000 tonnes (₹ 28 × 150)	4,200	Next 15,000 tonnes (₹ 28 × 150)	4,200
Balance 12,900 tonnes (₹ 19 × 129)	2,451	Balance 600 tonnes (₹ 19 × 6)	114
Daily TI:	10,261	Daily TI:	7,924
Total TI for the Previous Year ₹ 10, 261 × 300	30,78,300	Total TI for the Previous Year ₹ 7,924 × 366	29,00,184

ILLUSTRATIONS ON MUTUAL ASSOCIATION

Illustration 100.

(a) Compute the taxable income of Chamber of Commerce from the following data:

	1 (₹)	2 (₹)	3 (₹)
Gross receipts for specified services rendered to members	2,00,000	2,00,000	2,00,000
Expenses incurred in connection with the above	50,000	1,00,000	1,50,000
Interest on bank deposits	40,000	40,000	60,000
Receipt from members	2,00,000	3,00,000	2,50,000
Expenditure incurred on members	1,40,000	4,50,000	2,60,000

(b) Will your answer be different if the above particulars are of a social club?

Solution:

(a) **Statement showing computation of taxable income:**

	1 (₹)	**2 (₹)**	**3 (₹)**
Net income from rendering specific services (Gross receipts – Expenses)	1,50,000	1,00,000	50,000
Less: Deficiency set off [maximum to the extent of 50% of total assessable income before set off of deficiency (as per notes)]	—	70,000	50,000
Business Income (A)	1,50,000	30,000	Nil
Interest on bank deposit under other heads	40,000	40,000	60,000
Less: Deficiency although allowable upto 50% of total assessable income which could not be set off against business income	—	—	5,000
Other Income (B)	40,000	40,000	55,000
Gross Total Income (A)+(B)	1,90,000	70,000	55,000
Less: Deduction u/s 80C to 80U	Nil	Nil	Nil
Total Income	1,90,000	70,000	55,000

Note 1: Surplus of ₹ 60,000 under case 1 is not taxable as it is from mutual activity.

Note 2: Deficiency under case 2 and 3 wolud not allowed but for the benefit given u/s 44A.

Note 3:

	Case 2 (₹)	Case 3 (₹)
Surplus from specified services	1,00,000	50,000
Interest income	40,000	60,000
	1,40,000	1,10,000
Less: Deduction u/s 80C to 80U	Nil	Nil
	1,40,000	1,10,000

Note 4: In case 3, 50% of the assessable income is ₹ 55,000 (i.e. 50% of ₹1,10,000) but it will be set off from business income which in this case is ₹50,000 and the balance shall be set off from the other income.

(b) In the case of social club neither surplus from members nor surplus on account of specific services rendered to it members is taxable. Further, if there is any deficiency from mutual activity, it cannot be set off as provisions of section 44A are applicable only in case of trade, professional or similar association.

Therefore, income of a club will be calculated as under:

	1(₹)	2 (₹)	3 (₹)
Receipt from members	2,00,000	3,00,000	2,50,000
Gross receipts for specified services rendered to members	2,00,000	2,00,000	2,00,000
	4,00,000	5,00,000	4,50,000
Less: Expenses	1,90,000	5,50,000	4,10,000
Surplus/ (Deficiency)	2,10,000	(50,000)	40,000

The above surplus is exempt and deficiency is not allowed to be set off.

	1 (₹)	2 (₹)	3 (₹)
Interest on bank deposits	40,000	40,000	60,000
Gross Total Income	40,000	40,000	60,000
Less: Deduction	Nil	Nil	Nil
	40,000	40,000	60,000

Illustration 101. Whether the transfer fee realised by a co-operative society from its members when the members intended to transfer the flats to any other person, member or otherwise, is liable to tax under section 4 of the Income Tax Act?

Solution:

The transfer fee is not liable to tax provided the co-operative society does not carry on any business, and the transfer fee is meant for the benefit of the members of the co-operative society [CIT vs. Apsara Co-operative Housing Society Ltd., (1993) 204 ITR 662 (Cal)].

Illustration 102. Whether 'Gurudakshina' received from the members is liable to tax under section 4 of the Income Tax Act?

Solution:

No. The 'Gurudakshina' is exempt on ground of mutuality.

Illustration 103. A co-operative society bought text books at a discount from the Government and sold them at profit to various persons including its members. The society claimed that the profit earned by the sales to its members was not taxable on ground of mutuality. Whether the claim of the society is in order?

Solution:

The participators in the profit are members; but the contributors to such profit are non-members who are the buyers of the books. There is no identity between the contributors and the participants. Therefore, the profits derived from the sales to the members is not exempt but taxable [Bihar Rajya Sikshak Sahyog Sangh Ltd. vs. CIT (1987) 165 ITR 681 (Pat.)].

Illustration 104. Whether the principle of mutuality is applicable to income from rent received from house property?

Solution:

The principle may not apply where the use of residential accommodation is not confined to members. In such cases, the rent is taxable under the head 'Income from house property'. Even if the income is treated as business income, it would not be exempt, because only some of the members occupy the accommodation, and there is no identity between the contributors and the participants.

In the case of the Presidency Club Ltd. vs. CIT (1981) 127 ITR 264 (Mad.), the Madras High Court accepted the claim for exemption on the basis of mutuality, where the guests of members were allowed the use of the premises. In the case of CIT vs. Bankipur Club Ltd. (1992) 198 ITR 261 (Pat.) (FB) now confirmed by the Supreme Court in CIT vs. Bankipur Club Ltd. (1997) 226 ITR 97 (SC), where the income from the guest houses was received from the members of the club for their use and the use of their guests, principle of mutuality was accepted.

Illustration 105. Can a company registered under section 8 of the Companies Act claim exemption on basis of mutuality?

Solution:

There is no reason why a mutual organisation formed as a company should not be treated as a mutual association. This view was reiterated recently in CIT vs. Cement Allocation and Coordinating Organisation (1999) 236 ITR 553 (Bom.) following its own decision in CIT vs. Bombay Oilseeds and Oil Exchange Ltd. (1993) 202 ITR 198 (Bom.) and CIT vs. Bankipur Club Ltd. (1197) 226 ITR 97 (SC).

Illustration 106. Can a mutual association claim to be a charitable organisation?

Solution:

If the object is charitable, a mutual association like a trade association can claim exemption under section 11 as was successfully claimed in CIT vs. Andhra Chamber of Commerce (1965) 55 ITR 722 (SC) where the surplus was to use only for public benefit and not to be distributed to its members. If the surplus is to be shared between members, it could claim exemption on grounds of mutuality, if other conditions like participants and contributors are both members with no dealings with outsiders.

Illustration 107. A union of truck owners was registered as a trade union formed for the purpose of promoting relationship between truck operators and the employees and for promoting feeling of co-operation among the truck operators themselves. Should such union be eligible for exemption on the principle of mutuality?

Solution:

Since the activity is not confined to the members as it is intended to promote relationship between workmen, and workmen and the truck operators, mutuality principle can have no application. Under Indian Trade Unions Act, 1926, when such workers are not members, there is no principle of mutuality, and hence tax cannot be avoided [Sumerpur Truck Operators Union vs. ITO (2003) 259 ITR 749 (Raj.).

Illustration 108. Can a Nidhi company registered under section 406 of the Companies Act, 2013, be a mutual society, immune from application of section 269SS barring deposits in cash above the specified limit?

Solution:

A Nidhi company is also a mutual association recognised under section 406 of tie Companies Act, 2013. Hence, any transactions as between such company and members should be treated as with self on principle of mutuality, so that sections 269SS and 269T should have no application. It has been so held by the Tribunal [Muslim Urban Co-operative Credit Society Ltd. vs. Jt. CIT (2005) 96 ITD 83 (Pune)].

Illustration 109. Does mutuality get lost, if a mutual association has different classes of members with different corresponding rights?

Solution:

Principle of mutuality does not get destroyed merely because a club has different classes of members with different rights with entrance fees and subscriptions being different for each such class depending upon their rights to participation in the affairs of the club with some classes of membership not having right to vote. The assessee in this case was held entitled to exemption [CIT vs. Willingdon Sports Club (2008) 302 ITR 279 (Bom)].

9.11 DIFFERENT ASPECTS OF DIRECT TAX PLANNING

Introduction:

The provisions of the Income-Tax are contained in the Income-Tax Act, 1961 (the Act), which extends to whole of India and is operative from the 1st day of April, 1962(the Rules). The Act provides for determination of taxable income, Tax liability, procedures for assessment, appeals, penalties, interest levies, the tax payment schedules and its determination, refunds and prosecutions.

Depending upon Government polices certain income is exempted from tax, for example SEZ (Special Economic Zone) units income, Agriculture income, etc. and deduction are also provided on fulfillment of prescribed criteria. Provisions relating to such exemptions and deduction are also contained in the Act.

Corporate form of business is much in vogue. Therefore, certain taxes specific to companies like Tax on Book profit (115JB), tax on Dividend Distributed (115O), are levied.

At times in Cross border transactions income earned get exposed to tax in India as well as in some other countries. Provisions for upholding relief from double taxation are also made in the Income Tax Act.

The Act also lays down the powers duties of various income-tax authorities. Being revenue legislation, the act is amended once a year through union budgets and the finance bill is normally presented to the Parliament for approval around February. The Act has empowered the Central Board of Direct Taxes (CBDT) to frame the rules and these rules are implemented after necessary Gazette notifications. The CBDT also issues circulars and clarifications from time to time for implementation by the income-tax authorities by virtue of section 119, which gives such rule making powers to the CBDT. It is impracticable for the Act to provide exhaustively for everything relating to limits, conditions, procedures, forms and various other aspects. Therefore this power has been delegated to CBDT and thus periodical changes and modification by an executive authority is facilitated. The power to frame rules is vested with the Board u/s 295 of the Act and the word 'prescribed' used in section 2(33) means what is prescribed by rules made under the Act.

The Income-Tax Act gives definitions of the various terms expressions used in the Act. Unless the context otherwise requires, these definition should be applied. The words 'means' 'includes' and 'means and includes' are used in these definitions and the significance of these terms needs to be understood. When a definition uses the word 'means' the definition is self-explanatory, restrictive and in a sense exhaustive. It implies that the term or expression so defined means only as to what is defines as and nothing else. For example, the terms 'agricultural income' 'assessment year ' 'capital asset', are exhaustively defined. When the legislature wants to widen the scope of a term or expression and where an exhaustive definition cannot be provided, it uses the word 'includes' in the definition. Generally an inclusive definition provides an illustrative meaning and the definition could include what is not specifically mentioned in the definition so long as the stipulated criteria are satisfied. To illustrate refer to the definitions of 'income', 'person', 'transfer ' in the Act. When the legislature intends to define a term or expression to mean something and also intends to specify certain items to be included, other the words ' means' as well as ' includes' are used. Such definition is not only exhaustive but also illustrative in specifying what is intended to be included. Sometimes specific items are included in an exhaustive definition in order to avoid ambiguity and to provide clarity. Please refer to definitions of 'assessee', 'Indian company','recognised provident fund', under the Act.

Further any decision given by the Supreme Court also becomes a law on the subject and will be binding on all the courts, tribunals, income-tax authorities as well as the taxpayers. In case of apparent contradictions in the Supreme Court rulings, the following rules may have to be followed:-

1. The decision of the larger bench would prevail.
2. The principle of the later decision shall prevail, where the decisions are by equal number if judges. Decisions given by High Courts are binding on all taxpayers and It authorities, which fall under its jurisdiction till it is overruled by higher authority.

Tax Planning vs. Tax Evasion

The word 'tax planning' connotes the exercise carried out by the taxpayer to meet his tax obligations in proper, systematic and orderly manner availing all permissible exemptions, deductions and reliefs available under the statute as may be applicable to his case. To illustrate, assessee software company setting up assessee software technology park in assessee notified area to avail benefits of section 10A of the Act is assessee legally allowable course. Planning does not necessarily mean reduction in tax liability but is also aimed at avoiding controversies and consequential litigations.

Every taxpayer is expected to voluntarily make disclosures of his incomes and tax liabilities through legal compliance. When a tax payer deliberately or consciously do not furnish material particulars or furnishes inaccurate or false particulars or defrauds the State by violating any of the legal provisions, it shall be termed as 'tax evasion'. It is also illegal, but also unethical and immoral. Inflation of expenditure, suppuration of income, recording of fictitious transactions, claiming deductions wrongly are few examples.

Benjamin Franklin is credited with this classical statement: There are two certainties in this world – death and taxes. This makes all tax payers in general, and the companies in particular, realize the bitterness or hardship of taxes. Three methods of saving taxes have been developed in most countries of the world in the past few decades: tax evasion, tax avoidance and tax planning. A great deal of confusion prevails in corporate sector about correct connotations of these terms. Hence, we shall attempt to explain these terms to show tax planning is absolutely legal. The expression 'Tax Evasion' means illegally hiding income or concealing the particulars of income or concealing the particular source or sources of income or in manipulating the accounts so as to inflate the expenditure and other outgoings with a view to illegally reduce the burden of taxation. Hence, tax evasion is illegal and unethical. It is uneconomical as well. It deserves to be deprecated not only by the Government but by the companies as well. The next expression is 'Tax avoidance' which is assessee art of dodging taxes without breaking the law. In my opinion, tax avoidance means traveling within framework of the law or acting as per language of the law only in form, but murdering the very spirit of the law and defeating the purpose of the particular legal enactment. If, by adopting an artifice or device against the intension of the legislature but apparently on the face of it acting within the framework of the law, a company is able to dodge income tax, it would be a clear case of tax avoidance. In contrast, 'Tax Planning' takes maximum advantages of the exemptions, deductions, rebates, reliefs, and other tax concessions allowed by taxation statutes, leading to the reduction of the tax liability of the tax payer. Tax planning has been contrasted with the expression tax avoidance and has the legal sanction of the Supreme Court as well. In recent years the sentiments in favour of tax avoidance have changed and the courts view tax avoidance with displeasure. For example, Lord Summer in IRC vs. Fisher 's Executors AC 395, 412 had earlier as per the ratio of Westminister 's case said:

"My Lords, the highest authorities have always recognized that the subject is entitled so to arrange his affairs as not to attract taxes imposed by the Crown, so far as he can do so with the law, and that he may legitimately claim the advantage of any express terms or any omissions that he could find in this favour in taxing Acts. In so doing, he neither comes under liability nor incurs blame."

The significance of Ramsay as assessee turning point in the interpretation of tax laws in England and the departure from the principle of Westminister 's case were explained in TRC vs. Burmah Oil Co. Ltd., STC 30 where Lord Diplok said:

"It would be disingenuous to suggest and dangerous on the part of those who advise on elaborate tax-avoidance scheme to assume, that Ramsay's case did not mark assessee significant change in the approach adopted by this House its judicial role to assessee pre-ordained series of transactions into which they were inserted steps that have no commercial purpose apart from the avoidance of tax liability, which in the absence of those particular steps would have been payable. The difference is in approach."

Commenting on this judgment the Supreme Court of India in the McDowell Co. Ltd., vs. CTO 154 ITR 148(SC) said:

"It is neither fair nor desirable to except the legislature to intervene and take care of every device and scheme to avoid taxation, it is up to the court to determine the nature of new and sophisticated legal devices to avoid tax and consider whether the situation created by the devices for what they really are and to refuse to give judicial benediction."

In the same judgment, Supreme Court Judges made a clear distinction between tax avoidance and tax planning. This is what the judges of the Supreme Court have said in the same case:

"Tax Planning may be legitimate provided it is within the framework of law. Colorable devises cannot be part of tax planning and it is wrong to encourage or entertain the belief that it is honorable to avoid the payment of tax by resorting to dubious methods. It is the obligation of every citizen to pay the taxes honestly without resorting to subterfuges."

Form the above it is very clear that tax planning by Assessee Company cannot be called a crime or an illegal activity or an immoral action as is wrongly considered by confused thinkers on the subject. What constitutes a crime is tax evasion and what is undesirable is tax avoidance but it is certainly desirable to engage in the exercise of tax planning.

In UK, wherefrom the principal coined in McDowell's case was coined, the House of Lords expressly reaffirmed the basic principle, 'A subject is entitled to arrange his affairs so as to reduce his liability to tax. The fact that the motive for a transaction may be to avoid tax does not invalidate it unless a particular enactment so provides'.

The House of Lords expressly reaffirmed the cardinal principle of *Duke of Westminister,* 'Given that a document or transaction is genuine, the Court cannot go behind it to some supposed underlying substance'. They only ruled against the principle being overstated or overextended.

Mukharji J, who in his prompt and lethal report in CWT vs. Arvind Narottam said: '…no amount of moral sermons would change people's attitude towards tax avoidance', and soon thereafter in UoI v Playworld Electronics stated: 'one should avoid subverting the rule of law'. As a matter of law, the Supreme Court in these two latter cases reiterated that where the true effect of a transaction is clear, the appeal to discourage tax avoidance is not a relevant consideration.

In any event, when the language of a deed of settlement is clear, an attempt to invoke McDowell would be futile even if the deed results in tax avoidance. as the Madras High Court held in Valliapan vs. ITO, McDowell does not hit tax planning.

The manner in which McDowell is to be dealt with was well summed up by the Gujarat High Court in Banyan and Berry vs. CIT thus:

The court (in McDowell) nowhere said that every action or inaction on the part of the taxpayer which results in reduction of the tax liability to which he may be subjected in future, is to be viewed with suspicion and be treated as a device for avoidance of tax irrespective of legitimacy or genuineness of the act…. The principle enunciated in the above case has not affected the freedom of the citizen to the act in a manner according to his requirements, his wishes in the manner to do any trade, activity or planning his affairs with circumspection, within the framework of law, unless the same falls in the category of colourable device.

The House concluded that steps which had no commercial purpose and had been artificially inserted for tax purposes into a composite transaction, should be disregarded; but that a transaction which came into statutory language could not be disregarded merely because it was entered into solely for tax purposes.

Therefore, while tax planning these principles emanating from court made law need to be kept in sight. Otherwise, planning looking good on paper may fail in practice.

Tax Management

Planning which leads to filing of various returns on time, compliance of the applicable provisions of law and avoiding of levy of interest and penalties can be termed as efficient tax management. In short, it is an exercise by which defaults are avoided and legal compliance is secured. Through proper tax planning and management, the penalty of upto ₹100000 for delay in furnishing of tax audit reports u/s 44AB can be avoided.

Similarly by applying for Permanent Account Number (PAN), the penalty under the Act can be avoided. The borrowal of loan otherwise than by way of an account payee cheque or bank draft attracts 100% penalty and this can be avoided by conscious planning of the execution of loan transactions. Planning is a perception conceived on legitimate grounds and achieved through genuine transactions within the framework of law e.g. contribution to Public Provident Fund and claiming rebate u/s 88 of the Act. The filing of the returns with all proper documentary evidence for the various claims, rebates, reliefs, deductions, income computations and tax liability calculations would also be termed as tax management.

Tax management is also an important aspect of tax planning. Assessee is exposed to certain unpleasant consequences if obligations cast under the tax laws are not duly discharged. Such consequences take shape of levy of interest, penalty, prosecution, forfeiture of certain rights, etc.

Therefore, any effort in tax planning is incomplete unless proper discharge of responsibilities is not made.

Tax management includes:

1. Compiling and preserving data and supporting documents evidencing transactions, claims, etc.
2. Making timely payment of taxes e.g. advance tax, self assessment tax, etc.
3. TDS and TCS compliance
4. Following procedural requirements e.g. payment of expenses or acceptance of loans or repayment thereof, over ₹ 20,000 by account payee bank cheque or bank draft, etc.
5. Compliance with the prescribed requirements like tax audit, certification of international transactions, etc.
6. Timely filing of returns, statements, etc.
7. Responding to notices received from the authorities.
8. Preserving record for the prescribed number of years.
9. Mentioning PAN, TAN, etc. at appropriate places.
10. Responding to requests for balance confirmation from the other assessees.

Tax Implications in Planning

The main objectives in any exercise on tax planning are to :—

1. Avail all concessions and relief 's and rebates permissible under the Act.
2. Arrange the affairs in a commercial way to minimize the incidence of tax.
3. Claim maximum relief where taxes are paid in more than one country.
4. Become tax compliant and avoid penalties, prosecutions and interest payments.
5. Fruitful investment of savings.
6. Timely compliance of procedural requirements like tax audit, TDS, TCS, etc.
7. Appropriate record keeping
8. Avoidance of litigation.
9. Growth of economy and its stability.
10. Pay taxes – not a penny more, not a penny less.

E-Commerce and Taxation:

In the era of e-commerce, the determination of the place of source with reference to an item of income may quite often pose difficulty. The source-based taxation of business income depends on physical presence in the form of fixed place of business or a dependent agent in the source country. With e-commerce the need for physical presence virtually ceases. The change in mode of delivery from physical to online raises characterization issues and the lack of physical presence also creates problems in enforcement of tax laws. Therefore the long- term solution of the problems created by characterization lies in making direct taxation identical for all streams of income in a manner aimed at ensuring equitable sharing of revenues between residence country and source country. The following rulings by the Authority for Advanced Ruling may be worth remembering in this context:

1. A company incorporated in Mauritius for sale and distribution of television channels enters into an agreement with an Indian company where under the latter would solicit orders from purchasers of airtime and pass on those orders to the former. The business profits earned by the Mauritian company through Indian company are profits deemed to accrue or arise in India u/s 9 of the Act. However by virtue of Article 7 of the DTAA between India and Mauritius, they are not liable to be taxed in India, if: a) The liability of the Mauritian company to pay tax in Mauritius was established and b) The Mauritian company and not the Indian company is shown to exercise generally the power to conclude the advertisement contract for sale of airtime - P No. 296 of 1996 TVM vs. CIT 237 ITR 230 (AAR).

2. An American company is engaged in providing international credit cards, travelers cheques and travel related services. It has Central Processing Unit (CPU) in USA and Consolidated Data Network (CDN) in Hong Kong. Indian company is given access to the CPU through CDN for the reporting and processing of information on travel by customers in India. Charges for the use of CPU and CDN of American company paid by Indian company is royalty for the case of 'design or model, plan secret formula and process' and therefore taxable in India under Article 12(3)(a) of DTAA between India and USA – p. no. 30 of 1999 238 ITR 296 (AAR).

3. Where there is a PE for a non resident income attributable to such PE is chargeable to tax in the country in which such PE exist – p. no.28 of 1999 242 ITR 208 (AAR). A foreign company having a fixed office will be constructed to have a PE-p. no.13 of 1995 228 ITR 487 (AAR).

Strategic Management Decisions – Tax Implications

In business, the decisions are taken with a view of optimize returns to the stakeholders. A dominant aspect to be considered taking in view the tax consequences of the same on the bottom-line so as to share minimum profits with Government without violating any tax or any other laws in force. It is significant that tax consequences alone need not bind the management to take a decision and it is only a factor which influences the management decisions.

Moreover, in case of taxes, there are both direct as well as indirect taxes and in efforts for planning implications of both category of taxes are required to be considered.

Management decisions, which have a bearing on the bottom line are analyzed below from the point of view of income-tax implications.

(a) Make or Buy
(b) Own or Lease
(c) Retain or Replace
(d) Repair/Scrap or Return
(e) Export or Domestic Sale
(f) Shut Down or Continue
(g) Expand or Contract
(h) Demerger
(i) New Capital Investments
(j) Accounting Standards for Taxes on Income

CASELETS ON TAX MANAGEMENT AND PLANNING

(a) Capital Structure

Before setting up a new project, an important decision about the type of capital structure has to be taken. While selecting a particular capital structure, the entrepreneur has to keep in view the following considerations:

(i) Serving the capital base with consistent dividend policy

(ii) Cost of capital to be raised from the market

(iii) Chargeability or otherwise of taxes, i.e., direct and indirect taxes

(iv) Keeping a margin for ploughing back of profits for future plan towards diversification, expansion, modernisation and other development aspects.

Generally, the following means of finance are available for a new project:

(i) Equity share capital, (ii) Debentures/Loans and borrowings/Lease Finance.

In making capital structure decision, financial leverage plays an important role. The financial leverage states the percentage increase in earning before taxes corresponding to percentage increase in earning before interest and taxes. This can be explained with the help of following example:

Earning before interest and taxes (EBIT)	₹2,000
Less: Interest on securities	₹1,000
Earning before taxes (EBT)	₹1,000
Financial leverage (2,000/1,000)	2

Here, this financial leverage states that any increase in earning before interest and taxes will have two fold increase in earning before taxes. So if EBIT is ₹3,000 then EBT will be—

Earning before interest and taxes (EBIT)	₹3,000
Less: Interest on securities	₹1,000
Earning before taxes (EBT)	₹2,000

Hence, it is clear that 50% increase in EBIT has resulted 100% increase in EBT, Therefore, a high financial leverage would result in a very high return when there is high profitability. But in case of depression, this may prove to be dangerous because the residual net income available to shareholders may reduce to a great extent and sometimes may convert in losses. How much financial leverage is safe is considered with reference to the likely fluctuation in the operating profits and the debt equity mix.

A capital structure is said to be optimum when it has a mix of debt and equity that will yield the lowest weighted average cost of capital. At the same time, a capital mix should not have high debt equity ratio. A high debt/equity ratio has its own advantages and disadvantages.

(b) Lease or buy decisions: In recent years, leasing has become a popular source of financing in India. From the lessees point of view, leasing has the attraction of eliminating immediate cash outflow, and the lease rentals can be claimed as admissible expenditure against the business income. On the other hand, buying has the advantages of depreciation allowance and interest on borrowed capital being tax-deductible. Thus, an evaluation of the two alternatives is to be made in order to take a decision.

However, before opting for a lease decision one has to keep in mind the following disadvantages:

(i) Leased assets are not owned assets and therefore, the asset cover to equity comes down due to increased dependence on lease finance.

(ii) Financial ratios are also distorted due to greater dependence on lease finance.

(iii) Lease rent payments are made out of working capital funds which mean that fixed assets are financed out of short-term funds.

(iv) The asset taken on lease is taken back by the lessor at the expiry of lease period. Thus, he will be bothered about finding alternative asset at the expiry of lease period.

(c) Make or buy decision: The leasing or buying decision is taken only when it is finalised that a particular asset is to be acquired. In most of the industries, the conception of establishing a new project itself involves acquisition of fixed assets. In assembling industry different components are assembled to make a product. Now a decision regarding the manufacturing of these components is to be taken. It is decided whether the product/part/component of product should be bought from the market or should be manufactured by having necessary manufacturing facilities. The main consideration affecting such a decision is cost. In a make or buy decision, the variable cost of making the product or part/component of product is compared with its purchase price prevailing in the market.

In this decision making process, it may be possible that the decision to manufacture does not result in increasing the fixed cost, and the existing manufacturing facilities cannot otherwise be utilised profitably. Thus, where no fixed costs are incurred for producing the product or component, the main criterion is that it would be more profitable to manufacture than to purchase, if the variable cost is lower than the purchase price.

For example, if a particular component can be acquired at a cost of ₹40 from the market then it will be profitable for the project to produce that component if the variable cost is below ₹40. Here it is assumed that no extra fixed costs are to be incurred on the manufacturing of these components.

However, where the component manufacturing involves additional fixed expenditure, purchase of any plant and machinery or establishment of a new separate unit, then total cost will have to be considered. In such special situations the following tax consideration must be kept in mind:

(1) **Where the manufacturing of the product requires additional fixed cost also:** In this case, as the assessee will have to incur the additional fixed cost it will form part of the cost of manufacturing of the product.

(2) **Where the manufacturing of the product requires establishment of a new unit:** In this case, although, there will be cash outflow for establishing a new unit, but the tax incentives shall be as under:—

   (i) Exemption under section 10AA: The unit of an entrepreneur, which begins to manufacture or produce any article or thing or provide any service in a special economic zone on or after 1.4.2005, shall be allowed a deduction of 100% the profits and gains derived from the export, of such articles or things or from services for a period of 5 consecutive assessment years beginning with the assessment year relevant to the previous year in which the Unit begins to manufacture or produce such articles or things or provide services, as the case may be, and 50% of such profits and gains for further 5 assessment years. Besides this, a further deduction for next 5 consecutive assessment years beyond the period of 10 assessment years mentioned above shall be allowed if certain conditions are satisfied.

   (ii) Depreciation under section 32: Since a new unit will be established, it will acquire building, plant and machinery, furniture and certain intangible assets, the assessee, in this case, shall be eligible for depreciation on such assets.

   (iii) Deduction of Interest on money borrowed for acquisition of such capital assets: If the money is borrowed for the acquisition of above capital assets, the assessee will be eligible to claim interest as deduction.

(3) **If the facilities for production are existing and the assessee wishes to discontinue the manufacturing of such product:** It is possible that buying of such product is cheaper than manufacturing and if it is to be continued for a very long time, the assessee may have to sell the existing plant and

machinery etc. In this case, there will be short term capital gain/loss if the entire block of assets is sold or there will be short term capital gain if the part of the block is sold for a price more than the W.D.V. of the block.

(d) Repair/Renewal or Replacement of an asset: The old and worn out assets need to be either repaired/ renewed or replaced at regular intervals. Sometimes, even a good machine requires up gradation or replacement so as to compete in the market. The main tax consideration in these cases shall be whether the assessee, while computing his business income, shall be allowed deduction on account of such expenditure or not.

Repairs/Renewal: Deduction for expenditure on repairs/renewal will be allowed as revenue expenditure in computation of business income as under:—

If the building is a rented building, any expenditure on repairs shall be allowed as deduction. On the other hand, if the building is owned, only current repairs shall be allowed as deduction.

As regards plant & machinery, only current repairs shall be allowed as deduction.

However : the accumulated repairs in the above cases can be claimed under section 37(1).

It may be noted that if the repairs expenditure are of capital nature it shall not be allowed as deduction either under section 30, 31 or 37.

Replacement of assets: If the asset has to be replaced, the expenditure incurred on replacement shall be capital expenditure and the assessee shall only be entitled to depreciation on such assets and as such, the entire expenditure cannot be claimed as deduction which was allowed in case of repairs. The capital expenditure incurred on construction of super structure on rented building is also eligible for depreciation under section 32.

Tax planning in case of employee's remuneration

This requires consideration from the point of view of—

(1) Employer : While calculating the business income of the employer, the remuneration payable to the employee, in whatever form, should be fully deductible otherwise the employer will have to pay tax on such remuneration also as the same will not be allowed as deduction while computing his business income.

(2) Employee: The salary received by the employee, whether in cash or kind, should attract minimum income tax liability. He should be in a position to avail maximum exemption / concession in respect of such salary received by him. Some of the exemptions / concessions available to employee under Income Tax Act are as under:

   (i) Section 10(10) exemption in case of death-cum-retirement gratuity.

   (ii) Section 10(10A) exemption of commuted pension.

   (iii) Section 10(10B) exemption of retrenchment compensation.

   (iv) Section 10(10C) exemption of compensation on voluntary retirement.

   (v) Section 10(13A) exemption of House Rent Allowance.

   (vi) Section 10(14) exemption of specified/notified special allowance.

   (vii) Tax free perquisites, like medical facility, reimbursement of medical expenses, telephone at the residence of employee, free lunch or dinner / free refreshment, leave travel concession, etc.

   (viii) Contribution by the employer to the provident fund or other welfare fund of the employee.

   (ix) Perquisites taxable at concessional rate, like rent free accommodation, motorcar, etc.

TAX PLANNING-AN OVERVIEW

Q.1. Why is tax planning necessary?

Answer.

The tax paid is an addition to the cost. Just as every businessman tries to maximise his profit by reducing the cost, he should also arrange his affairs in such a way, that he pays the least amount of tax. This however should be done within the four corners of law and there should be no element of fraud in it.

Q. 2. Is tax planning confined only to direct taxes?

Answer.

No. The effect of other taxes like sales-tax, customs duty and excise duty, are to be taken into account. It is a dynamic concept and the decision once taken is not valid for all times and requires continuous reappraisal.

Q.3. Is tax planning harmful?

Answer.

Tax planning is not harmful. The tax saved can always be recycled in business and not necessarily wasted in conspicuous personal expenditure. The idea behind grant of incentives is to stimulate economy and hence there should be proper planning to make use of these incentives.

Q. 4. When should planning be done?

Answer.

Planning has to be done before the income accrues or arises, i.e., at the source itself. Planning done after receipt of income is only diversion of income and may even lead to an inference of fraud.

Q. 5. What are the factors to be taken in tax planning?

Answer.

The choice of taxable entity and other choice like time and place have all are common instances. Time is relevant for fixing the year of accrual. Place is relevant for fixing the residential status. The status in which the income is to be assessed, i.e., individuals, HUF firm or AOP or company is also to be considered.

Q. 6. Has tax planning any effect on the rate of tax?

Answer.

Yes. As dispersal of income over different taxable entities, slab rate can be reduced .

Q. 7. What is the difference between dispersal and diversion of income?

Answer.

Dispersal ensures that income accrues separately in different hands. Diversion is said to take place when money is siphoned off to other hands after accrual in one hand. The decision of the *Supreme Court in CIT* vs. *Sitaldas Thirakhdas* is as to what constitutes diversion as distinct from dispersal. In this case, an amount of annuity decreed by the court to be paid by son to his mother in view of his obligation was held to be dispersal, i.e., diversion by overriding title, so that he was entitled to reduce such payment from his taxable income. While diversion by overriding title will amount to dispersal, any other diversion without title at source is a mere application of income. The decision of Supreme Court in *CIT* vs. *Thakar Das Bhargava* illustrates the principle of application of income, which does not help, where a lawyer who had assigned his right to fees to a charitable institution and had not received the same was still held liable to pay tax on such fees.

Q. 8. Does tax planning include compliance within law?

Answer.

Certainly. Timely filing of returns, payment of advance tax, finally tax deduction at source, etc., are all important to avoid penal interest, penalty, prosecution, etc.

Q. 9. Is method of accounting important?

Answer.

Yes. It is because income for tax purposes is one which is ascertained on the basis of what is computed under ordinary principles of commercial accounting subject only to such adjustments as are specifically required by the statute.

Q.10. What is the caution necessary in tax planning?

Answer.

Tax planning may be legitimate provided it is within the law. But colorable devices are not only dishonorable but should not be recognized by the Assessing Officer. One such device is to avoid tax though not prohibited by the statute. It is not necessary that there should be a specific disapproval of every device or scheme. If they are artificial, they are prone to be rejected. What is to be noted is that the device should be genuine in that the income really goes to the person to whom it is intended and does not come back or held effectively by the devisor of the scheme.

Though the decision of the Supreme Court in *Union of India* vs. *Azadi Bachao Andolan* has granted great recognition to tax planning, the warning against artificial transactions lacking in commercial credibility in *McDowell's case* is still valid.

The concessional treatment for Short-term Capital Gains is available on such gains under section 111A. It may, however, be noticed that these concessions are available only where the transactions are on capital account and not where the shares are held as stock-in-trade.

TAX PLANNING-AVAILABLE AREAS

Q. 1. How to choose the most suitable form of organisation for tax planning?

Answer.

It depends on the rate of tax applicable to the organisation, business needs, risk of non-observation of formalities, ability to raise finance, etc.

Q. 2. In what way, does the choice of head of income affect tax?

Answer.

Actually assessment under different heads has diverse results as regards deduction and taxability. An asset, if it is property, gets a lump sum deduction at one fourth of annual value and as a business asset it gets depreciation on cost. On sale long term capital gains arises in former case and Short Term Capital Gains in latter.

Q. 3. How to select a location for business?

Answer.

Deficiencies in infrastructure have to be balanced against the tax incentives. Excise duty and Sales-tax implications may also prove to be of greater importance.

Q. 4. What is the impact of the size of the business?

Answer.

Small units gets some concession from State authorities. Dispersal amongst separate subsidiaries will give relief under certain sections.

Q. 5. Can accounting method have an impact on tax?

Answer.

Yes. At present, only two methods mercantile and cash are available. For professionals and money lenders cash system is preferred. Also accounting practices to reflect the correct amount of income have to be adopted so that there is no overload in some years and deficiency in others. Inventory valuation is another area of accounting, which has impact on tax. But it should also be borne in mind that where the statute itself determines the income, accounting method has no relevance.

Q. 6. In what way capital can be restructured for maximum benefit?

Answer.

A balance between own and borrowed capital has to be achieved. When own capital is more there will be larger taxable profits and poorer after-tax return. With more borrowed capital, taxable profits are less but after-tax return on own investment is better. There should be a continuous appraisal in this behalf.

Q. 7. What is the best investment?

Answer.

Choice of investment depends on the expectations of the investors. Risky investments may involve larger profit or loss. Safe investments give a lesser but steady return. Period of holding depends upon varying needs of liquidity for the investors. As between investment in shares, deposits and debentures in companies, dividends have an edge because these are not taxed in the hand of the receiver. Interest is fully taxed subject to certain deductions.

Q. 8. What should be the consideration regarding investment in plant and machinery?

Answer.

Depreciation is a significant deduction from taxable income. Plant and machinery relating to generation of power and pollution control equipment, and those relating to Research and Development, etc., are eligible for 100% deduction. Plant and machinery can be acquired, replaced, repaired, purchased or hired or assembled with different tax consequences.

There has been drastic reduction in rates of depreciation effective from assessment year 2006-07.

Q. 9. Is there any restriction in method of valuing stock?

Answer.

Accountancy text books give various methods like: cost, market value, cost or market value whichever is less, FIFO, LIFO, etc. Some value obsolete or slow-moving stocks at lesser cost. At any rate the method adopted should be regular and should not distort the profits inviting rejection of accounts.

Q. 10. Is transfer pricing important?

Answer.

Transfer pricing is important in reckoning of reliefs as well as in matters of non-resident taxation. Adoption of correct transfer pricing is a matter of concern for Revenue, but it should be equally a matter of concern for taxpayer lest the method adopted loses for himself the benefit which is otherwise available. This is all the more important in international transactions. Sections 92 to 92F may be seen.

Q. 11. What is the importance of dividend policy?

Answer.

Dividend policy determines liquidity, possible impact as price of shares, credit rating, borrowing capacity, shareholder satisfaction, etc., which are matters of business policy. It also affects shareholders' tax liability. It is of importance in closely held companies particularly because even loans to substantial shareholders are treated as deemed dividends under section 2(22)(e) of the I.T. Act.

Q. 12. What are the factors to be borne in foreign collaborations?

Answer.

The degree of participation of the foreign concern in Indian business, the extent of investment, duration of physical presence in India, the manner in which such participation is expected, whether by way of equity, loan, royalty, technical fees, etc., would decide liability. For the Indian partner the question whether payments made will be allowed as a deduction will be relevant. Double taxation agreements and where there is none section 91 of Income tax Act will also have relevance. The new provision introduced by Finance Act, 2001 in respect of transfer pricing in sections 92 to 92F w.e.f. 1.4.2002 would require consideration in matters of taxation of business income of non-residents.

Q. 13. Can an employee benefit from tax planning?

Answer. There is large scope for tax benefit for employees. This is done by designing a pay package taking into consideration tax-free and concessional perquisites in a manner that take-home pay is maximum. Minimisation of tax incidence in otherwords an important objective of tax planning. There are certain allowances that are exempted. An employee should make a wise choise between perquisits and allowances and go for the one which is most beneficial for him or her.

TAX PLANNING-FOR INCOME FROM HOUSE PROPERTY

Q. 1. How is income to be computed, if a property is partly let out and partly self-occupied?

Answer.

It has to be treated as two residential units and income from each unit has to be computed according to law by allocating common outgoings on a basis proportionate to area of occupation.

Q. 2. Is it necessary that the person must be a legal owner in order that the income should be computed under the head "income from property"?

Answer.

No. If a person is entitled to the income under the law, such income is bound to be assessed under the head "income from property". Tax laws are generally concerned with beneficial ownership as laid down in *CIT* vs. *Podar Cement Pvt. Ltd.*

Q.3. Is municipal tax deductible in computation of income from: (i) self-occupied property; and (ii) where demand notice is reserved but it has not been paid?

Answer.

Since income from one self-occupied property is nil, subject only to deduction of interest the question of deduction of municipal tax does not arise. For let out proper-ties, municipal tax is deductible only if it is paid during the year.

Q.4. Is deduction for repairs available, when tenant undertakes repairs under the rental agreement? What is meant by repairs?

Answer.

By repairs we mean only substantial repairs as held in *CIT* vs. *Parbutty Churn Law* and *Sir Shadi Lai & Sons* vs. *CIT*. Where even substantial repairs other than normal maintenance is undertaken by tenant, annual value should get enhanced by the extent of repairs which should have been borne by the landlord so that any deduction for repairs then available to landlord will neutralise the amount added to annual rent. It would, therefore, mean that where there is specific stipulation that all repairs will be borne by tenant, there can be no deduction for repairs.

Q. 5. Is an annual charge on rent receivable on account of mortgage of property for obtaining funds for business or paying income tax deductible under section 24(1)(iv) of the Income Tax Act, 1961 ?

Answer.

No. Since it is a charge created voluntarily by the assessee, it is not deductible as was held in *CIT* vs. *Indramani Devi Singhcmia1* in case of a business loan and *CIT* vs. *Tarachand Kalyanji* in the case of a charge created for payment of excess profit tax In the latter case, it was held that the amount is not deductible even if the charge has been created before 1st April, 1969, when such amount was deductible in law.

Q. 6. What are the conditions for deduction of unrealised rent?

Answer.

Rule 4 of the Income-tax Rules as substituted by the Income-tax (Eighth Amendment) Rules, 2001 prescribes the conditions as under:

Unrealised rent—For the purposes of the Explanation below sub-section (1) of section 23, the amount of rent which the owner cannot realise shall be equal to the amount of rent payable but not paid by a tenant of the assessee and so proved to be lost and irrecoverable where,—

(a) the tenancy is *bona fide;*

(b) the defaulting tenant has vacated, or steps have been taken to compel him to vacate the property;

(c) the defaulting tenant is not in occupation of any other property of the assessee;

(d) the assessee has taken all reasonable steps to institute legal proceedings for the recovery of the unpaid rent or satisfies the Assessing Officer that legal proceedings would be useless.

Q.7. Is salary paid to a caretaker deductible?

Answer.

No. Only deductions specified under section 24 are deductible.

Q. 8. How is the income of co-owned property computed?

Answer.

Income has to be split up between co-owners and each co-owner has to be assessed as his share of the income as provided under section 26 of the Act.

Q. 9. Where an assessee borrows a second loan for repaying the first loan taken for acquiring a property, will the interest on second loan be deductible as amount borrowed for acquiring the property?

Answer.

Yes. It is so conceded in Board's Circular No. 28 dated 20th August, 1969.

Q. 10. Ground rent—whether arrears of earlier years deductible?

Answer.

No. The deduction under section 24(1)(v) is confined to the ground rent of previous year, and thus arrears of earlier years are not deductible.

Ground rent is no longer deductible from A.Y.2002-2003.

Q. 11. Interest deductible under section 24(1)(vi): whether simple interest or compound Interest?

Answer.

Only simple interest is deductible.

Q. 12. What is the treatment given to loss from property?

Answer.

Loss from property can be set off against other heads of income in the same year and to the extent unabsorbed, it will be carried forward and set off in next eight years.

Q. 13. Where municipal valuation is higher than the rent charged, what is the basis of computation of property income?

Answer.

The law requires that either annual value as fixed by the local authorities or actual rent received, whichever is higher, should be treated as annual value. But where the assessee is unable to enhance the rent due to Rent Control Act, there is a case for acceptance of rent receivable as the basis. It was so held in *CIT* vs. *Sampathammal Chordia* .

Q.14. Are municipal taxes allowed on the basis of tax leviable for a year or on the basis of payment? If it is on the basis of what is leviable, what happens if demand for earlier years is received only during the year with the result that the payments for earlier years are made during the year?

Answer.

Section 23(1) allows property tax levied by local authority on the basis of payment from assessment year 1985-86 vide amendment by Taxation Laws (Amendment) Act, 1984 so that the controversy in the prior law is now avoided. So, the amount paid during the year, including any amount of arrears for earlier years, is deductible in the year of payment.

Q. 15. Where the assessee is a mutual association having a property, will the property income be covered by the principle of mutuality so as to be exempt?

Answer.

Yes, it has been held that principle of mutuality applies even to income from house property in Chelmsford Club vs. CIT.

Q. 16. The assessee — Mrs. A is in enjoyment of the property but the right is limited only for life under a Will in her favour. Who has to pay the tax, whether she as the person in enjoyment of the property as the holder of life interest or the remainderman treated as the owner in law?

Answer.

Ownership is a bundle of rights. Right to enjoy the property is also a right which is part of such ownership right. Hence it will be assessable in the hands of life interest owner. It has been so held in *Estate of Ambalal Sarabhai* vs. *CIT*.

Q. 17. Where an assessee receives interest on deposit taken from a tenant, is it necessary to enhance the annual value by the notional interest which would have otherwise been payable?

Answer.

Where actual rent received is more than the fair rent, i.e., annual value fixed by the local authorities, notional interest need not be added. It was so held in *CIT* vs. *J.K. Investors (Bombay) Ltd.* Where such notional interest is to be taken, as for example, where no rent is charged because of such interest free deposit, the interest or other income earned by deployment of the interest free deposit will have to be correspondingly reduced from the annual value but the law does not provide for the same. But it stands to reason that such reduction may have to be allowed, though it is doubtful whether such reasonable interpretation will be acceptable to revenue.

Q. 18. Is it open to the Assessing Officer to substitute reasonable rent where the property is let out to an associate company at a lower rate?

Answer.

Since annual value is not the only criterion, it is open to the Assessing Officer to adopt a reasonable rate where it is let out at a concessional rate. It was so held in *T. V. Sundaram Iyengar & Sons Ltd.* vs. *CIT* .

Q. 19. Where the property is in existence for less than 12 months, is it possible to assess the income as income from property since the scheme of the Act is to assess the annual rent? Does the income escape assessment in such cases?

Answer.

The argument that the property should have been held for entire 12 months to be assessable under the head 'Income from property' was accepted in *P.J. Eapen* vs. *CIT.* But it was held that such income will be assessable under 'Other sources'. The decision is open to doubt because there is no reason why the proportionate income should not be assessed with reference to the period of holding because such proportionality is recognised in section 23 where the property is let out for part of the year and used for own residence for rest of the year under section 23(2)(a)(ii). Hence, similar apportionment should be possible though the annual value is with reference to the income which the property might fetch if let out from year to year.

Q. 20. Where the deduction under section 24 exceeds the available income, can such excess be allowable?

Answer.

Where the property is partly let out and partly used for own residence, the deduction under section 24(1) will be limited to the income determined under that clause under the substituted section 24 by Finance Act, 2001. with effect from 1.4.2002, there are no detailed deductions but only 30% of annual value and interest on borrowed capital subject to the limit of ₹ 30,000 for self-occupied property with enhanced limit up to ₹2.00 lakhs subject to conditions as to the date of the loan and the date of construction. Hence, there can be a loss from the property depending upon interest on borrowed capital. It is only in respect of annual value, that there cannot be loss.

Q. 21. There is a practice of receiving deposit instead of rent. The assessee accounts for interest on such deposits as its income. Should he also account for notional income from property?

Answer.

The answer was against the assessee in *S.Ujjanappa* vs. *CIT,* where it was held that ownership confers the duty to account for notional income from such property. The issue as to whether it involves double taxation was not posed in this case. Interest income earned by the assessee on the deposits or notional interest when used in business could have been set off against such income. There is clearly double taxation implicit in such cases. In *Webb's Agricultural & Automobile Industries* vs. *ITO* , a car received by way of lottery winnings brought to tax as income was held to be eligible for depreciation, though assessee had not paid for the same, because of the notional cost. This line of reasoning should avoid elimination of double taxation by setting off the two incomes one notional and the other real as between them, but the law on the subject is still nebulous.

Q.22. Is the amount of interest paid on unpaid consideration for acquiring property deductible as interest on borrowing under section 24(1)(vi) of the Income-tax Act?

Answer.

In the context of similar interest on unpaid consideration for acquiring a business; the Supreme Court had held in *Bombay Steam Navigation Co. (1953) P. Ltd.* vs. *CIT* that such interest is not deductible under section 36(1)(iii) of the Income-tax Act, 1961. But in the same case, it was found that it can be allowed as deduction under section 37 of the Act. It is for this reason that it has felt that in absence of similar residuary clause, interest on unpaid consideration for acquiring property would not be deductible. However it was found in *CIT* vs. *Sunil Kumar Sharma* following *CIT* vs. *R.P. Goenka and J.P. Goenka* that it makes no difference, whether the buyer borrows from a third party to acquire a property or gets the necessary financial assistance from the seller of the property. It should be construed that the seller is the lender and the purchaser is the borrower. It would thus appear that such interest is deductible.

Q. 23. What is the change in respect of computation of property income by the Finance Act, 2005?

Answer.

There is no change in computation of property income, but the incentive for re-payment of loan for acquiring a property is enlarged by removing the limit of ₹ 20,000 in respect of such repayment and by providing such repayment as an outright deduction from the gross total income by the new section 80C substituting section 88, subject, however, to the limit of total deduction under section 80C to ₹ 1.50 lakh. Interest payable on such loan would be admissible as deduction, if the property were let out, subject to limit of ₹30,000 in case of self- occupation.

Q. 24. If a person puts up a property on leased land, is the lease rent deductible as income from property?

Answer.

There is no special provision for deduction of lease rent as was available in the pre-existing law under section 24 either as an annual charge on the property or as ground rent, but all the same, what is payable on leased land gets diverted at source and should not be part of the annual value, so that in determination of annual value, the amount should be deductible. Any other view could not be reasonable. An alternative argument may well be that if it is not deductible, income itself may not be assessable as a property income as the assessee is not the full owner of the property, so that income will be assessable as from "Other sources", so that the deduction in such a case cannot be denied, though the assessee may not be eligible for an ad hoc deduction at 30%; but only actual repairs, where it is assessable as income from other sources.

Q.25. Where a landlord undertakes to meet the expenses of watch and ward, corridor, lighting, lift, etc., are such expenses deductible from property income?

Answer.

Expenses which are ordinarily borne by the tenant, but undertaken by the landlord according to terms of rental agreement will go to reduce the annual value, because the rental value of the property can only be the net income after meeting the tenant's burden.

Q.26. Where the assessee allows the property to be used by firm of which he is a partner without charging rent, is he entitled to self-occupation allowance or depreciation?

Answer.

Since the firm is not a separate legal entity, the use of property by the firm should be treated as use and occupation of the property by the partner itself, so that self-occupation benefit will be available from income from such property. If the property is used for business, there is eligibility for depreciation also.

Q. 27. Where a partner allows the use of the property by the firm and charges rent for the same, would he be entitled to ad hoc deduction at 30% or depreciation of the property because of the use for business?

Answer.

Since the rent is received from a firm of which he is a partner, the amount of rent receivable may not be treated as received in his capacity as landlord, but as a partner. If the property is used for business, the owner should be entitled to depreciation. It was so held in *CIT* vs. *Ramlubhaiya R. Malhotra* following *A.M. Ponnuranga Mudaliar* vs. *CIT.* The latter decision was followed in *CIT* vs. *Texspin Engineering and Manufacturing Works.*

Q.28. In the case where a tenant sublets the property, is the rent paid by the tenant deductible from the income from subletting?

Answer.

Since the tenant is not the owner, the income should ordinarily be assessable as income from other sources, so that the rent paid should be deductible. Even if it were lease- hold property, the rent paid may have to be taken into account in determining the annual value. Contrary view taken in *CIT* vs. *Hemraj Mahabir Prasad Ltd.* would need review.

Q.29. Where the assessee borrows money on mortgage of his property for his daughter's marriage, is such interest paid deductible from the property income?

Answer.

Merely because the loan is charged on the property, interest does not become deductible, because the amount is not borrowed for purpose of acquiring or constructing the property.

Q.30. To take advantage of mutuality principle, persons renting the hall of a club for marriage become temporary members. Is such receipt exempt from liability in the hands of the club?

Answer.

No. There is no mutuality involved. Temporary membership for an ulterior purpose is not permissible. The rents are taxable in the hands of the club.

TAX PLANNING-FOR BUSINESS EXPENDITURE

Q. 1. There is a prevailing practice of a businessman taking loan of stock from another businessman and returning the same. Since he may have to pay for replacement at a higher price for return of loan of stock, can a provision made for the extra cost be deductible?

Answer.

The issue had come up in *Welding Rods Manufacturing Co.* vs. *CIT,* where it was found that the price rise at the time of closure of accounts in respect of outstanding loan of stock could be recognised and the provision therefore would be allowed as a deduction. In coming to the conclusion the High Court followed the decision in *Calcutta Co. Ltd.* vs. *CIT.*

In this context, one may refer to the statutory provision in section 47(xv) in respect of capital gains on stock lending, whereby tax on capital gains is spared on such stock lending, if the guidelines issued by Securities and Exchange Board of India had been followed. The provision, however, is only for exemption from capital gains and the mere act of lending of securities in pursuance of stock lending scheme. It cannot have application for dealers in shares. Similarly, the final outcome of the transaction even in the case of an investor may have to be recognised for capital gains tax purposes under the law as exemption is at the stage of lending and not at the stage when the contractual obligation gets discharged.

Q. 2. Does a liability arise under excise law on show cause notice, which makes a special recognition for show cause notice, where such notice has been issued?

Answer.

Notwithstanding the effect of a show cause notice, it does not create a demand for payment by itself, so as to justify the amount covered by the notice as statutory liability, on the basis of the decision in *Kedarnath Jute Mfg. Co. Ltd.* vs. *CIT*. It was so pointed out in *CIT vs. Morarji Goculdas Spg. & Wvg. Co. Ltd.*

Q. 3. Should the right to deduction await final result of any claim?

Answer.

Courts have not taken a uniform view. Ordinarily when a final decision is awaited, deduction could be made only in the year in which the matter gets resolved as in the case of requirement of approval from the authorities following the decision in *Nonsuch Tea Estate Ltd.* vs. *CIT* . But in a case on converse facts, it was held that in the accrual concept in mercantile system of accounting, a mere requirement of approval, when it has become available at the time of assessment or even in appeal, such delay in approval need not bar assessment in the year of receipt as was held in *CIT* vs. *Jai Hind Travels (P) Ltd.* , where the concept of the doctrine of relating back was adopted for accrual system. Such a view cannot be treated as non-controversial. Deduction need not be denied, where *ex post facto* approval is a formality. It is difficult to draw a line in such cases. It is for the taxpayer to make a provision in such cases in the year of claim, so that even if it is disallowed, it can be claimed in the year of payment. Failure to make the claim in an earlier year may lose the right, if revenue decides that the claim could be allowed only in the first year.

Q. 4. Is it open to the Revenue to disallow a portion of electricity charges paid with reference to the refund claim made during the year, but given in a subsequent year?

Answer.

Receipt of refund in a subsequent year cannot be taken as a ground for not allowing a deduction at the time, when it was payable as was held in *Travancore Chemical and Mfg. Co.Ltd.* vs. *CIT* following the decision in *CIT* vs. *Bharat Iron and Steel Industries,* The High Court pointed out that the need for section 41(1) to tax amounts that had been remitted or waived would not have arisen, if allowance due for an earlier year could be modified with reference to the later waiver or remission.

Q. 5. Is it possible to value stock by methods other than cost, market value, or cost or market value, whichever is lower?

Answer.

Any method which is consistently followed and is not likely to distort the income and is consistent with accounting principles should be acceptable. Lower valuation for slow moving goods in the view that future carrying cost would require to be taken into consideration was approved in *India Motor Parts and Accessories P. Ltd.* vs. *CIT.* The method, it was pointed out, had been suggested as a proper valuation in *Industrial Accountants Hand Book* edited by Wyman P Firke of John A. Beckett. Such a view had also the approval of Delhi High Court in *CIT* vs. *Bharat Commerce and Industries Ltd.* .

Q. 6. How is the work in progress valued? Should the overheads be treated as part of cost?

Answer.

Work-in-progress is generally valued at cost. The issue as to whether the overheads should be taken into consideration by adoption of "on-cost" basis or whether only direct cost should be taken was considered in *Duple Motor Bodies Ltd.* vs. *Inland Revenue Commissioner* , where it was found that either method can be adopted but where the assessee has adopted one method, it is not open to him to change it.

Where an assessee had followed a method of accounting, which excluded over-heads in valuation of work-in-progress on the ground that the goods under manufacture may not result in marketable commodities, the Tribunal rejected the change mainly on the ground that there was no evidence of possible deterioration of work-in-progress. The High Court, however, found that since the assessee had followed the same method in earlier years, it was entitled to continue the same practice. The Supreme Court in *CIT* vs. *British Paints India Ltd.* decided on the short point that merely because a system has been consistently followed, it does not mean that Revenue is bound by it, if it finds that it is not consistent with accounting principles. If the income could xiot be rightly deduced from the system followed, it was open to the Assessing Officer to reject the same, since there is no estoppel in such matters. According to this decision, the cost ordinarily has to reckon overheads as well. The distinction between finished stock and work-in-progress was however not appreciated in this case, when it reversed the decision of the Calcutta High Court. But it is still an authority for the view that the method followed should be consistent with accounting principles. A scientific method of valuation of work-in-progress is probably only the retrievable value or a value which makes an allowance for a situation, if the goods turn out to be non-marketable. In other words, valuation at less than the cost or market value for work-in-progress should be permissible in certain lines of manufacture, where there is possible wastage before completion of the manufacture of the product, if such valuation is consistently followed.

Q. 7. An assessee had the practice of accounting receipts from contract only when the bills raised by it were passed by the contractee. Where such a method is regularly followed, can it be rejected by the Assessing Officer?

Answer.

Yes. It was so held in *CIT* vs. *Shaik Mohd Rowther Shipping and Agencies (P) Ltd.* , where it was pointed out that the method is not consistent with any accounting principles. The work has been done on the basis of which bills were raised. 90% of the amount was also received, the balance pending for passing of the bills. Merely because the amount received is shown as advance, it is not possible to postpone recognition of revenue. The mere fact that the Assessing Officer had not disturbed the system in earlier years does not prevent him from correcting the same as the principle of *res judicata* can have no application to tax cases as was pointed out in *CIT vs. Brit.*

Q.8. Which is the best head of income from tax point of view, where there is a possible choice?

Answer.

The best head is business as it is eligible for a list of deductions and reliefs.

Q.9. A business executive has purchased and sold shares through a stock broker. Will the loss, if any, be assessable under the head "business" or "capital gain"?

Answer.

The mere fact that he has purchased and sold shares through a broker does not entitle the assessee to treat the income as business income. There should be a continuous activity. Moreover, if the interval between purchase and sale is short, profit will be referred under the head "Short Term Capital Gains" without any advantage.

Q.10. A piece of land acquired five years before is plotted out and sold. What is the head of income?

Answer.

To treat the sale of land as a business transaction more facts are required. There should be facts to suggest that the land was converted to a business asset and dealt with as such and the sale is not just for the sake of realisation of appreciation in value.

Q.11. Can what is "accrued but not due" ever be treated as accrued for tax purposes? What is the correct treatment of interest from cumulative deposits in the hands of payer and payee?

Answer.

This depends on the system of accounting. An assessee might choose with advantage to declare that income from year to year on accrual basis. However, the payer will deduct tax on the accumulated interest at the time of payment accords to section 194A in which case the assessee may have to ask for a refund.

Q.12. How far are Income computation and Disclosure Standards relevant in computation of business income?

Answer.

Income for income-tax purposes is computed under ordinary principles of commercial accounting. Income computation and disclosure standards lay down such principles accepted by the profession and have even been made mandatory for purposes of company law. Hence they have great persuasive value.

Q.13. A taxpayer has changed his method of stock valuation. Statutory auditors did not agree to the change and have qualified the balance sheet. Assessing Officer relies upon the decision of Supreme Court in *British Paint's* case for rejecting the change. Is he justified in doing so?

Answer.

What is required is that the change in the method of valuation should be bona fide and thereafter followed continuously.

In *Karnataka State Forest Industries Corporation Ltd.* vs. *CIT* High Court found that the Income-tax Officer cannot reject a change in the method of valuation of stock merely because statutory auditors objected to it.

Q.14. A firm replaces defective TV sets long after the guarantee period was over with a view to maintain goodwill of the firm. Cost of replacement is disallowed by the Assessing Officer. Is he right?

Answer.

Since the outlay was incurred on grounds of commercial expediency the claim is admissible. The paragraph under "commercial expediency" (supra) would give necessary authorities for the same.

Q.15. Is a payment made to Life Insurance Corporation of India towards group gratuity fund deductible under section 36(1)(v), though it has not been routed through an approved gratuity fund?

Answer.

The deduction need not be denied merely because a direct payment has been made as long as it is towards account of group gratuity fund. It was so decided in *CIT* vs. *Textool Co. Ltd.* In fact this would have even otherwise been allowed under Sec. 37.

Q.16. Can dumpers used in contract work be classified as earth moving machinery?

Answer.

Yes. They are entitled to depreciation and extra depreciation as earth moving machinery as held in *CIT* vs. *Abdulkarim Stone Contractor* . They are not road transport vehicles.

Q.17. What is meant by block asset?

Answer.

Certain types of assets are grouped into one block and additions to the same will be treated as part of the block.

Q.18. What are the changes brought about by bringing in the concept of 'block asset' in evaluating cost for depreciation?

Answer.

Each item of machineries is not separately considered for depreciation. Where a particular capital asset or assets forming part of the block is sold, the difference between the full value of the consideration on one hand and the WDV of the block asset, plus expenditure incurred in the transfer, plus value of any asset added to the block on the other hand is treated as Short-term Capital Gains.(Sec. 50)

The idea was to give up the profit under section 41(2) as it stood then which represented the amount of depreciation actually received. Earlier this amount was added as income and any excess above the depreciation was to be treated as capital gains as held in *CIT vs. Artex Manufacturing Co.*

However section 41(2) has now been reintroduced with effect from 1.4.1998.

Q. 19. The assessee has a project report for a new venture carried out at the cost of ₹5 lakhs. Assessing Officer disallows the same as the venture re-lates to a new business. Is the assessee eligible for deduction and if not, is he eligible for depreciation?

Answer.

If the project report relates to an existing business for its expansion, it will be a revenue expenditure. But if it relates to a new business, it will be a capital expenditure eligible for depreciation as decided in *CIT* vs. *Harsha Tractor Ltd.* following the decision in *Scientific Engineering House P. Ltd.* vs. *CIT*. After amendment to section 32(1) allowing depreciation on intangible assets from 1.4.1998, it is a matter of statutory right for the assessee to get depreciation not merely by treating such project report as a plant as under the pre-existing law but as an intangible asset on par with other tangible assets, so that the cost is entitled to depreciation like other intangible assets like know-how, patents, copyrights, trademarks, licence, franchise or any other business or commercial rights of similar nature.

Q.20. Where an air-conditioning plant is fixed in a bus, would such air-conditioner and bus be eligible for rates respectively applied to them?

Answer.

Air-conditioning plant, which is an integral part of bus would not be entitled to rate of depreciation different from what is available for motor vehicles, where they are installed.

Q.21. Can fencing be treated as a plant?

Answer.

No, it can be treated only as a building.

Q.22. It is the normal practice of revenue to deduct all depreciation allowed including initial depreciation in arriving at the WDV. Is this correct?

Answer.

According to Gujarat High Court, depreciation is referable to wear and tear. Initial depreciation being in the form of an incentive is not to be deducted.

Q.23. Where a wholly owned subsidiary company acquires depreciable assets from the holding company at market value, is it eligible for depreciation on such market value?

Answer.

No. Explanation 6 to section 43(1) provides that in the case of acquisition of assets by a wholly-owned subsidiary from its holding company, the written down value of the holding company will be the actual cost to the subsidiary as held in *Dalmia Ceramic Industries Ltd.* vs. *CIT.*

Q.24. Could a road in a factory building used exclusively for industrial purpose be treated as a plant for purposes of depreciation?

Answer.

Road could not be treated as a plant, but only as a building for purposes of depreciation.

Q.25. Where the assessee undertook gratuity liability of the vendor of the business as per agreement for sale, such liability is also consideration, so that it could be treated as part of the cost of assets entitled to depreciation. Is this correct?

Answer.

Since the assessee has undertaken only a future liability, it cannot form part of the cost so as to be entitled to depreciation.

Q.26. Is it possible to capitalise expenditure as cost of the asset for purposes of depreciation?

Answer.

Expenditure which has nexus with the asset can be treated as part of the cost of the asset. Cost of temporary electricity connection, power line and inspection fee relating thereto were held to be part and parcel of cost of machinery for purposes of depreciation.

Q.27. Are computers office equipments so as to be ineligible for investment allowance or additional depreciation?

Answer.

'Office equipment' has not been defined in the statute. What is barred is plant and machinery installed in office premises. Office premises have also not been defined. In case of a doctor, a clinic may be his office, but at the same time, it is also his place of practice. A computer is not ordinarily an office equipment like a typewriter or a duplicating machine. Computers are, therefore, eligible for investment allowance, when it was in vogue and additional depreciation.

9.12 INCOME COMPUTATION AND DISCLOSURE STANDARDS

Central Government vide **Notification No. 32/2015, dated 31-3-2015** has notifies the "Income Computation and Disclosure Standards" as specified below to be followed by all assessees, following the mercantile system of accounting, for the purposes of computation of income chargeable to income-tax under the head **"Profit and Gains of Business or Profession"** or **"Income from Other Sources"**. This notification shall come into force with effect from 1st day of April, 2015, and shall accordingly apply to the assessment year 2016-17 and subsequent assessment years.

List of Standards are as follows:

(A) Income Computation and Disclosure Standard I relating to accounting policies Preamble

(B) Income Computation and Disclosure Standard II relating to valuation of inventories

(C) Income Computation and Disclosure Standard III relating to construction contracts

(D) Income Computation and Disclosure Standard IV relating to revenue recognition Preamble

(E) Income Computation and Disclosure Standard V relating to tangible fixed assets Preamble

(F) Income Computation and Disclosure Standard VI relating to the effects of changes in foreign exchange rates

(G) Income Computation and Disclosure Standard VII relating to government grants Preamble

(H) Income Computation and Disclosure Standard VIII relating to securities Preamble

(I) Income Computation and Disclosure Standard IX relating to borrowing costs Preamble

(J) Income Computation and Disclosure Standard X relating to provisions, contingent liabilities and contingent assets.

(A) Income Computation and Disclosure Standard I relating to accounting policies Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard deals with significant accounting policies.

2. Fundamental Accounting Assumptions

The following are fundamental accounting assumptions, namely:—

(a) Going Concern

"Going concern" refers to the assumption that the person has neither the intention nor the necessity of liquidation or of curtailing materially the scale of the business, profession or vocation and intends to continue his business, profession or vocation for the foreseeable future.

(b) Consistency

"Consistency" refers to the assumption that accounting policies are consistent from one period to another.

(c) Accrual

"Accrual" refers to the assumption that revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the previous year to which they relate.

3. Accounting Policies

The accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by a person.

4. Considerations in the Selection and Change of Accounting Policies

Accounting policies adopted by a person shall be such so as to represent a true and fair view of the state of affairs and income of the business, profession or vocation. For this purpose,—

(i) the treatment and presentation of transactions and events shall be governed by their substance and not merely by the legal form; and

(ii) marked to market loss or an expected loss shall not be recognised unless the recognition of such loss is in accordance with the provisions of any other Income

5. Computation and Disclosure Standard

An accounting policy shall not be changed without reasonable cause.

6. Disclosure of Accounting Policies

All significant accounting policies adopted by a person shall be disclosed.

7. Any change in an accounting policy which has a material effect shall be disclosed. The amount by which any item is affected by such change shall also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact shall be indicated. If a change is made in the accounting policies which has no material effect for the current previous year but which is reasonably expected to have a material effect in later previous years, the fact of such change shall be appropriately disclosed in the previous year in which the change is adopted and also in the previous year in which such change has material effect for the first time.

8. Disclosure of accounting policies or of changes therein cannot remedy a wrong or inappropriate treatment of the item.

9. If the fundamental accounting assumptions of Going Concern, Consistency and Accrual are followed, specific disclosure is not required. If a fundamental accounting assumption is not followed, the fact shall be disclosed.

10. Transitional Provisions

All contract or transaction existing on the 1st day of April, 2015 or entered into on or after the 1st day of April, 2015 shall be dealt with in accordance with the provisions of this standard after taking into account the income, expense or loss, if any, recognised in respect of the said contract or transaction for the previous year ending on or before the 31st March, 2015.

(B) Income Computation and Disclosure Standard II relating to valuation of inventories

Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of Business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of Income Tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard shall be applied for valuation of inventories, except:

(a) Work-in-progress arising under 'construction contract' including directly related service contract which is dealt with by the Income Computation and Disclosure Standard on construction contracts;

(b) Work-in-progress which is dealt with by other Income Computation and Disclosure Standard;

(c) Shares, debentures and other financial instruments held as stock-in-trade which are dealt with by the Income Computation and Disclosure Standard on securities;

(d) Producers' inventories of livestock, agriculture and forest products, mineral oils, ores and gases to the extent that they are measured at net realizable value;

(e) Machinery spares, which can be used only in connection with a tangible fixed asset and their use is expected to be irregular, shall be dealt with in accordance with the Income Computation and Disclosure Standard on tangible fixed assets.

2. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Inventories" are assets:

(i) held for sale in the ordinary course of business;

(ii) in the process of production for such sale;

(iii) in the form of materials or supplies to be consumed in the production process or in the rendering of services.

(b) "Net realisable value" is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

2(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meanings assigned to them in that Act.

3. Measurement

Inventories shall be valued at cost, or net realisable value, whichever is lower.

4. Cost of Inventories

Cost of inventories shall comprise of all costs of purchase, costs of services, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

5. Costs of Purchase

The costs of purchase shall consist of purchase price including duties and taxes, freight inwards and other expenditure directly attributable to the acquisition. Trade discounts, rebates and other similar items shall be deducted in determining the costs of purchase.

6. Costs of Services

The costs of services in the case of a service provider shall consist of labour and other costs of personnel directly engaged in providing the service including supervisory personnel and attributable overheads.

7. Costs of Conversion

The costs of conversion of inventories shall include costs directly related to the units of production and a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods. Fixed production overheads shall be those indirect costs of production that remain relatively constant regardless of the volume of production. Variable production overheads shall be those indirect costs of production that vary directly or nearly directly, with the volume of production.

8. The allocation of fixed production overheads for the purpose of their inclusion in the costs of conversion shall be based on the normal capacity of the production facilities.

Normal capacity shall be the production expected to be achieved on an average over a number of periods or seasons under normal circumstances, taking into account the loss of capacity resulting from planned maintenance. The actual level of production shall be used when it approximates to normal capacity. The amount of fixed production overheads allocated to each unit of production shall not be increased as a consequence of low production or idle plant. Unallocated overheads shall be recognised as an expense in the period in which they are incurred. In periods of abnormally high production, the amount of fixed production overheads allocated to each unit of production is decreased so that inventories are not measured above the cost. Variable production overheads shall be assigned to each unit of production on the basis of the actual use of the production facilities.

9. Where a production process results in more than one product being produced simultaneously and the costs of conversion of each product are not separately identifiable, the costs shall be allocated between the products on a rational and consistent basis. Where by-products, scrap or waste material are immaterial, they shall be measured at net realisable value and this value shall be deducted from the cost of the main product.

10. Other Costs

Other costs shall be included in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition.

11. Interest and other borrowing costs shall not be included in the costs of inventories, unless they meet the criteria for recognition of interest as a component of the cost as specified in the Income Computation and Disclosure Standard on borrowing costs.

12. Exclusions from the Cost of Inventories

In determining the cost of inventories in accordance with paragraphs 4 to paragraphs 11, the following costs shall be excluded and recognised as expenses of the period in which they are incurred, namely:—

(a) Abnormal amounts of wasted materials, labour, or other production costs;

(b) Storage costs, unless those costs are necessary in the production process prior to a further production stage;

(c) Administrative overheads that do not contribute to bringing the inventories to their present location and condition;

(d) Selling costs.

13. Cost Formulae

The Cost of inventories of items—

(i) that are not ordinarily interchangeable; and

(ii) goods or services produced and segregated for specific projects shall be assigned by specific identification of their individual costs.

14. 'Specific identification of cost' means specific costs are attributed to identified items of inventory.

15. Where there are a large numbers of items of inventory which are ordinarily interchangeable, specific identification of costs shall not be made.

16. First-in First-out and Weighted Average Cost Formula

Cost of inventories, other than the inventory dealt with in paragraph 13, shall be assigned by using the First-in First-out (FIFO), or weighted average cost formula. The formula used shall reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition.

17. The FIFO formula assumes that the items of inventory which were purchased or produced first are consumed or sold first, and consequently the items remaining in inventory at the end of the period are those most recently purchased or produced. Under the weighted average cost formula, the cost of each item is determined from the weighted average of the cost of similar items at the beginning of a period and the cost of similar items purchased or produced during the period. The average shall be calculated on a periodic basis, or as each additional shipment is received, depending upon the circumstances.

18. Retail Method

Where it is impracticable to use the costing methods referred to in paragraph 16, the retail method can be used in the retail trade for measuring inventories of large number of rapidly changing items that have similar margins. The cost of the inventory is determined by reducing from the sales value of the inventory, the appropriate percentage gross margin. The percentage used takes into consideration inventory, which has been marked down to below its original selling price.

19. Net Realisable Value

Inventories shall be written down to net realisable value on an item-by-item basis. Where 'items of inventory' relating to the same product line having similar purposes or end uses and are produced and marketed in the same geographical area and cannot be practicably evaluated separately from other items in that product line, such inventories shall be grouped together and written down to net realisable value on an aggregate basis.

20. Net realisable value shall be based on the most reliable evidence available at the time of valuation. The estimates of net realisable value shall also take into consideration the purpose for which the inventory is held. The estimates shall take into consideration fluctuations of price or cost directly relating to events occurring after the end of previous year to the extent that such events confirm the conditions existing on the last day of the previous year.

21. Materials and other supplies held for use in the production of inventories shall not be written down below the cost, where the finished products in which they shall be incorporated are expected to be sold at or above the cost. Where there has been a decline in the price of materials and it is estimated that the cost of finished products will exceed the net realisable value, the value of materials shall be written down to net realisable value which shall be the replacement cost of such materials.

22. Value of Opening Inventory

The value of the inventory as on the beginning of the previous year shall be—

(i) the cost of inventory available, if any, on the day of the commencement of the business when the business has commenced during the previous year; and

(ii) the value of the inventory as on the close of the immediately preceding previous year, in any other case.

23. Change of Method of Valuation of Inventory

The method of valuation of inventories once adopted by a person in any previous year shall not be changed without reasonable cause.

24. Valuation of Inventory in Case of Certain Dissolutions

In case of dissolution of a partnership firm or association of person or body of individuals, notwithstanding whether business is discontinued or not, the inventory on the date of dissolution shall be valued at the net realisable value.

25. Transitional Provisions

Interest and other borrowing costs, which do not meet the criteria for recognition of interest as a component of the cost as per para 11, but included in the cost of the opening inventory as on the 1st day of April, 2015, shall be taken into account for determining cost of such inventory for valuation as on the close of the previous year beginning on or after 1st day of April, 2015 if such inventory continue to remain part of inventory as on the close of the previous year beginning on or after 1st day of April, 2015.

26. Disclosure

The following aspects shall be disclosed, namely:—

(a) the accounting policies adopted in measuring inventories including the cost formulae used; and

(b) the total carrying amount of inventories and its classification appropriate to a person.

(C) Income Computation and Disclosure Standard III relating to construction contracts

Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard should be applied in determination of income for a construction contract of a contractor.

2. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Construction contract" is a contract specifically negotiated for the construction of an asset or a combination of assets that are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use and includes:

(i) contract for the rendering of services which are directly related to the construction of the asset, for example, those for the services of project managers and architects;

(ii) contract for destruction or restoration of assets, and the restoration of the environment following the demolition of assets.

(b) "Fixed price contract" is a construction contract in which the contractor agrees to a fixed contract price, or a fixed rate per unit of output, which may be subject to cost escalation clauses.

(c) "Cost plus contract" is a construction contract in which the contractor is reimbursed for allowable or otherwise defined costs, plus a mark up on these costs or a fixed fee.

(d) "Retentions" are amounts of progress billings which are not paid until the satisfaction of conditions specified in the contract for the payment of such amounts or until defects have been rectified.

(e) "Progress billings" are amounts billed for work performed on a contract whether or not they have been paid by the customer.

(f) "Advances" are amounts received by the contractor before the related work is performed.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meaning respectively assigned to them in the Act.

3. A construction contract may be negotiated for the construction of a single asset. A construction contract may also deal with the construction of a number of assets which are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use.

4. Construction contracts are formulated in a number of ways which, for the purposes of this Income Computation and Disclosure Standard, are classified as fixed price contracts and cost plus contracts. Some construction contracts may contain characteristics of both a fixed price contract and a cost plus contract, for example, in the case of a cost plus contract with an agreed maximum price.

5. Combining and Segmenting Construction Contracts

The requirements of this Income Computation and Disclosure Standard shall be applied separately to each construction contract except as provided for in paragraphs 6, 7 and 8 herein. For reflecting the substance of a contract or a group of contracts, where it is necessary, the Income Computation and Disclosure Standard should be applied to the separately identifiable components of a single contract or to a group of contracts together.

6. Where a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

7. A group of contracts, whether with a single customer or with several customers, should be treated as a single construction contract when:

(a) the group of contracts is negotiated as a single package;

(b) the contracts are so closely interrelated that they are, in effect, part of a single project with an overall profit margin; and

(c) the contracts are performed concurrently or in a continuous sequence.

8. Where a contract provides for the construction of an additional asset at the option of the customer or is amended to include the construction of an additional asset, the construction of the additional asset should be treated as a separate construction contract when:

(a) the asset differs significantly in design, technology or function from the asset or assets covered by the original contract; or

(b) the price of the asset is negotiated without having regard to the original contract price.

9. Contract Revenue

Contract revenue shall be recognised when there is reasonable certainty of its ultimate collection.

10. Contract revenue shall comprise of:

(a) the initial amount of revenue agreed in the contract, including retentions; and

(b) variations in contract work, claims and incentive payments:

    (i) to the extent that it is probable that they will result in revenue; and

    (ii) they are capable of being reliably measured.

11. Where contract revenue already recognised as income is subsequently written off in the books of accounts as uncollectible, the same shall be recognised as an expense and not as an adjustment of the amount of contract revenue.

12. Contract Costs

Contract costs shall comprise of:

(a) costs that relate directly to the specific contract;

(b) costs that are attributable to contract activity in general and can be allocated to the contract;

(c) such other costs as are specifically chargeable to the customer under the terms of the contract; and

(d) allocated borrowing costs in accordance with the Income Computation and Disclosure Standard on Borrowing Costs. These costs shall be reduced by any incidental income, not being in the nature of interest, dividends or capital gains, that is not included in contract revenue.

13. Costs that cannot be attributed to any contract activity or cannot be allocated to a contract shall be excluded from the costs of a construction contract.

14. Contract costs include the costs attributable to a contract for the period from the date of securing the contract to the final completion of the contract. Costs that are incurred in securing the contract are also included as part of the contract costs, provided

(a) they can be separately identified; and

(b) it is probable that the contract shall be obtained.

When costs incurred in securing a contract are recognised as an expense in the period in which they are incurred, they are not included in contract costs when the contract is obtained in a subsequent period.

15. Contract costs that relate to future activity on the contract are recognised as an asset. Such costs represent an amount due from the customer and are classified as contract work in progress.

16. Recognition of Contract Revenue and Expenses

Contract revenue and contract costs associated with the construction contract should be recognised as revenue and expenses respectively by reference to the stage of completion of the contract activity at the reporting date.

17. The recognition of revenue and expenses by reference to the stage of completion of a contract is referred to as the percentage of completion method. Under this method, contract revenue is matched with the contract costs incurred in reaching the stage of completion, resulting in the reporting of revenue, expenses and profit which can be attributed to the proportion of work completed.

18. The stage of completion of a contract shall be determined with reference to:

(a) the proportion that contract costs incurred for work performed upto the reporting date bear to the estimated total contract costs; or

(b) surveys of work performed; or

(c) completion of a physical proportion of the contract work.

Progress payments and advances received from customers are not determinative of the stage of completion of a contract.

19. When the stage of completion is determined by reference to the contract costs incurred upto the reporting date, only those contract costs that reflect work performed are included in costs incurred upto the reporting date. Contract costs which are excluded are:

(a) contract costs that relate to future activity on the contract; and

(b) payments made to subcontractors in advance of work performed under the subcontract.

20. During the early stages of a contract, where the outcome of the contract cannot be estimated reliably contract revenue is recognised only to the extent of costs incurred. The early stage of a contract shall not extend beyond 25 % of the stage of completion.

21. Changes in Estimates

The percentage of completion method is applied on a cumulative basis in each previous year to the current estimates of contract revenue and contract costs.

Where there is change in estimates, the changed estimates shall be used in determination of the amount of revenue and expenses in the period in which the change is made and in subsequent periods.

22. Transitional Provisions

Contract revenue and contract costs associated with the construction contract, which commenced on or before the 31st day of March, 2015 but not completed by the said date, shall be recognised as revenue and costs respectively in accordance with the provisions of this standard. The amount of contract revenue, contract costs or expected loss, if any, recognised for the said contract for any previous year commencing on or before the 1st day of April, 2014 shall be taken into account for recognising revenue and costs of the said contract for the previous year commencing on the 1st day of April, 2015 and subsequent previous years.

23. Disclosure

A person shall disclose:

(a) the amount of contract revenue recognised as revenue in the period; and

(b) the methods used to determine the stage of completion of contracts in progress.

24. A person shall disclose the following for contracts in progress at the reporting date, namely:—

(a) amount of costs incurred and recognised profits (less recognised losses) upto the reporting date;

(b) the amount of advances received; and

(c) the amount of retentions.

(D) Income Computation and Disclosure Standard IV relating to revenue recognition Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

(1) This Income Computation and Disclosure Standard deals with the bases for recognition of revenue arising in the course of the ordinary activities of a person from

(i) the sale of goods;

(ii) the rendering of services;

(iii) the use by others of the person's resources yielding interest, royalties or dividends.

(2) This Income Computation and Disclosure Standard does not deal with the aspects of revenue recognition which are dealt with by other Income Computation and Disclosure Standards.

2. Definitions

(1) The following term is used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Revenue" is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of a person from the sale of goods, from the rendering of services, or from the use by others of the person's resources yielding interest, royalties or dividends. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meanings assigned to them in that Act.

3. Sale of Goods

In a transaction involving the sale of goods, the revenue shall be recognised when the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership. In a situation, where transfer of property in goods does not coincide with the transfer of significant risks and rewards of ownership, revenue in such a situation shall be recognised at the time of transfer of significant risks and rewards of ownership to the buyer.

4. Revenue shall be recognised when there is reasonable certainty of its ultimate collection.

5. Where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim for escalation of price and export incentives, revenue recognition in respect of such claim shall be postponed to the extent of uncertainty involved.

6. Rendering of Services

Revenue from service transactions shall be recognised by the percentage completion method. Under this method, revenue from service transactions is matched with the service transactions costs incurred in reaching the stage of completion, resulting in the determination of revenue, expenses and profit which can be attributed to the proportion of work completed. Income Computation and Disclosure Standard on construction contract also requires the recognition of revenue on this basis. The requirements of that Standard shall mutatis mutandis apply to the recognition of revenue and the associated expenses for a service transaction.

7. The Use of Resources by Others Yielding Interest, Royalties or Dividends

Interest shall accrue on the time basis determined by the amount outstanding and the rate applicable. Discount or premium on debt securities held is treated as though it were accruing over the period to maturity.

8. Royalties shall accrue in accordance with the terms of the relevant agreement and shall be recognised on that basis unless, having regard to the substance of the transaction, it is more appropriate to recognise revenue on some other systematic and rational basis.

9. Dividends are recognised in accordance with the provisions of the Act.

10. Transitional Provisions

The transitional provisions of Income Computation and Disclosure Standard on construction contract shall mutatis mutandis apply to the recognition of revenue and the associated costs for a service transaction undertaken on or before the 31st day of March, 2015 but not completed by the said date.

11. Revenue for a transaction, other than a service transaction referred to in Para 10, undertaken on or before the 31st day of March, 2015 but not completed by the said date shall be recognised in accordance with the provisions of this standard for the previous year commencing on the 1st day of April, 2015 and subsequent previous year. The amount of revenue, if any, recognised for the said transaction for any previous year commencing on or before the 1st day of April, 2014 shall be taken into account for recognising revenue for the said transaction for the previous year commencing on the 1st day of April, 2015 and subsequent previous years.

12. Disclosure

Following disclosures shall be made in respect of revenue recognition, namely:—

(a) in a transaction involving sale of good, total amount not recognised as revenue during the previous year due to lack of reasonably certainty of its ultimate collection along with nature of uncertainty;

(b) the amount of revenue from service transactions recognised as revenue during the previous year;

(c) the method used to determine the stage of completion of service transactions in progress; and

(d) for service transactions in progress at the end of previous year:

  (i) amount of costs incurred and recognised profits (less recognised losses) upto end of previous year;

  (ii) the amount of advances received; and

  (iii) the amount of retentions.

(E) Income Computation and Disclosure Standard V relating to tangible fixed assets Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard deals with the treatment of tangible fixed assets.

2. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Tangible fixed asset" is an asset being land, building, machinery, plant or furniture held with the intention of being used for the purpose of producing or providing goods or services and is not held for sale in the normal course of business.

(b) "Fair value" of an asset is the amount for which that asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meanings assigned to them in that Act.

3. Identification of Tangible Fixed Assets

The definition in clause (a) of sub-paragraph (1) of paragraph 2 provides criteria for determining whether an item is to be classified as a tangible fixed asset.

4. Stand-by equipment and servicing equipment are to be capitalised. Machinery spares shall be charged to the revenue as and when consumed. When such spares can be used only in connection with an item of tangible fixed asset and their use is expected to be irregular, they shall be capitalised.

5. Components of Actual Cost

The actual cost of an acquired tangible fixed asset shall comprise its purchase price, import duties and other taxes, excluding those subsequently recoverable, and any directly attributable expenditure on making the asset ready for its intended use. Any trade discounts and rebates shall be deducted in arriving at the actual cost.

6. The cost of a tangible fixed asset may undergo changes subsequent to its acquisition or construction on account of—

(i) price adjustment, changes in duties or similar factors; or

(ii) exchange fluctuation as specified in Income Computation and Disclosure

7. Standard on the effects of changes in foreign exchange rates.

Administration and other general overhead expenses are to be excluded from the cost of tangible fixed assets if they do not relate to a specific tangible fixed asset.

Expenses which are specifically attributable to construction of a project or to the acquisition of a tangible fixed asset or bringing it to its working condition, shall be included as a part of the cost of the project or as a part of the cost of the tangible fixed asset.

8. The expenditure incurred on start-up and commissioning of the project, including the expenditure incurred on test runs and experimental production, shall be capitalised. The expenditure incurred after the plant has begun commercial production, that is, production intended for sale or captive consumption, shall be treated as revenue expenditure.

9. Self-constructed Tangible Fixed Assets

In arriving at the actual cost of self-constructed tangible fixed assets, the same principles shall apply as those described in paragraphs 5 to 8. Cost of construction that relate directly to the specific tangible fixed asset and costs that are attributable to the construction activity in general and can be allocated to the specific tangible fixed asset shall be included in actual cost. Any internal profits shall be eliminated in arriving at such costs.

10. Non-monetary Consideration

When a tangible fixed asset is acquired in exchange for another asset, the fair value of the tangible fixed asset so acquired shall be its actual cost.

11. When a tangible fixed asset is acquired in exchange for shares or other securities, the fair value of the tangible fixed asset so acquired shall be its actual cost.

12. Improvements and Repairs

An Expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance is added to the actual cost.

13. The cost of an addition or extension to an existing tangible fixed asset which is of a capital nature and which becomes an integral part of the existing tangible fixed asset is to be added to its actual cost. Any addition or extension, which has a separate identity and is capable of being used after the existing tangible fixed asset is disposed of, shall be treated as separate asset.

14. Valuation of Tangible Fixed Assets in Special Cases

Where a person owns tangible fixed assets jointly with others, the proportion in the actual cost, accumulated depreciation and written down value is grouped together with similar fully owned tangible fixed assets. Details of such jointly owned tangible fixed assets shall be indicated separately in the tangible fixed assets register.

15. Where several assets are purchased for a consolidated price, the consideration shall be apportioned to the various assets on a fair basis.

16. Transitional Provisions

The actual cost of tangible fixed assets, acquisition or construction of which commenced on or before the 31st day of March, 2015 but not completed by the said date, shall be recognised in accordance with the provisions of this standard. The amount of actual cost, if any, recognised for the said assets for any previous year commencing on or before the 1st day of April, 2014 shall be taken into account for recognising actual cost of the said assets for the previous year commencing on the 1st day of April, 2015 and subsequent previous years.

17. Depreciation

Depreciation on a tangible fixed asset shall be computed in accordance with the provisions of the Act.

18. Transfers

Income arising on transfer of a tangible fixed asset shall be computed in accordance with the provisions of the Act.

19. Disclosures

Following disclosure shall be made in respect of tangible fixed assets, namely:—

(a) description of asset or block of assets;

(b) rate of depreciation;

(c) actual cost or written down value, as the case may be;

(d) additions or deductions during the year with dates; in the case of any addition of an asset, date put to use; including adjustments on account of—

  (i) Central Value Added Tax credit claimed and allowed under the CENVAT Credit Rules, 2004;

  (ii) change in rate of exchange of currency;

  (iii) subsidy or grant or reimbursement, by whatever name called;

(e) depreciation Allowable; and

(f) written down value at the end of year.

(F) Income Computation and Disclosure Standard VI relating to the effects of changes in foreign exchange rates

Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard deals with:

(a) treatment of transactions in foreign currencies;

(b) translating the financial statements of foreign operations;

(c) treatment of foreign currency transactions in the nature of forward exchange contracts.

2. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Average rate" is the mean of the exchange rates in force during a period.

(b) "Closing rate" is the exchange rate at the last day of the previous year.

(c) "Exchange difference" is the difference resulting from reporting the same number of units of a foreign currency in the reporting currency of a person at different exchange rates.

(d) "Exchange rate" is the ratio for exchange of two currencies.

(e) "Foreign currency" is a currency other than the reporting currency of a person.

(f) "Foreign operations of a person" is a branch, by whatever name called, of that person, the activities of which are based or conducted in a country other than India.

(g) "Foreign currency transaction" is a transaction which is denominated in or requires settlement in a foreign currency, including transactions arising when a person:—

(i) buys or sells goods or services whose price is denominated in a foreign currency; or

(ii) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or

(iii) becomes a party to an unperformed forward exchange contract; or

(iv) otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.

(h) "Forward exchange contract" means an agreement to exchange different currencies at a forward rate, and includes a foreign currency option contract or another financial instrument of a similar nature;

(i) "Forward rate" is the specified exchange rate for exchange of two Currencies at a specified future date;

(j) "Indian currency" shall have the meaning as assigned to it in section 2 of the Foreign Exchange Management Act, 1999;

(k) "Integral foreign operation" is a foreign operation, the activities of which are an integral part of the operation of the person;

(l) "Monetary items" are money held and assets to be received or liabilities to be paid in fixed or determinable amounts of money. Cash, receivables, and payables are examples of monetary items;

(m) "Non-integral foreign operation" is a foreign operation that is not an integral foreign operation;

(n) "Non-monetary items" are assets and liabilities other than monetary items. Fixed assets, inventories, and investments in equity shares are examples of non-monetary items;

(o) "Reporting currency" means Indian currency except for foreign operations where it shall mean currency of the country where the operations are carried out.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meaning assigned to them in the Act.

Foreign Currency Transactions

3. Initial Recognition

(1) A foreign currency transaction shall be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction.

(2) An average rate for a week or a month that approximates the actual rate at the date of the transaction may be used for all transaction in each foreign currency occurring during that period. If the exchange rate fluctuates significantly, the actual rate at the date of the transaction shall be used.

4. Conversion at Last Date of Previous Year

At last day of each previous year:—

(a) foreign currency monetary items shall be converted into reporting currency by applying the closing rate;

(b) where the closing rate does not reflect with reasonable accuracy, the amount in reporting currency that is likely to be realised from or required to disburse, a foreign currency monetary item owing to restriction on remittances or the closing rate being unrealistic and it is not possible to effect an exchange of currencies at that rate, then the relevant monetary item shall be reported in the reporting currency at the amount which is likely to be realised from or required to disburse such item at the last date of the previous year; and

(c) non-monetary items in a foreign currency shall be converted into reporting currency by using the exchange rate at the date of the transaction.

5. Recognition of Exchange Differences

(i) In respect of monetary items, exchange differences arising on the settlement thereof or on conversion thereof at last day of the previous year shall be recognised as income or as expense in that previous year.

(ii) In respect of non-monetary items, exchange differences arising on conversion thereof at the last day of the previous year shall not be recognised as income or as expense in that previous year.

6. Exceptions to Paragraphs 3,4 and 5

Notwithstanding anything contained in paragraph 3, 4 and 5; initial recognition, conversion and recognition of exchange difference shall be subject to provisions of section 43A of the Act or Rule 115 of Income-tax Rules, 1962, as the case may be.

Financial Statements of Foreign Operations

7. Classification of Foreign Operations

(1) The method used to translate the financial statements of a foreign operation depends on the way in which it is financed and operates in relation to a person. For this purpose, foreign operations are classified as either "integral foreign operations" or "non-integral foreign operations".

(2) The following are indications that a foreign operation is a non-integral foreign operation rather than an integral foreign operation:—

(a) while the person may control the foreign operation, the activities of the foreign operation are carried out with a significant degree of autonomy from the activities of the person;

(b) transactions with the person are not a high proportion of the foreign operation's activities;

(c) the activities of the foreign operation are financed mainly from its own operations or local borrowings;

(d) costs of labour, material and other components of the foreign operation's products or services are primarily paid or settled in the local currency;

(e) the foreign operation's sales are mainly in currencies other than Indian currency;

(f) cash flows of the person are insulated from the day-to-day activities of the foreign operation;

(g) sales prices for the foreign operation's products or services are not primarily responsive on a short-term basis to changes in exchange rates but are determined more by local competition or local government regulation;

(h) there is an active local sales market for the foreign operation's products or services, although there also might be significant amounts of exports.

8. Integral Foreign Operations

The financial statements of an integral foreign operation shall be translated using the principles and procedures in paragraphs 3 to 6 as if the transactions of the foreign operation had been those of the person himself.

9. Non-integral Foreign Operations

(1) In translating the financial statements of a non-integral foreign operation for a previous year, the person shall apply the following, namely:—

(a) the assets and liabilities, both monetary and non-monetary, of the non-integral foreign operation shall be translated at the closing rate;

(b) income and expense items of the non-integral foreign operation shall be translated at exchange rates at the dates of the transactions; and

(c) all resulting exchange differences shall be recognised as income or as expenses in that previous year.

(2) Notwithstanding anything stated in sub-paragraph 1, translation and recognition of exchange difference in cases referred to in section 43A of the Act or Rule 115 of Income-tax Rules, 1962 shall be carried out in accordance with the provisions contained in that section or that Rule, as the case may be.

10. Change in the Classification of a Foreign Operation

(1) When there is a change in the classification of a foreign operation, the translation procedures applicable to the revised classification should be applied from the date of the change in the classification.

(2) The consistency principle requires that foreign operation once classified as integral or non-integral is continued to be so classified. However, a change in the way in which a foreign operation is financed and operates in relation to the person may lead to a change in the classification of that foreign operation.

11. Forward Exchange Contracts

(1) Any premium or discount arising at the inception of a forward exchange contract shall be amortised as expense or income over the life of the contract. Exchange differences on such a contract shall be recognised as income or as expense in the previous year in which the exchange rates change. Any profit or loss arising on cancellation or renewal shall be recognised as income or as expense for the previous year.

(2) The provisions of sub-para (1) shall apply provided that the contract:

(a) is not intended for trading or speculation purposes; and

(b) is entered into to establish the amount of the reporting currency required or available at the settlement date of the transaction.

(3) The provisions of sub-para (1) shall not apply to the contract that is entered into to hedge the foreign currency risk of a firm commitment or a highly probable forecast transaction. For this purpose, firm commitment, shall not include assets and liabilities existing at the end of the previous year.

(4) The premium or discount that arises on the contract is measured by the difference between the exchange rate at the date of the inception of the contract and the forward rate specified in the contract. Exchange difference on the contract is the difference between:

(a) the foreign currency amount of the contract translated at the exchange rate at the last day of the previous year, or the settlement date where the transaction is settled during the previous year; and

(b) the same foreign currency amount translated at the date of inception of the contract or the last day of the immediately preceding previous year, whichever is later.

(5) Premium, discount or exchange difference on contracts that are intended for trading or speculation purposes, or that are entered into to hedge the foreign currency risk of a firm commitment or a highly probable forecast transaction shall be recognised at the time of settlement.

12. Transitional Provisions

(1) All foreign currency transactions undertaken on or after 1st day of April, 2015 shall be recognised in accordance with the provisions of this standard.

(2) Exchange differences arising in respect of monetary items or non-monetary items, on the settlement thereof during the previous year commencing on the 1st day of April, 2015 or on conversion thereof at the last day of the previous year commencing on the 1st day of April, 2015, shall be recognised in accordance with the provisions of this standard after taking into account the amount recognised on the last day of the previous year ending on the 31st March,2015 for an item, if any, which is carried forward from said previous year.

(3) The financial statements of foreign operations for the previous year commencing on the 1st day of April, 2015 shall be translated using the principles and procedures specified in this standard after taking into account the amount recognised on the last day of the previous year ending on the 31st March, 2015 for an item, if any, which is carried forward from said previous year.

(4) All forward exchange contracts existing on the 1st day of April, 2015 or entered on or after 1st day of April, 2015 shall be dealt with in accordance with the provisions of this standard after taking into account the income or expenses, if any, recognised in respect of said contracts for the previous year ending on or before the 31st March, 2015.

(G) Income Computation and Disclosure Standard VII relating to government grants Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of account.

In case of conflict between the provisions of the Income Tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard deals with the treatment of Government grants. The Government grants are sometimes called by other names such as subsidies, cash incentives, duty drawbacks, waiver, concessions, reimbursements, etc.

2. This Income Computation and Disclosure Standard does not deal with:—

(a) Government assistance other than in the form of Government grants; and

(b) Government participation in the ownership of the enterprise.

3. Definitions

(1) The following terms are used in the Income Computation and Disclosure Standard with the meanings specified:

(a) "Government" refers to the Central Government, State Governments, agencies and similar bodies, whether local, national or international.

(b) "Government grants" are assistance by Government in cash or kind to a person for past or future compliance with certain conditions. They exclude those forms of Government assistance which cannot have a value placed upon them and the transactions with Government which cannot be distinguished from the normal trading transactions of the person.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meaning assigned to them in the Act.

4. Recognition of Government Grants

(1) Government grants should not be recognised until there is reasonable assurance that (i) the person shall comply with the conditions attached to them, and (ii) the grants shall be received.

(2) Recognition of Government grant shall not be postponed beyond the date of actual receipt.

5. Treatment of Government Grants

Where the Government grant relates to a depreciable fixed asset or assets of a person, the grant shall be deducted from the actual cost of the asset or assets concerned or from the written down value of block of assets to which concerned asset or assets belonged to.

6. Where the Government grant relates to a non-depreciable asset or assets of a person requiring fulfillment of certain obligations, the grant shall be recognised as income over the same period over which the cost of meeting such obligations is charged to income.

7. Where the Government grant is of such a nature that it cannot be directly relatable to the asset acquired, so much of the amount which bears to the total Government grant, the same proportion as such asset bears to all the assets in respect of or with reference to which the Government grant is so received, shall be deducted from the actual cost of the asset or shall be reduced from the written down value of block of assets to which the asset or assets belonged to.

8. The Government grant that is receivable as compensation for expenses or losses incurred in a previous financial year or for the purpose of giving immediate financial support to the person with no further related costs, shall be recognised as income of the period in which it is receivable.

9. The Government grants other than covered by paragraph 5, 6, 7, and 8 shall be recognised as income over the periods necessary to match them with the related costs which they are intended to compensate.

10. The Government grants in the form of non-monetary assets, given at a concessional rate, shall be accounted for on the basis of their acquisition cost.

11. Refund of Government Grants

The amount refundable in respect of a Government grant referred to in paragraphs 6, 8 and 9 shall be applied first against any unamortised deferred credit remaining in respect of the Government grant. To the extent that the amount refundable exceeds any such deferred credit, or where no deferred credit exists, the amount shall be charged to profit and loss statement.

12. The amount refundable in respect of a Government grant related to a depreciable fixed asset or assets shall be recorded by increasing the actual cost or written down value of block of assets by the amount refundable. Where the actual cost of the asset is increased, depreciation on the revised actual cost or written down value shall be provided prospectively at the prescribed rate.

13. Transitional Provisions

All the Government grants which meet the recognition criteria of para 4 on or after 1st day of April, 2015 shall be recognised for the previous year commencing on or after 1st day of April, 2015 in accordance with the provisions of this standard after taking into account the amount, if any, of the said Government grant recognised for any previous year ending on or before 31st day of March, 2015.

14. Disclosures

Following disclosure shall be made in respect of Government grants, namely:—

(a) nature and extent of Government grants recognised during the previous year by way of deduction from the actual cost of the asset or assets or from the written down value of block of assets during the previous year;

(b) nature and extent of Government grants recognised during the previous year as income;

(c) nature and extent of Government grants not recognised during the previous year by way of deduction from the actual cost of the asset or assets or from the written down value of block of assets and reasons thereof; and

(d) nature and extent of Government grants not recognised during the previous year as income and reasons thereof.

(H) Income Computation and Disclosure Standard VIII relating to securities Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of account.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard deals with securities held as stock in-trade.

2. This Income Computation and Disclosure Standard does not deal with:

(a) the bases for recognition of interest and dividends on securities which are covered by the Income Computation and Disclosure Standard on revenue recognition;

(b) securities held by a person engaged in the business of insurance;

(c) securities held by mutual funds, venture capital funds, banks and public financial institutions formed under a Central or a State Act or so declared under the Companies Act, 1956 or the Companies Act, 2013.

3. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Fair value" is the amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm's length transaction.

(b) "Securities" shall have the meaning assigned to it in clause (h) of section 2 of the Securities Contract (Regulation) Act, 1956, other than Derivatives referred to in sub-clause (Ia) of that clause.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meaning respectively assigned to them in the Act.

4. Recognition and Initial Measurement of Securities

A security on acquisition shall be recognised at actual cost.

5. The actual cost of a security shall comprise of its purchase price and include acquisition charges such as brokerage, fees, tax, duty or cess.

6. Where a security is acquired in exchange for other securities, the fair value of the security so acquired shall be its actual cost.

7. Where a security is acquired in exchange for another asset, the fair value of the security so acquired shall be its actual cost.

8. Where unpaid interest has accrued before the acquisition of an interest-bearing security and is included in the price paid for the security, the subsequent receipt of interest is allocated between pre-acquisition and post-acquisition periods; the pre-acquisition portion of the interest is deducted from the actual cost.

9. Subsequent Measurement of Securities

At the end of any previous year, securities held as stock-in-trade shall be valued at actual cost initially recognised or net realisable value at the end of that previous year, whichever is lower.

10. For the purpose of para 9, the comparison of actual cost initially recognised and net realisable value shall be done categorywise and not for each individual security. For this purpose, securities shall be classified into the following categories, namely:

(a) shares;

(b) debt securities;

(c) convertible securities; and

(d) any other securities not covered above.

11. The value of securities held as stock-in-trade of a business as on the beginning of the previous year shall be:

(a) the cost of securities available, if any, on the day of the commencement of the business when the business has commenced during the previous year; and

(b) the value of the securities of the business as on the close of the immediately preceding previous year, in any other case.

12. Notwithstanding anything contained in para 9, 10 and 11, at the end of any previous year, securities not listed on a recognised stock exchange; or listed but not quoted on a recognised stock exchange with regularity from time to time, shall be valued at actual cost initially recognised.

13. For the purposes of para 9, 10 and 11 where the actual cost initially recognised cannot be ascertained by reference to specific identification, the cost of such security shall be determined on the basis of first-in-first-out method.

(I) Income Computation and Disclosure Standard IX relating to borrowing costs Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of account.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

(1) This Income Computation and Disclosure Standard deals with treatment of borrowing costs.

(2) This Income Computation and Disclosure Standard does not deal with the actual or imputed cost of owners' equity and preference share capital.

2. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Borrowing costs" are interest and other costs incurred by a person in connection with the borrowing of funds and include:

(i) commitment charges on borrowings;

(ii) amortised amount of discounts or premiums relating to borrowings;

(iii) amortised amount of ancillary costs incurred in connection with the arrangement of borrowings;

(iv) finance charges in respect of assets acquired under finance leases or under other similar arrangements.

(b) "Qualifying asset" means:

(i) land, building, machinery, plant or furniture, being tangible assets;

(ii) know-how, patents, copyrights, trade marks, licences, franchises or any other business or commercial rights of similar nature, being intangible assets;

(iii) inventories that require a period of twelve months or more to bring them to a saleable condition.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meaning assigned to them in the Act.

3. Recognition

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset shall be capitalised as part of the cost of that asset. The amount of borrowing costs eligible for capitalisation shall be determined in accordance with this Income Computation and Disclosure Standard. Other borrowing costs shall be recognised in accordance with the provisions of the Act.

4. For the purposes of this Income Computation and Disclosure Standard, "capitalisation" in the context of inventory referred to in item (iii) of clause (b) of sub-paragraph (1) of paragraph 2means addition of borrowing cost to the cost of inventory.

5. Borrowing Costs Eligible for Capitalisation

To the extent the funds are borrowed specifically for the purposes of acquisition, construction or production of a qualifying asset, the amount of borrowing costs to be capitalised on that asset shall be the actual borrowing costs incurred during the period on the funds so borrowed.

6. To the extent the funds are borrowed generally and utilised for the purposes of acquisition, construction or production of a qualifying asset, the amount of borrowing costs to be capitalised shall be computed in accordance with the following formula namely:—

$$A \times \frac{B}{C}$$

Where

A = borrowing costs incurred during the previous year except on borrowings directly relatable to specific purposes;

B = (i) the average of costs of qualifying asset as appearing in the balance sheet of a person on the first day and the last day of the previous year;

(ii) in case the qualifying asset does not appear in the balance sheet of a person on the first day or both on the first day and the last day of previous year, half of the cost of qualifying asset;

(iii) in case the qualifying asset does not appear in the balance sheet of a person on the last day of previous year, the average of the costs of qualifying asset as appearing in the balance sheet of a person on the first day of the previous year and on the date of put to use or completion, as the case may be, other than those qualifying assets which are directly funded out of specific borrowings; or

C = the average of the amount of total assets as appearing in the balance sheet of a person on the first day and the last day of the previous year, other than those assets which are directly funded out of specific borrowings;

7. Commencement of Capitalisation

The capitalisation of borrowing costs shall commence:

(a) in a case referred to in paragraph 5, from the date on which funds were borrowed;

(b) in a case referred to in paragraph 6, from the date on which funds were utilised.

8. Cessation of Capitalisation

Capitalisation of borrowing costs shall cease:

(a) in case of a qualifying asset referred to in item (i) and (ii) of clause (b) of subparagraph (1) of paragraph 2, when such asset is first put to use;

(b) in case of inventory referred to in item (Hi) of clause (b) of sub-paragraph (1) of paragraph 2, when substantially all the activities necessary to prepare such inventory for its intended sale are complete.

9. When the construction of a qualifying asset is completed in parts and a completed part is capable of being used while construction continues for the other parts, capitalization of borrowing costs in relation to a part shall cease:—

(a) in case of part of a qualifying asset referred to in item (i) and (ii) of clause (b) of sub-paragraph (1) of paragraph 2, when such part of a qualifying asset is first put to use;

(b) in case of part of inventory referred to in item (Hi) of clause (b) of sub-paragraph (1) of paragraph 2, when substantially all the activities necessary to prepare such part of inventory for its intended sale are complete.

10. Transitional Provisions

All the borrowing costs incurred on or after 1st day of April, 2015 shall be capitalized for the previous year commencing on or after 1st day of April, 2015 in accordance with the provisions of this standard after taking into account the amount of borrowing costs capitalised, if any, for the same borrowing for any previous year ending on or before 31st day of March, 2015.

11. Disclosure

The following disclosure shall be made in respect of borrowing costs, namely:—

(a) the accounting policy adopted for borrowing costs; and

(b) the amount of borrowing costs capitalised during the previous year.

(J) Income Computation and Disclosure Standard X relating to provisions, contingent liabilities and contingent assets

Preamble

This Income Computation and Disclosure Standard is applicable for computation of income chargeable under the head "Profits and gains of business or profession" or "Income from other sources" and not for the purpose of maintenance of books of accounts.

In the case of conflict between the provisions of the Income-tax Act, 1961 ('the Act') and this Income Computation and Disclosure Standard, the provisions of the Act shall prevail to that extent.

1. Scope

This Income Computation and Disclosure Standard deals with provisions, contingent liabilities and contingent assets, except those:

(a) resulting from financial instruments;

(b) resulting from executory contracts;

(c) arising in insurance business from contracts with policyholders; and

(d) covered by another Income Computation and Disclosure Standard.

2. This Income Computation and Disclosure Standard does not deal with the recognition of revenue which is dealt with by Income Computation and Disclosure Standard - Revenue Recognition.

3. The term 'provision' is also used in the context of items such as depreciation, impairment of assets and doubtful debts which are adjustments to the carrying amounts of assets and are not addressed in this Income Computation and Disclosure Standard.

4. Definitions

(1) The following terms are used in this Income Computation and Disclosure Standard with the meanings specified:

(a) "Provision" is a liability which can be measured only by using a substantial degree of estimation.

(b) "Liability" is a present obligation of the person arising from past events, the settlement of which is expected to result in an outflow from the person of resources embodying economic benefits.

(c) "Obligating event" is an event that creates an obligation that results in a person having no realistic alternative to settling that obligation.

(d) "Contingent liability" is:

(i) a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or nonoccurrence of one or more uncertain future events not wholly within the control of the person; or

(ii) a present obligation that arises from past events but is not recognised because:

A. it is not reasonably certain that an outflow of resources embodying economic benefits will be required to settle the obligation; or

B. a reliable estimate of the amount of the obligation cannot be made.

(e) "Contingent asset" is a possible asset that arises from past events the existence of which will be confirmed only by the occurrence or nonoccurrence of one or more uncertain future events not wholly within the control of the person.

(f) "Executory contracts" are contracts under which neither party has performed any of its obligations or both parties have partially performed their obligations to an equal extent.

(g) "Present obligation" is an obligation if, based on the evidence available, its existence at the end of the previous year is considered reasonably certain.

(2) Words and expressions used and not defined in this Income Computation and Disclosure Standard but defined in the Act shall have the meaning respectively assigned to them in the Act.

Recognition

5. Provisions

A provision shall be recognised when:

(a) a person has a present obligation as a result of a past event;

(b) it is reasonably certain that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision shall be recognised.

6. No provision shall be recognised for costs that need to be incurred to operate in the future.

7. It is only those obligations arising from past events existing independently of a person's future actions, that is the future conduct of its business, that are recognised as provisions.

8. Where details of a proposed new law have yet to be finalised, an obligation arises only when the legislation is enacted.

9. Contingent Liabilities

A person shall not recognise a contingent liability.

10. Contingent Assets

A person shall not recognise a contingent asset.

11. Contingent assets are assessed continually and when it becomes reasonably certain that inflow of economic benefit will arise, the asset and related income are recognised in the previous year in which the change occurs.

Measurement

12. Best Estimate

The amount recognised as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the previous year. The amount of a provision shall not be discounted to its present value.

13. The amount recognised as asset and related income shall be the best estimate of the value of economic benefit arising at the end of the previous year. The amount and related income shall not be discounted to its present value.

14. Reimbursements

Where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement shall be recognised when it is reasonably certain that reimbursement will be received if the person settles the obligation. The amount recognised for the reimbursement shall not exceed the amount of the provision.

15. Where a person is not liable for payment of costs in case the third party fails to pay, no provision shall be made for those costs.

16. An obligation, for which a person is jointly and severally liable, is a contingent liability to the extent that it is expected that the obligation will be settled by the other parties.

17. Review

Provisions shall be reviewed at the end of each previous year and adjusted to reflect the current best estimate. If it is no longer reasonably certain that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision should be reversed.

18. An asset and related income recognised as provided in para 11 shall be reviewed at the end of each previous year and adjusted to reflect the current best estimate. If it is no longer reasonably certain that an inflow of economic benefits will arise, the asset and related income shall be reversed.

19. Use of Provisions

A provision shall be used only for expenditures for which the provision was originally recognised.

20. Transitional Provisions

All the provisions or assets and related income shall be recognised for the previous year commencing on or after 1st day of April, 2015 in accordance with the provisions of this standard after taking into account the amount recognised, if any, for the same for any previous year ending on or before 31st day of March, 2015.

21. Disclosure

(1) Following disclosure shall be made in respect of each class of provision, namely:

(a) a brief description of the nature of the obligation;

(b) the carrying amount at the beginning and end of the previous year;

(c) additional provisions made during the previous year, including increases to existing provisions;

(d) amounts used, that is incurred and charged against the provision, during the previous year;

(e) unused amounts reversed during the previous year; and

(f) the amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.

(2) Following disclosure shall be made in respect of each class of asset and related income recognised as provided in para 11, namely:—

(a) a brief description of the nature of the asset and related income;

(b) the carrying amount of asset at the beginning and end of the previous year;

(c) additional amount of asset and related income recognised during the year, including increases to assets and related income already recognised; and

(d) amount of asset and related income reversed during the previous year.

Study Note - 10

DOUBLE TAXATION RELIEF

This Study Note includes

10.1 AGREEMENT WITH FOREIGN COUNTRIES OR SPECIFIED TERRITORIES [SECTION 90]

(1) The Central Government may enter into an agreement with the Government of any country outside India or specified territory outside India-

(a) for the granting of relief in respect of-

(i) income on which have been paid both income-tax under this Act and income-tax in that country or specified territory, as the case may be, or

(ii) income-tax chargeable under this Act and under the corresponding law in force in that country or specified territory, as the case may be, to promote mutual economic relations, trade and investment, or

(b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that country or specified territory, as the case may be, or

(c) for exchange of information for the prevention of evasion or avoidance of income-tax chargeable under this Act or under the corresponding law in force in that country or specified territory, as the case may be, or investigation of cases of such evasion or avoidance, or

(d) for recovery of income-tax under this Act and under the corresponding law in force in that country or specified territory, as the case may be, and may, by notification in the Official Gazette, make such provisions as may be necessary for implementing the agreement.

(2) Where the Central Government has entered into an agreement with the Government of any country outside India or specified territory outside India, as the case may be, under sub-section (1) for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

(2A) Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee even if such provisions are not beneficial to him.

(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.

(4) An assessee, not being a resident, to whom an agreement referred to in sub-section (1) applies, shall not be entitled to claim any relief under such agreement unless a certificate of his being a resident in any country outside India or specified territory outside India, as the case may be, is obtained by him from the Government of that country or specified territory.

(5) The assessee referred to in sub-section (4) shall also provide such other documents and information, as may be prescribed.

Explanation 1 -For the removal of doubts, it is hereby declared that the charge of tax in respect of a foreign company at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such foreign company.

Explanation 2 -For the purposes of this section, "specified territory" means any area outside India which may be notified as such by the Central Government.

Explanation 3 -For the removal of doubts, it is hereby declared that where any term is used in any agreement entered into under sub-section (1) and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued under sub-section (3) and the notification issued thereunder being in force, then, the meaning assigned to such term shall be deemed to have effect from the date on which the said agreement came into force.

Concept of Business Connection and Permanent Establishment: The liability to tax in the source country generally arises out of "Business Connection" or through what is called "Permanent Establishment". Most of the agreements spell out what they regard as "Permanent Establishment" as this is of utmost importance while fixing the tax liability. These agreements also lay down maximum limits of tax that can be levied or withheld and the manner in which it can be levied.

Meaning of business connection [Explanation 2 to section 9(1)]: For the removal of doubts, it is hereby declared that "business connection" shall include any business activity carried out through a person who, acting on behalf of the non-resident,—

(a) has and habitually exercises in India, an authority to conclude contracts on behalf of the non-resident, unless his activities are limited to the purchase of goods or merchandise for the non-resident; or

(b) has no such authority, but habitually maintains in India a stock of goods or merchandise from which he regularly delivers goods or merchandise on behalf of the non-resident; or

(c) habitually secures orders in India, mainly or wholly for the non-resident or for that non-resident and other non-residents controlling, controlled by, or subject to the same common control, as that non-resident.

However, such business connection shall not include any business activity carried out through a broker, general commission agent or any other agent having an independent status, if such broker, general commission agent or any other agent having an independent status is acting in the ordinary course of his business.

Further, where such broker, general commission agent or any other agent works mainly or wholly on behalf of a non-resident (hereafter in this proviso referred to as the principal non-resident) or on behalf of such non-resident and other non-residents which are controlled by the principal non-resident or have a controlling interest in the principal nonresident or are subject to the same common control as the principal non-resident, he shall not be deemed to be a broker, general commission agent or an agent of an independent status.

The concept of Permanent Establishment is one of the most important concepts in determining the tax implications of cross border transactions. The term Permanent Establishment (PE) postulates existence of a substantial element of an enduring or permanent nature of a foreign enterprise in another country which can be attributed to a fixed place of business in that country.

Article 5(1) of the DTAA provides that for the purpose of this convention the term 'Permanent Establishment (PE)' means a fixed place of business through which the business of an enterprise is wholly or partly carried in.

Accordingly Article 5(2) enumerates various instances of PE. The term PE includes (a) a place of management (b) a branch (c) an office (d) a factory (e) a workshop (f) a sales outlet (g) a warehouse (h) a mine, a oil or gas well, a quarry or other place of extraction of natural resources.

Business income of a non resident will not be taxed in India unless such non-resident has a permanent establishment in India.

Thus if there is no double taxation agreement with the country of which the non-resident in India is a resident, we will see his business connection in India and tax such income in India to the extent such income is attributable to business connection in India. On the other hand, if there is a double taxation avoidance agreement with the country of which the non-resident in India is a resident, we will see whether such non-resident has Permanent Establishment (PE) in India as per Article 5 of the treaty. If he has PE in India, then Article 7 of treaty shall apply to tax such income in India.

DTAA overrides the provision of Income-tax Act: Where an entity does not fall within the meaning of "permanent establishment" as per the DTAA, it cannot be taxed in India by virtue of its business connection as per Explanation 2 to section 9(1)(i) as in the particular case, DTAA provided that income of non-resident shall be taxable only when it has permanent establishment in India. If such non-resident has business connection in India, such income shall not be taxable in India. Therefore, even though the foreign publishing house has business connection in India, since the applicant is not covered by the definition of 'PE' as contained in article 5 of the DTAA, the publishing house is not liable to tax under the treaty [Speciality Magazines Pvt. Ltd, In re (2005) 274 ITR 310 (AAR - New Delhi)].

Residential status under Double Tax Avoidance Agreement is generally decided in the case of a company not with reference to the place of incorporation, but with reference to the place of "effective management" [Integrated Container Feeder Service vs. Joint CIT (2005) 278 ITR (AT) 182 (Mumbai)].

The applicant is a company incorporated in the UAE. The applicant company is engaged in offering remittance services for transferring amounts from UAE to India on commission basis. It received the entire commission in UAE. The company was granted licence by the RBI for setting up liaison offices in India for undertaking certain approved activities. The activities of the liaison office were:

(a) Attending to complaint of clients in cases where remittances are sent directly to banks in India; and

(b) Downloading information from internet, printing cheques/drafts in the name of beneficiaries and sending them through couriers to various places in India in cases where the applicant has to be remit amounts to beneficiaries in India.

As regards the first activity, where the amount is directly transferred, the liaison office has no role to play except to attend to complaints of clients. This work is of auxiliary nature, and so the applicant is exempted from constituting a Permanent Establishment (PE) as per the DTAA between India and UAE. However, as regards the second activity, the liaison office performs an important part of the main work since the performance of the contract would not be complete without remittance of the amount to the beneficiaries. Therefore, the liaison office undertaking this work would constitute PE of the applicant. In such a case, that portion of the profits which is attributable to the liaison office (PE) is deemed to accrue to the applicant in India, and hence, would be taxable in India [UAE Exchange Centre, In re (2004) 268 ITR 9 (AAR-New Delhi)].

10.2 ADOPTION BY CENTRAL GOVERNMENT OF AGREEMENT BETWEEN SPECIFIED ASSOCIATIONS FOR DOUBLE TAXATION RELIEF [SECTION 90A]

(1) Any specified association in India may enter into an agreement with any specified association in the specified territory outside India and the Central Government may, by notification in the Official Gazette, make such provisions as may be necessary for adopting and implementing such agreement-

 (a) for the granting of relief in respect of-

  (i) income on which have been paid both income-tax under this Act and income-tax in any specified territory outside India; or

(ii) income-tax chargeable under this Act and under the corresponding law in force in that specified territory outside India to promote mutual economic relations, trade and investment, or

(b) for the avoidance of double taxation of income under this Act and under the corresponding law in force in that specified territory outside India, or

(c) for exchange of information for the prevention of evasion or avoidance of income- tax chargeable under this Act or under the corresponding law in force in that specified territory outside India, or investigation of cases of such evasion or avoidance, or

(d) for recovery of income-tax under this Act and under the corresponding law in force in that specified territory outside India.

(2) Where a specified association in India has entered into an agreement with a specified association of any specified territory outside India under sub-section (1) and such agreement has been notified under that sub-section, for granting relief of tax, or as the case may be, avoidance of double taxation, then, in relation to the assessee to whom such agreement applies, the provisions of this Act shall apply to the extent they are more beneficial to that assessee.

(2A) Notwithstanding anything contained in sub-section (2), the provisions of Chapter X-A of the Act shall apply to the assessee even if such provisions are not beneficial to him.

(3) Any term used but not defined in this Act or in the agreement referred to in sub-section (1) shall, unless the context otherwise requires, and is not inconsistent with the provisions of this Act or the agreement, have the same meaning as assigned to it in the notification issued by the Central Government in the Official Gazette in this behalf.

(4) An assessee, not being a resident, to whom the agreement referred to in sub-section (1) applies, shall not be entitled to claim any relief under such agreement unless a certificate of his being a resident in any specified territory outside India, is obtained by him from the Government of that specified territory.

(5) The assessee referred to in sub-section (4) shall also provide such other documents and information, as may be prescribed.

Explanation 1- For the removal of doubts, it is hereby declared that the charge of tax in respect of a company incorporated in the specified territory outside India at a rate higher than the rate at which a domestic company is chargeable, shall not be regarded as less favourable charge or levy of tax in respect of such company.

Explanation 2 -For the purposes of this section, the expressions-

(a) "specified association" means any institution, association or body, whether incorporated or not, functioning under any law for the time being in force in India or the laws of the specified territory outside India and which may be notified as such by the Central Government for the purposes of this section;

(b) "specified territory" means any area outside India which may be notified as such by the Central Government for the purposes of this section.

Explanation 3 -For the removal of doubts, it is hereby declared that where any term is used in any agreement entered into under sub-section (1) and not defined under the said agreement or the Act, but is assigned a meaning to it in the notification issued under sub-section (3) and the notification issued there-under being in force, then, the meaning assigned to such term shall be deemed to have effect from the date on which the said agreement came into force.

10.3 COUNTRIES WITH WHICH NO AGREEMENT EXISTS [SECTION 91]

(1) If any person who is resident in India in any previous year proves that, in respect of his income which accrued or arose during that previous year outside India (and which is not deemed to accrue or arise in India), he has paid in any country with which there is no agreement under section 90 for the relief or avoidance of double taxation, income-tax, by deduction or otherwise, under the law in force in that country, he shall be entitled to the deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

(2) If any person who is resident in India in any previous year proves that in respect of his income which accrued or arose to him during that previous year in Pakistan he has paid in that country, by deduction or otherwise, tax payable to the Government under any law for the time being in force in that country relating to taxation of agricultural income, he shall be entitled to a deduction from the Indian income-tax payable by him-

(a) of the amount of the tax paid in Pakistan under any law aforesaid on such income which is liable to tax under this Act also; or

(b) of a sum calculated on that income at the Indian rate of tax;

whichever is less.

(3) If any non-resident person is assessed on his share in the income of a registered firm assessed as resident in India in any previous year and such share includes any income accruing or arising outside India during that previous year (and which is not deemed to accrue or arise in India) in a country with which there is no agreement under section 90 for the relief or avoidance of double taxation and he proves that he has paid income-tax by deduction or otherwise under the law in force in that country in respect of the income so included he shall be entitled to a deduction from the Indian income-tax payable by him of a sum calculated on such doubly taxed income so included at the Indian rate of tax or the rate of tax of the said country, whichever is the lower, or at the Indian rate of tax if both the rates are equal.

Explanation -In this section,-

(i) the expression "Indian income-tax" means income-tax charged in accordance with the provisions of this Act;

(ii) the expression "Indian rate of tax" means the rate determined by dividing the amount of Indian income-tax after deduction of any relief due under the provisions of this Act but before deduction of any relief due under this Chapter, by the total income;

(iii) the expression "rate of tax of the said country" means income-tax and super-tax actually paid in the said country in accordance with the corresponding laws in force in the said country after deduction of all relief due, but before deduction of any relief due in the said country in respect of double taxation, divided by the whole amount of the income as assessed in the said country;

(iv) the expression "income-tax" in relation to any country includes any excess profits tax or business profits tax charged on the profits by the Government of any part of that country or a local authority in that country.

10.4 TAX RESIDENCY CERTIFICATE [TRC] [Section 90 & 90A]

For claiming relief under DTAA – section 90 & 90A empowers the Central Government to enter into Double Taxation Avoidance Agreement with the foreign countries / foreign territories.

With effect from 1st April 2013, to avail the benefit, submission of TRC would be necessary.

A simple certificate of being resident of a country is required to avail the benefits of DTAA.

10.5 CERTAIN SPECIAL CASES

Taxation of Business process outsourcing units in India

The provisions containing taxation of IT-enabled business process outsourcing units are not contained the Income-tax Act, 1961 but are given in Circular No. 5/2004 dated 28-9-2004 issued by the CBDT which is as under:

(1) A non-resident entity may outsource certain services to a resident Indian entity. If there is no business connection between the two, the resident entity may not be a Permanent Establishment of the non-resident entity, and the resident entity would have to be assessed to income-tax as a separate entity. In such a case, the non-resident entity will not be liable under the Income-tax Act, 1961.

(2) However, it is possible that the non-resident entity may have a business connection with the resident Indian entity. In such a case, the resident Indian entity could be treated as the Permanent Establishment of the non-resident entity. The tax treatment of the Permanent Establishment in such a case is under consideration in this circular.

(3) During the last decade or so, India has seen a steady growth of outsourcing of business processes by non-residents or foreign companies to IT-enabled entities in India. Such entities are either branches or associated enterprises of the foreign enterprise or an independent Indian enterprise. Their activities range from mere procurement of orders for sale of goods or provision of services and answering sales related queries to the provision of services itself like software maintenance service, debt collection service, software development service, credit card/mobile telephone related service, etc. The non-resident entity or the foreign company will be liable to tax in India only if the IT-enabled BPO unit in India constitutes its Permanent Establishment. The extent to which the profits of the non-resident enterprise are to be attributed to the activities of such Permanent Establishment in India has been under consideration of the Board.

(4) A non-resident or a foreign company is treated as having a Permanent Establishment in India under Article 5 of the Double Taxation Avoidance Agreements entered into by India with different countries if the said non-resident or foreign company carries on business in India through a branch, sales office, etc. or through an agent (other than an independent agent) who habitually exercises an authority to conclude contracts or regularly delivers goods or merchandise or habitually secures orders on behalf of the non-resident principal. In such a case, the profits of the non-resident or foreign company attributable to the business activities carried out in India by the Permanent Establishment becomes taxable in India under Article 7 of the Double Taxation Avoidance Agreements.

(5) Paragraph 1 of Article 7 of Double Taxation Avoidance Agreements provides that if a foreign enterprise carries on business in another country through a Permanent Establishment situated therein, the profits of the enterprise may be taxed in the other country but only so much of them as are attributable to the Permanent Establishment. Paragraph 2 of the same Article provides that subject to the provisions of Paragraph 3, there shall in each contracting state be attributed to that Permanent Establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing independently with the enterprise of which it is a Permanent Establishment. Paragraph 3 of the Article provides that in determining the profits of a Permanent Establishment there shall be allowed as deductions expenses which are incurred for the purposes of the Permanent Establishment including executive and general administrative expenses so incurred, whether in the State in which the Permanent Establishment is situated or elsewhere. The expenses that are deductible would have to be determined in accordance with the accepted principles of accountancy and the provisions of the Income-tax Act, 1961.

(6) Paragraph 2 contains the central directive on which the allocation of profits to a Permanent Establishment is intended to be based. The paragraph incorporates the view that the profits

to be attributed to a Permanent Establishment are those which the Permanent Establishment would have made if, instead of dealing with its Head Office, it had been dealing with an entirely separate enterprise under conditions and at prices prevailing in the ordinary market. This corresponds to the "arm's length principle". Paragraph 3 only provides a rule applicable for the determination of the profits of the Permanent Establishment, while paragraph 2 requires that the profits so determined correspond to the profit that a separate and independent enterprise would have made. Hence, in determining the profits attributable to an IT-enabled BPO unit constituting a Permanent Establishment, it will be necessary to determine the price of the services rendered by the Permanent Establishment to the Head office or by the Head office to the Permanent Establishment on the basis of "arm's length principle".

(7) "Arm's length price" would have the same meaning as in the definition in section 92F(iii) of the Income-tax Act. The arm's length price would have to be determined in accordance with the provisions of sections 92 to 92F of the Income-tax Act.

(8) The CBDT Circular No. 1/2004, dated 2.1.2004 is hereby withdrawn with immediate effect [Circular No. 5/2004, dated 28.9.2004].

Dividend: Dividend is taxed in the country where the company is incorporated, the other country foregoing the tax thereon even if the dividend income is to be assessed under the relevant laws of that country. Incorporation of the company itself may well depend upon the country, choice of those in control and management, so as to avail a lesser rate of tax. India taxed non-residents on dividend at 20%, before dividend distribution tax was introduced. The range of tax in most countries is 10% to 20%.

Interest: Under the most Double Taxation Avoidance Agreement, rate of tax on interest is 10% but may range from 10% to 20% with a nominal variation for Syria which is 7.5%. Domestic rate of tax itself was 10% for foreign direct loan utilized in India now, by an amendment by the Finance Act, 2012, reduced to 5% from A.Y.2013-2014, so that one has not to look to Double Taxation Avoidance Agreement for relief in most cases.

Royalty: Royalty for supply of technical know-how, patents or other intellectual property rights is most common occurrence in most collaboration agreements with India taxing such royalty at 30% where agreements were made before 31st day of March, 1997, at 20% where agreements were made on or after 1st day of April, 1997 up to 31st day of May, 2005 and finally reduced to 10% where agreements were made on or after 1st day of June, 2005.

Definition of 'royalty' requires attention because of amendment expanding the meaning of royalty with retrospective effect from 1.6.1976. The definition vide Explanations 4, 5 and 6 of section 9(1)(vi) as it stands after amendment made by the Finance Act, 2012, reads as follows:

Explanation 4 — For the removal of doubts, it is hereby clarified that the transfer of all or any rights in respect of any right/property/information includes and has always included transfer of all or any right for use or right to use a computer software (including granting of a licence) irrespective of the medium through which such right is transferred.

Explanation 5 — For the removal of doubts, it is hereby clarified that the royalty includes and has always included consideration in respect of any right, property or information, whether or not—

(a) the possession or control of such right/property/information is with the payer;

(b) such right/property/information is used directly by the payer;

(c) the location of such right/property/information is in India.

Explanation 6 — For the removal of doubts, it is hereby clarified that the expression "process" includes and shall be deemed to have always included transmission by satellite (including up-linking, amplification, conversion for down-linking of any signal), cable, optic fibre or by any other similar technology, whether or not such process is secret.

But in most countries in respect of supplies on royalty basis the rate of tax is low at 10% so as to encourage development of technology. In respect of some countries the rate is lower, if it is in connection with supply of scientific or technical services.

According to the Amendments made by Finance Act, 2013, the tax rate, in case of non-resident tax payer, in respect of income by way of royalty as provided u/s 115A, shall be 25%.

Technical Fees: Explanation 2 to section 9(1)(vii) defines "fee for technical services", which reads as under:

"Fees for Technical Services" means any consideration including any lump sum consideration for the rendering of any managerial, technical or consultancy services including the provision of services of technical or other personnel but does not include consideration for any construction, assembly, mining or like project undertaken by the recipient or consideration which would be income of the recipient chargeable under the head "Salaries".

Regular agreements or protocols relating to copyright, patents, designs, etc., may provide for sharing of R&D services or provide for assistance by deputation of personnel and even for undertaking training. Services may be rendered either from the home country or in the host country with the result that the identification of the income accruing in respective countries under the local laws may present a problem as it has happened in a number of cases in India. the technical fees of non-residents is taxed by Indian Laws at 20% where agreements were made up to 31.5.2005 and 10% thereafter.

The Finance Act, 2013 has increased the rate to 25%.

The interpretation of the Department with reference to definition of technical fees u/s 9(1)(vii) has been that any use of such technical service in India would attract tax at the domestic rate, even if the entire service is rendered abroad.

Hence, the country with which Indian importer of technical know-how makes an agreement may make vital difference to the non-resident's liability which is relevant for the Indian taxpayer either because he bears such tax under the agreement or such tax forms the component of the amount which he has agreed to pay with the result that it is always the burden of the taxpayer in the market where demand overruns supply.

Where tax rate under the agreement is lower than the domestic rate, the non-resident is entitled to be taxed at such lower rate under the agreement [CIT vs. Reiter Ingolsteadt Spinnereimaschinenbau AG, (2006) 285 ITR 199 (Mad)].

In case the inference of technical service fails, royalty may be sought to be inferred. Royalty in respect of technical know-how should be one, which is capable of being patented and even if not patented, it should be a matter of purveyance of not mere knowledge, but of technique. If it were knowledge, it should be special knowledge, not a matter of public property. A copyrighted article may be sold without attracting the inference of royalty, but copyright itself can be transferred only subject to royalty.

There has been considerable controversy with conflicting decisions of courts in respect of licensed software with Delhi High Court taking the view in Director of Income Tax vs. Ericsson A.B. New Delhi (2012) 343 ITR 470 (Del.), and Karnataka High Court in CIT (International Taxation) vs. Samsung Electronics Co. Ltd. (2011) 203 Taxman 477 (Karn) with Authority for Advance Ruling earlier taking the view favourable to the taxpayer in CIT vs. Dynamic Vertical Software India (P) Ltd. (2011) 332 ITR 222 (Del.), and later in favour of revenue in Dassault Systems K.K. In re (2010) 322 ITR 125 (AAR), Citrix Systems Asia Pacific Ltd. In re (2012) 343 ITR 1 (AAR) and Acclerys K.K. In re (2012) 343 ITR 304 (AAR). A retrospective amendment with effect from 1.6.1976 to section 9(1)(vi) by the Finance Act, 2012 would treat any payment for licensed software to be royalty. Other amendments to the definition of royalty on one hand and the Explanations 4 and 5 to section 9(1)(i) by providing for "look through" and by targeting "underlying assets" have similar effect of experiencing tax base under the domestic law without any impact on Double Taxation Avoidance Agreement in view of Treaty Override, which is specifically recognised by dropping the proposal for amendment to section 96(2) for such override by way of amending the Finance Bill, 2012 before it became law.

Explanation under section 9(2), as substituted by the Finance Act, 2010 with retrospective effect from 1st June, 1976, would seek to clarify that inference of liability u/s 9 does not depend upon place of residence, business connection or service in India. It could apply more appropriately for royalty and technical fee.

Salary: An employee of a non-resident company in India working for such company will become a resident, if he stays in India for 183 days, so that his salary may accrue in India. But where such salary was not borne by a permanent establishment of the non-resident in India and it was paid abroad, such salary income could not be taxable under Double Taxation Avoidance Agreement as was rendered in the context of Agreement between India and such other country.

Conducting Examination in India: A non-resident non-profit organisation was conducting examination through an agent in India without itself having an office in India, besides conducting training programmes on subjects like corporate training, management, consultancy, publishing and trading in educational materials, etc. Authority for Advance Rulings ruled that the applicant for ruling was a non-resident being a tax resident of US and a non-profit organisation was spared liability by the Double Taxation Avoidance Agreement between India and US, in Knowerx Education (India) P. Ltd., In re (2008) 301 ITR 207 (AAR). Indian company, however, could not be treated as an agent of the non-resident, since it was not concluding contracts on behalf of the non-resident. It could not also be treated as a dependent agency, since it enjoyed independent status. The acceptance of candidature of an individual for a certification in the examination was solely by the non-resident. It was further found that the nature of service was such that it could only be characterised as business, so that it falls under Article 7 of the Indo-US Agreement with liability for non-resident, if the non-resident has a permanent establishment in India, in which case, the income attributable to such PE would have become taxable. It follows that the applicant was not liable to deduct tax at source from payments made by it or routed through it.

Consultancy Services: In case marketing consultancy service is involved, it may not be construed as technical service either in the definition of 'technical service' in Explanation to section 9(1)(vii) or in the relevant Article 12 relating to royalty and technical fees under Double Taxation Avoidance Agreement. What is contemplated in such cases is purely one of marketing of service abroad, if such service is confined outside India. Payment for such service is on par with common sales not liable to tax in India, if services are rendered abroad [CIT vs. Toshoku Ltd. (1980) 125 ITR 525 (SC)].

The interpretation placed by the Tribunal in Deputy CIT vs. Boston Consulting Group P. Ltd. (2006) 280 ITR (AT)1(Mumbai) is more in keeping with the understanding that business of consultancy service is non-technical in nature, so that it may not be treated as royalty and technical fees, but only as professional services. Merely because such services are used in India, the income, there from, does not become taxable either under the domestic law in India or as royalty and technical fees under Double Taxation Avoidance Agreement.

The Delhi Bench of the Tribunal, in Sheraton International Inc. vs. Dy. Director of Income Tax(2007) 293 ITR (AT) 68, also understood the law on the subject in the same manner.

The Supreme Court by a Bench of three Judges in Barendra Prasad Ray vs. ITO(1981) 129 ITR 295 (SC) has decided on professional service in law, where a UK barrister came to India for discussions and had also appeared in a matter pending in Calcutta High Court along with the counsel entitled to appear before the High Court. The duration of the hearing was 13 days. The payment was made by his client, the German Corporation, which was interested in the suit. The Assessing Officer sought to treat the Indian company as agent of the German Corporation and sought to recover the tax payable by its lawyer. The issue which arose for consideration was whether there was any business connection which was real and intimate and not merely casual. The Supreme Court held that the visit was not casual and that the relationship with Indian company was such as to make it responsible for the liability of the lawyer, who assisted it. There was a business connection which would include within its scope profession, vocation and callings.

Where partners of a law firm stayed in India and rendered legal service for more than 90 days, the professional income of the firm was liable to be taxed in India under the agreement between India and U.K. But the reason given was that it was technical service as the legal assistance related to certain technical projects, the details of which were not made available by the assessee. The decision accords with law in the light of Article 15 dealing with Independent Personal Service.

A foreign company is not liable to tax in India. Mere provision of a data base by a non-resident, where data server is located outside India, since it does not constitute technical service. Since payment is not taxable, there is no duty to deduct tax. In the absence of a permanent establishment of the non-resident in India, there could be no liability for the non-resident on any part of the business income arising from such receipts from India. This decision of the Tribunal follows a number of precedents as in CIT vs. HEG Ltd. (2003) 263 ITR 230 (MP) holding that mere lending of information cannot give rise to inference of liability. The argument of the revenue that such payment could be royalty and/or fees for technical services either u/s 9(1)(vi) and/or 9(1)(vii) and corresponding Article in the Double Taxation Avoidance Agreement as well was not accepted.

In Wallace Pharmaceuticals P. Ltd. In re, (2005) 278 ITR 97 (AAR) the question related to the place of accrual of consultant's fees for consultancy services rendered abroad but utilised in India. The non-resident carried out services admittedly abroad inter alia engaging professionals for getting orders. Since it involved getting professional service like identification of potential market for the assessee's products, search for marketable products which could be manufactured by the assessee and such other services, such service was treated as technical service under the domestic law as understood u/s 9(1)(vii) of the Income Tax Act, so that the fact that such service is utilized in India should be sufficient for attracting tax. Tax was, therefore, required to be deducted at source.

A non-resident was giving consultancy service to a mine owner, where such consultancy related to analysis of samples and ores conducted in a technical laboratory in Canada. In South West Mining Ltd. In re, (2005) 278 ITR 233 (AAR) the issue was whether such consultancy fees paid in foreign currency abroad would be taxable in India. Technical consultants were also to visit India for collecting random samples at the mine head with the assessee bearing their expenses and providing necessary assistance and facilities. The AAR found that the consultancy service may fall to be assessed within the meaning of fees for technical service under Explanation 2 to section 9(1)(vii)(b) of the Income Tax Act. It was not saved, because it was neither salary nor any consideration for any construction, assembly, mining or like project. The word "consultancy" appearing in section 9(1)(vii), it was ruled, would have application, since the fact that such service is used in India would itself attract liability.

Klaus Vogel in Double Taxation Conventions would point out that the term "technical assistance" has not been clearly defined. It ordinarily implies imparting knowledge and supplying solutions in operation of equipments or providing staff for such operations. The fact that royalties and technical fees are included in the same Article in the Agreement is a pointer to the interpretation. In this position of law, both the domestic law and the Double Taxation Avoidance Agreement, a consultancy service should be more than giving data analysis of the product primarily carried out abroad, so that no part of such income may be liable in India. The fact that the technical consultant may be visiting India for taking random samples or that the report of the analysis may be used in India may not be conclusive, since the use is not for operations, which alone would ordinarily amount to technical service. The ruling in South West Mining's case (supra) would need review.

Foreign Branch Losses in the case of a Resident: The assessee, who is a resident and ordinarily resident in India is assessable on his global income. It follows that loss in foreign branch has to be set-off against other income of the assessee. Where the Assessing Officer sought to apply the provisions of the Double Taxation Avoidance Agreement between India and Japan to disallow the loss of the branch located in Japan, it was held, in Dy. CIT vs. Patni Computer Systems Limited, (2008) 301 ITR (AT) 60 (Pune), that the assessee is entitled to the benefit of either domestic law or Double Taxation Avoidance Agreement, whichever is more favourable to it. On this reasoning, based on Treaty Override, it is also open to the assessee to claim protection of Double Taxation Avoidance Agreement in a later year, when there is profit. Such claim cannot be barred, merely because of different treatment of loss in an earlier year.

Internet Access: Advance Ruling Authority, had ruled on information technology in cross-border transactions. The non-resident was having travel business issuing international credit cards, travellers' cheques and providing other travel related services through a worldwide data network maintained in Hong Kong. The act work supplied information through telephonic and microwave devices as to the transactions in India, through a computer linked with the network for an Indian company, which was rendering service to other group companies with the Indian company by passing on the information to Hong Kong for communication and for this purpose it had leased online facilities from VSNL. The Indian company though not a direct subsidiary of the American company was a subsidiary of its subsidiary, so that it has been described as sub-subsidiary. It is on these facts, the issue was whether the amount paid by the Indian sub-subsidiary to the applicant for advance ruling, an American company, for use of software and equipment could be called royalty. If it were royalty, it would be taxable in India vide Explanation 2 to section 9(1)(vi) and should be liable to Indian tax even under the Double Taxation Avoidance Agreement by following the source rule. The Authority for Advance Rulings found that the transaction involved a high degree of technical content, which could be described as intellectual property, so that the payment for the use of the same would partake of the character of royalty. There is secrecy involved in respect of transactions of the customers, while analytical data processing is also inevitable. Even that part of the definition covering the right to use "any industrial, commercial or scientific equipment" would also cover such payment. There is liability under Article 12 of the Agreement between the U. S. and India.

In Cargo Community Nehvork Pte. Ltd., In re(2007) 289 ITR 355 (AAR), the payment for access to internet based air cargo portals outside India, it was ruled, would be royalty, because it is not a payment merely for getting access to data, but use of the portal for booking cargo, besides training of subscribers and rendering help connected therewith. The decision could have been different, since the material part of agreement was for right to use technical equipment, so that it does not mean that technology gets transferred or that it constitutes a payment for royalty as held in CIT vs. HEG Ltd. (2003) 263 ITR 230 (MP). The provision of cellular mobile telephone services was held to be a service, which did not have the character of technical service. The Tribunal, in Wipro Ltd. vs. ITO (2005)278 ITR (AT) 57 (Bang) had held that payment to a foreign publishing house for access to certain data could not amount to royalty.

In case the software involves copyrighted technology with the right to use being limited to a particular server platform and the licence fee to be paid to the non-resident depends upon the extent of use limited to the licensed purposes with supporting technical service without extra charges, it should have the character of royalty. It would be royalty even within the meaning of the Double Taxation Avoidance Agreement between India and U.S. It was found that the decision in Dun and Bradstreet Espana S.A., In re (2005) 272 ITR 99 (AAR), which relates to payment merely for information, would have no application to the facts of the assessee's case, so that liability as royalty for the non-resident and consequent liability for the resident to deduct tax at source are absent.

The services, where conveyed through satellite communication may well be covered, so as to be taxable as royalty in view of Explanation 6 to section 9(1)(vi) inserted with retrospective effect from 1.6.1976. However, the interpretation for purposes of Double Taxation Avoidance Agreement is not covered by the amendment.

Logistic Survey: A payment made to a non-resident for reconnaissance of minerals made by a resident licensee for prospecting of mining for diamonds and other minerals was held to be not for technical service. Activities were collection of samples, geophysical survey by use of airborne multispectral scanner and electromagnetic equipment with such exploration being considered at different stages, made available with a team of experts making reports from time to time. The Tribunal reasoned, that though knowledge and expertise were involved, such knowledge and expertise themselves were not made available to the resident assessee. The data collected were further processed by use of software technology, which was not made available. The resident assessee was merely supplied with computer readable conclusions from data collected. This was an agreement for mere service and not for transfer of technology. Reports and maps only contain data, which could not also be treated as technical plan or technical design. Incidentally, it was also interpreted, that the language in Article 12(5)(b) pointing out that two activities of service or supply of technology are linked by the word "or", which is to be understood conjointly and not disjunctively. The decision follows the stricter meaning of 'technical service' with reference to Law Lexicons and the decision of the Supreme Court in Commissioner of Customs vs. Parasrampuria Synthetics Ltd. (2002) 253 ITR 274 (SC) , besides other decisions of the Tribunal.

Maintenance, Repairs and Cleaning Services: Where the predominant purpose involves cleaning service, even if done through use of technology is not technical service by itself as it does not involve transfer of technology. No technology is made available in India in what can be considered as purely cleaning service vide Example 2 in the Protocol in the Agreement between India and U.S. Similarly, maintenance and repairs cannot be treated as technical service. It is a business assignment, so that the income from such service cannot be taxed, unless the non-resident has a permanent establishment in India, through which such service is rendered. In the absence of such transfer, there can be no tax deduction at source.

Monitoring Consultancy Services of a Branch in India: In the case of Worleyparsons Services Pty. Ltd. In re (2008) 301 ITR 54 (AAR), it was held that in Service of monitoring consultants for a pipeline project in India has to be treated as a business activity, so that the payment for the same cannot be treated as royalty. The income from such activity can only be treated as profit from business. There was also no parting of technology involved as required under the definition of "technical services" under Article 12(3)(g) of the Double Taxation Avoidance Agreement between India and Australia to constitute technical fees. The assessable income, therefore, would be the profit attributable to the permanent establishment, which the non-resident had in India for purposes of its activity.

Payment for Engineering and Procurement Services/Consultants: Sometimes a non-resident without a permanent establishment in India provides engineering and procurement services to an Indian company under an agreement. The expression 'royalty' as defined both under domestic law and Double Taxation Avoidance Agreement, where there was service by way of development and transfer of technical plan and design, besides consultancy and technical service ancillary and subsidiary to tie supply of scientific, technical or commercial information/knowledge. The assessee in this case was rendering service in connection with Jamnagar to Bhopal pipeline and Goa to Hyderabad pipeline undertaken by Reliance. There was, therefore, liability [Worley Parsons Services Pty. Ltd. (No.1)(2009) 312 ITR 273 (AAR)]. In coming to the conclusion, the Authority for Advance Ruling distinguished the decision of the Supreme Court in Ishikawajima-Harima Heavy Industries vs. DIT (2007) 288 ITR 408 (SC) not only because it related to a different Agreement, but also because the offshore element in that case formed an integral part of the contract, apart from the fact that the issue in that case was ascertainment of income attributable to the permanent establishment.

In another matter relating to assessee in Worley Parsons Services Pty. Ltd., In re (No.2)(2009) 312 ITR 317 (AAR), the issue related to agreement for rendering professional service to Indian company for setting up an alumina refinery from inputs gathered from India, while design service was made from Australia. It was found, that the non-resident's employees came to India, stayed in India and collected the necessary data and information. The activities in preparation of design and plan, no doubt, were in Australia, but the work in India was by no means negligible. The service was utilised in India for the benefit of a resident in India. Part of the activities/ services was in India, so that there was sufficient nexus to warrant inference of royalty, so as to require the entire amount to be taxable in India. The ruling in the earlier case in Worley Parsons Services Pty. Ltd. (No.1)(2009) 312 ITR 273 (AAR), was followed distinguishing the decision in Ishikawajima-Harima Heavy Industries' case.

Technology along with Training: In the case of Director General of Inland Revenue vs. Phaltan Sugar Works(1983) 1 MLJ 74, it was held by a Malaysian court, that a payment in pursuance of a joint venture agreement, for supply of technology and investments besides supply of technical personnel could be treated as an agreement giving rise to receipts which could be treated as royalty.

Ticketing Service: Sheraton group of companies, a non-resident U.S. company engaged in hotel related services worldwide, had entered into an agreement with Indian companies including ITC Ltd. Hotel Division and others for helping to procure business for the hotels in India at 3 per cent of the room sales for services which included publicity, advertisement and reservation facilities for overseas customers, by way of brochures, directories, room magazines, brand advertising, promotion of trade shows abroad, etc. The Tribunal in Sheraton International Inc. vs. Deputy Director of Income Tax (2007) 293 ITR (AT) 68 (Delhi), found that services rendered by the non-resident would not attract either the definition of 'royalty' or 'technical fees'. The services rendered were more related to marketing of Indian hotels abroad by advertisement to promote tourism and encourage visitors coming to India to be lodged in these hotels by means which can be described as mere ticketing service, since advertisement, publicity and sales promotion abroad were the main functions with the use of the trade mark or trade name and other services was merely incidental to this main service of the publicising the hotels abroad. The definition of royalty and technical fees in the Indo-US Agreement, it was decided, would also not give rise to any different inference.

The alternate argument by the revenue that the agreement was a colourable device meant to defraud the revenue crossing the limits of legitimate tax planning, was found to lack foundation. It was pointed out, that the Income Tax Department itself allowed a deduction at 25 per cent from the payment in the tax deduction certificate u/s 195(2), though it was argued before the Tribunal that 100 per cent payment will be taxable, on the ground that the order u/s 195(2) was only an interim order not binding in an assessment. It was found that no part of payment was taxable.

The Departmental appeal against the decision of the Tribunal in this case was dismissed in Director of Income Tax vs. Sheraton International Inc.(2009) 313 ITR 267 (Del), where it was pointed out that the services were in the nature of advertisement, publicity and sales promotion services and that the use of the trade mark and trade name stylized "S" or other enumerated services for mutual interest of the Sheraton Group of hotels was merely incidental services.

Transponder Hire: In Asia Satellite Communications Co. Ltd. vs. DCIT, (2003) 85 ITD 478 (Del), it was held that payment for uplifting of transponder service through earth stations and conversion of signals was held to be royalty.

But it was held, in Wipro Ltd. vs. ITO (2003) 86 ITD 407 (Bang), ITO vs. Raj Television Newark Ltd. ITA No.1827 and 1828 MDS 1998, Dy. CIT vs. Panamsat International Systems Inc. (2006) 103 TTJ (Del) 861, that it was not to be treated as royalty, since it was use of a standard facility in favour of the taxpayer. The reasoning in such cases follows Dun and Bradstreet Espana S.A., In re (2005) 272 ITR 99 (AAR), and Raymond Ltd. vs. Dy. CIT (2003) 86 ITD 791 (Mum). The view of Madras High Court in Skycell Communications Ltd. vs. DCIT (2001) 251 ITR 53 (Mad), is also on the lines, when it held that use of technological facilities does not by itself have a character of technical service in following words:

"In the modern day world, almost every facet of one's life is linked to science and Technology in as much as numerous things used or relied upon in everyday life is the result if scientific and technological development. Every instrument or gadget that is used to make life easier is the result of scientific invention or development and involves the use of technology. On that score, every provider of every instrument or facility used by a person cannot be regarded as providing technical service."

Mere collection of a fee for a standard facility could hardly ever be treated as royalty or technical service.

In ISRO Satellite Centre (ISAC), In re (2008) 307 ITR 59 (AAR) it was ruled by the AAR that it will be a business transaction following its earlier ruling in Dell International Service P. Ltd., In re (2008) 305 ITR 37 (AAR). It was concluded, after referring to Klaus Vogel's Commentary on Double Taxation Conventions, that the use of satellite is a service and not a rental, unless resident had entire direction and control over the satellite. Where the non-resident has no permanent establishment in India, there could be no liability.

Transponder service providing facility for data transmission to telecasting/telecom operators, came up before a Special Bench of the Tribunal in New Skies Satellites N.V. vs. Asst. Director of Income Tax (International Taxation)(2009) 319 ITR (AT) 269 (Del) (SB) to sort out the conflicting decisions in Asia Satellite Telecommunication Co. Ltd. vs. Dy. CIT(2003) 85 ITD 478 (Del) and Dy. CIT vs. Pan Amsat International Systems Inc. (2006) 9 SOT 100 (Del). After detailed discussion, the Tribunal found that the payment is not for mere hire of transponder known as communication transponders. Sophisticated instruments are required to be installed on geostationary satellites with similarly sophisticated instruments installed in the earth stations for compatability of uplinking and downlinking the signals by telecasting companies. The specifications are made available by these companies and operated for obtaining optimum results. The activities of both satellite and telecasting companies are no doubt commercial in nature, but there is business connection, so that the income accrues for the non-resident in India under the domestic law because there is a process involved in India. Such process would attract tax, whether it is secret or otherwise. The right to use is made available in India. It is in this context, the non-resident's income becomes taxable in India.

However, the High Court overruled the Special Bench decision, in the case of Asia Satellite Telecommunications Co. Ltd. vs. Director of Income-tax, (2011) 332 ITR 340 (Del), when it upheld assessee's claim for non-liability. But the controversy has been finally statutorily resolved as far as domestic law is concerned by Explanation 6 to section 9(1)(vi) to cover transmission to satellite communication inserted by the Finance Act, 2012 retrospectively with effect from 1.6.1976. But this amendment cannot bind interpretation of Double Taxation Avoidance Agreement.

Availability of Mauritius Route: The issue whether adoption of Mauritius route itself could be treated as a method of tax planning, which can be ignored by the Assessing Officer, was the subject-matter of decision in Union of India vs. Azadi Bachao Andolan (2003) 263 ITR 706 (SC). The cloud created by the decision of the Delhi High Court in Shiva Kant Jha vs. Union of India (2002) 256 ITR 563 (Del) questioning the Circular No.789 dated 13th April, 2000 was lifted, when the Supreme Court upheld the validity of the circular. As regards income from dividend and capital gains, the inference that the Assessing Officer would be justified in accepting certificate of incorporation issued by the Mauritius Authorities as evidence of residence was found to be valid. But then the circular itself was withdrawn consequent on the Delhi High Court decision by another Circular No.1 of 2003. But then, it would appear that the decision of the Supreme Court would have even a greater effect than the circular which was withdrawn and was found to be valid. In the result, the Mauritius route continues to be a favourable one. It is understood that Cyprus route is becoming popular not only because of the Double Taxation Avoidance Agreements between India and Cyprus, but also because of the tax exemptions and other facilities made available by Cyprus Government.

More favourable treatment for companies incorporated in Mauritius had sparked a controversy as to the validity of such agreement merely with reference to incorporation certificate even for investment income, but was upheld by the Supreme Court in the case of Azadi Bachao Andolan (supra). However, the more favourable terms are under negotiation with Mauritius Government with possible revision on par with other countries.

Vodafone Case: Hutchison Group gave up its interest in the business of mobile-telephone operation in India in favour of Vodafone Group by overseas transactions as between holding companies, while the Indian shares continued to be in the hands of same holding companies. Hutchison in this line of business from 1992 of non-resident players functioning in many countries through subsidiaries and subsidiaries of subsidiaries. Briefly, the assessee which was required to deduct tax at source is Vodafone International Holdings B. V., Netherlands (VIH BV), a company controlled by the Vodafone Group Plc. U. K. The Hutchison Group company in Hong Kong acquired interests in the mobile telecommunication industry in India, through a special process vehicle by way of joint venture, Hutchison Max Telecom Ltd. (renamed Hutchison Essar Ltd.) formed in August 2005. Between 1992 and 2006, there had been many changes in international scenario with Hutchison Group acquiring interest in twenty-three mobile telecommunication circles in India in Hutchison Essar Ltd. through a structural arrangement of holding and subsidiary companies. Tax liability was inferred on transfer of control over the operational companies (Indian entities) which were under control, direct or indirect, inter alia, through Mauritius based companies recognized as overseas corporate bodies with tax residency certificates, exercising direct or indirect control held by Mauritian companies became the property of Vodafone Group acquiring on transfer of shares in CGP Investments (CGP), subsidiary of a holding company, both registered in the Cayman Islands [Vodafone International Holdings B.V. vs. UOI (2012) 341 ITR 1 (SC)].

There have been a number of amendments to nullify Vodafone's case. Underlying assets which were not found taxable in Vodafone's case in absence of "see through provision" is now introduced vide Explanation 4 to section 9(1)(vi) by the Finance Act, 2012 with retrospective effect from 1.4.1962. Explanation 5 to section 9(1)(i) would deem any share or interest in an Indian company as situated in India has also been inserted by the Finance Act, 2012 with effect from 1.4.1962 to nullify Vodafone 's case.

Case Laws:

(1) As regards the salary paid to a non-resident outside India for services rendered in India, the Authority for Advance Ruling, in Stanley Keith Kinnett vs. CIT (1999) 238 ITR 155 (AAR) held that the remuneration was not taxable in India as the payment was not borne by the non-resident's permanent establishment in India.

(2) A French company alleges that its Indian income was taxed at a rate higher than in France and so there was discrimination. The Authority for Advance Ruling held that discrimination clause does not apply to rates but only to income as held in P. No. 16 of 1998, In re(1999) 236 ITR 103 (AAR). However, this decision was set aside by the Supreme Court in Societe Generate vs. CIT (2001) 251 ITR 657 (SC) on the ground that AAR had no jurisdiction to decide the issue as the matter was pending before the Income Tax Authorities, so that it was left to be decided by normal course in assessment jurisdiction.

(3) Living allowance to a foreign technician given by an Indian resident is not taxable [CIT vs. H. Link (2000) 244 ITR 93 (Guj.)].

(4) Where a branch constitutes permanent establishment and makes the remittance to head office of income like interest, tax deduction at source cannot have application [ABN Amro Bank NV vs. Asstt. Dir. of IT. (2006) 280 ITR (AT) 117 (Kol.) (SB)].

(5) Technical service cannot be inferred unless there is sharing of technology or provision of drawings, designs, etc., for the exclusive use of resident assessee [Dy. CIT vs. Boston Consulting Group P. Ltd. (2006) 280 ITR (AT) 1 (Mum.)].

(6) Where a formula for inference of taxable income for film distribution rights had been accepted in the past, the same formula is bound to be repeated in the absence of a more positive guideline[Jt. CIT vs. Warner Brothers (FE) Inc. (2006) 282 ITR (AT) 90 (Mum.) (SB)].

(7) Fees for technical drawing furnished by Canadian company to Indian Government organization is consultancy service liable to tax as technical fees under Article 12 of Indo-Canadian treaty [SNC Lavalin International Inc. (2011) 332 ITR 314 (Del)].

(8) Denial of benefit of second proviso to section 48 (Indexation benefit) available for only residents does not amount to discrimination under the Article 24 of Indo-Canadian Agreement, since it is based on residential status and not on citizenship [Transworld Garnet Ltd. In re (2011) 333 ITR 32 (AAR)].

(9) Where the resident assessee received support services from Philippines branch of a Netherlands company, the relevant agreement is one between India and Netherlands. Indo-Philippines agreement will have no relevance merely on the ground that service was rendered from Philippines[Shell Technology India Private Ltd., In re (2012) 345 ITR 206 (AAR)].

(10) When the Indian has other clients, he is an independent agent, so that he cannot constitute a P.E. [Speciality Magazine Pvt. Ltd. In re, 274 ITR 310 (AAR)].

(11) When bonus shares are offered to the non-resident there is no release of assets, so there is no requirement for deduction of tax at source [Briggs of Burton (India) P. Ltd., In re (2005) 274 ITR 595 (AAR)].

ILLUSTRATIONS ON DOUBLE TAXATION RELIEF

Illustration 1.

R a resident Indian, has derived the following income for the Previous Year relevant to the Assessement Year 2016-2017.

Particulars	**Amount (₹)**
Income from profession	3,00,000
Share of income from a partnership in country X (tax paid in Country X for this income in equivalent Indian Rupees 25,000)	2,00,000
Commission income from a concern in country Y (tax paid in country Y @ 20%, converted in equivalent Indian Rupees)	40,000
Interest on scheduled banks [other than savings account]	20,000

R wishes to know whether he is eligible to any double taxation relief, if so, its quantum. India does not have any Double Taxation Avoidance Agreement with countries X and Y.

Solution:

(1) Computation of Total Income for the Assessment Year 2016-17

Particulars	Amount (₹)	Amount (₹)
Income from Business:		
Income from profession	3,00,000	
Share income in partnership firm in country X	2,00,000	5,00,000
Income from Other Sources:		
Interest from schedule bank	20,000	
Commission earned in country Y, assumed from other sources	40,000	60,000
Total Income		**5,60,000**

(2) Computation of Tax Liability on Total Income for the Assessment Year 2016-17

Particulars	Amount (₹)
Tax on Total Income of ₹ 5,60,000	37,000
Add: Surcharge on Income Tax (assuming total income is less than one crore)	Nil
Add: Education Cess @ 2%	740
Add: Secondary and Higher Education Cess @ 1%	370
	38,110
Less: Double taxation relief : (2,00,000 + 40,000) = 2,40,0000 x 6.805%	16,332
Tax Payable	21,778
Rounded off U/S 288B	21,780

Note: (i) Average rate of tax in the foreign country = [(25,000 + 8,000)/ (2,00,000 +40,000)] = 13.75%

(ii) Average rate of tax in India:

= 38,110/5,60,000 x 100 = 6.805%

Whichever is less, is applicable

Illustration 2.

Mr. Prasad, ordinarily resident in India, furnished the following particulars of his income/savings during the Previous Year 2015-2016.

(i)	Income from foreign business (Including ₹ 2,00,000 from business connection in India) accruing outside India	12,00,000
(ii)	Loss from Indian business	(–) 2,00,000
(iii)	Income from house property	4,00,000
(iv)	Dividends gross from Indian companies	60,000
(v)	Deposit in Public Provident Fund	70,000
(vi)	Tax paid in foreign country	2,50,000

There is no double taxation avoidance treaty. Compute the tax liability

Solution:

(1) Computation of Total Income for the Assessment Year 2016-17

Particulars	Amount (₹)	Amount (₹)
1. Income from House Property		4,00,000
2. Income from Business:		
(a) Income from Indian Business	(2,00,000)	
(b) (i) Income from foreign business accruing or arising outside India	10,00,000	
(ii)income from foreign business deemed to accrue or arise in India	2,00,000	10,00,000
3. Income from other sources		
Dividends from Indian Companies- exempted u/s 10(34)		Nil
Gross Total Income		14,00,000
Less: Deduction for approved savings u/s 80C – PPF deposits		70,000
Total Income		13,30,000

(2) Computation of Tax liability on Total Income for the Assessment Year 2016-17

Particulars	Amount (₹)
Tax on Total Income of ₹ 13,30,000	2,24,000
Add: Surcharge on Income Tax (assuming total income is less than one crore)	Nil
Add: Education Cess @ 2%	4,480
Add: Secondary and Higher Education Cess @ 1%	2,240
	2,30,720
Less: Double taxation relief : 10,00,000 x 17.347%	1,73,470
Tax Payable	57,250

Note: 1. Relief is allowed on the doubly taxed income either at average rate of Indian tax or average rate of foreign income tax, whichever is lower:-

(a) Average rate of Indian income tax : 2,30,720/ 13,30,000 × 100 = 17.347%

(b) Average rate of foreign income tax: (2,50,000/12,00,000) × 100 = 20.833%

2. The amount of doubly taxed income has been worked out as under:

Income from foreign business, accruing outside India	12,00,000
Less: Income from business connection deemed to accrue or arise in India which is not entitled to double taxation relief.	2,00,000
Doubly taxed income	10,00,000

3. Loss from Indian business has been set-off against profits from foreign business which is deemed to accrue or arise in India. The mode of set-off increases the amount of double taxation relief.

Illustration 3.

The Income-tax Act, 1961 provides for taxation of a certain income earned by X. The Double Taxation Avoidance Agreement, which applies to X, excludes the income earned by X from the purview of tax. Is X liable to pay tax on the income earned by him? Discuss.

Solution:

Where any conflict arises between the provisions of the Double Taxation Avoidance Agreement and the Income-tax Act, 1961, the provisions of the Double Taxation Avoidance Agreement would prevail over those of the Income-tax Act. X is, therefore, not liable to pay tax on the income earned by him.

Illustration 4.

Explain briefly the proposition of law in case of any conflict between the provisions of the Double Taxation Avoidance Agreement (DTAA) and the Income-tax Act, 1961.

Solution:

Where there is conflict between the provision as contained in the tax treaty and the provisions of Income Tax Act, a payer can take advantage of those provisions which are more beneficial to him. Thus, tax treaties override the provisions of Income Tax Act which can be enforced by the Appellate Authorities/ Courts.

Illustration 5.

Arif, a resident both in India and Malaysia in Previous Year 2015-2016, owns immoveable properties (including residential house) at Malaysia and India. He has earned income of ₹ 50 lakh from rubber estates in Malaysia during the Previous Year 2015-2016. He also sold some property in Malaysia resulting in short-term capital gain of ₹ 10 lakh during the year. Arif has no permanent establishment of business in India. However, he has derived rental income of ₹ 6 lakh from property let out in India and he has a house in Lucknow where he stays during his visit to India. The Article 4 of the Double Taxation Avoidance Agreement between India and Malaysia provides that where an individual is a resident of both the Contracting States, he shall be deemed to be resident of the Contracting State in which he has permanent home available to him. If he has permanent home in both the Contracting States, he shall be deemed to be a resident of the Contracting State with which his personal and economic relations are closer (centre of vital interests).

You are required to state with reasons whether the business income of Arif arising in Malaysia and the capital gains in respect of sale of the property situated in Malaysia can be taxed in India.

Solution:

Where the Central Government has entered into an agreement with the Government of any other country for granting relief to tax or for avoidance of double taxation, the provisions of the Income-tax Act, 1961 are applicable in such case to the extent they are more beneficial to the assessee.

Arif has a residential house both in Malaysia and India. Thus, he has a permanent home in both the countries. However, he has no permanent establishment of business in India. The Double Taxation Avoidance Agreement (DTAA) with Malaysia provides that where an individual is a resident of both countries, he is deemed to be resident of that country in which he has a permanent home and if he has a permanent home in both the countries, he is deemed to be resident of that country, which is the centre of his vital interests, i.e. the country with which he has closer personal and economic relations. Arif owns rubber estates in Malaysia from which he derives business income. However, Arif has no permanent establishment of his business in India. Therefore, his personal and economic relations with Malaysia are closer, since Malaysia is the place where:–

(a) the property is located ; and

(b) the permanent establishment (PE) has been set-up. Therefore, he is deemed to be resident of Malaysia for A.Y. 2016-2017.

So, in this case, Arif is not liable to Income tax in India for Assessement Year 2016-2017 in respect of business income and capital gains arising in Malaysia.

Illustration 6.

Ms. Sania, a resident Indian, furnishes the details for the Assessement Year 2016-2017 :

Particulars	Amount (₹)
(1) Income from profession	1,94,000
(2) Share of income from a partnership in country X (tax paid in Country X for this income in equivalent Indian Rupees 8,000)	40,000
(3) Commission income from a concern in country Y (tax paid in country Y @ 20%, converted in equivalent Indian Rupees	30,000
(4) Interest on scheduled banks [other than savings account]	20,000

Ms. Sania wishes to know whether she is eligible to any double taxation relief, if so, its quantum. India does not have any Double Taxation Avoidance Agreement with countries X and Y.

Solution :

(1) Computation of Total Income for the Assessment Year 2016-17

Particulars	Amount (₹)	Amount (₹)
(a) Income from Business or Profession:		
(i) Income from Profession	1,94,000	
(ii) Share of income in partnership firm in country X	40,000	2,34,000
(b) Income from other sources:		
(i) Interest from scheduled bank	20,000	
(ii) Commission earned in Country Y, assumed from other sources	30,000	50,000
Total Income		**2,84,000**

(2) Computation of Tax Liability on Total Income for the Assessment Year 2016-17

Particulars	**Amount (₹)**
Tax on Total Income of ₹ 2,84,000	3,400
Add: Surcharge on Income Tax	Nil
Add: Education Cess @ 2%	168
Add: Secondary and Higher Education Cess @ 1%	34
	3,502
Less: Double taxation relief : 70,000 x 1.233%	863
Tax Payable	2,639
Rounded off u/s 288B	**2,640**

Note : (i) Average rate of tax in the foreign country = 20% i.e. [(₹ 8,000 + 20% of ₹ 30,000)/(40,000+30,000)] x 100

(ii) Average rate of tax in India = (3,502/2,84,000) x 100 = 1.233%

Illustration 7.

Mr. B is a musician deriving income from foreign concerts performed outside India, ₹ 50,000. Tax of ₹10,000 was deducted at source in the country where the concerts were given. India does not have any agreement with that country for avoidance of double taxation. Assuming that Indian income of B is ₹ 2,50,000, what is the relief due to him under Sec. 91 for the Assessement Year 2016-2017.

Solution:

(1) Computation of Total Income for the Assessment Year 2016-17

Particulars	**Amount (₹)**
Indian Income	2,50,000
Foreign Income	50,000
Gross Total Income or Total Income	3,00,000

(2) Computation of Tax Liability on Total Income for the Assessment Year 2016-17

Particulars	**Amount (₹)**
Tax on Total Income	5,000
Add: Education Cess @ 2%	100
Add: Secondary and Higher Education Cess @ 1%	50
Less: Double taxation relief u/s 91 = ₹ 50,000 x 1.72%	860
Tax Payable	4,290

Note: 1. Average rate of Indian income tax: (5,150 x 3,00,000) x 100 = 1.72%

2. Average rate of foreign income tax:

Relief is allowed either at the average rate of Indian Income Tax or the average rate of Foreign Income Tax = (10,000/50,000) x 100 = 20%

whichever is lower. Accordingly, the relief has been allowed at the average rate of Indian Income tax.

Illustration 8.

A resident assessee, earned foreign exchange of ₹ 78,800. The foreign income was also subjected to tax deduction of ₹ 8,800 at source in the foreign country with which India had no agreement for avoidance of double taxation. The assessee claimed relief under Sec. 91 of the Income-tax Act in respect of the whole foreign income. Discuss his contention with reference to decided case laws.

Solution:

Where any income is taxed outside India as well as in India, a resident assessee is entitled to claim double taxation relief on such doubly taxed income provided such income is not deemed to accrue or arise in India. If any income arising outside India, is not subjected to tax in India, such foreign income does not form part of doubly taxed income for the purposes of Sec. 91. The expression "doubly taxed income" refers to foreign income which also suffered tax in India.

Where any foreign income, taxed outside India, is also eligible to deduction in computing total income in India, double taxation relief would be allowed only on such income as forms part of total income.

On the amount of doubly taxed income, Income-tax is calculated at the Indian rate of tax and rate of tax of the foreign country. The foreign tax rate has to be calculated separately for each country – CIT vs. Bombay Burmah Trading Corpn. Ltd. [2003] 126 Taxman 403 (Bom.)

Double taxation relief will be allowed on such doubly taxed income either at the average rate of Foreign Income Tax or Indian Income Tax, whichever is lower out of the two.

Illustration 9.

An Indian company pays to a foreign company for providing engineering services to be utilised in India. Part of the work is done abroad but the payment is made entirely outside India. Is the foreign company liable for Indian Income-tax?

Solution:

Yes. The criterion is not where it is paid but where the services are utilized [Steffen Robertson and Kirsten Consulting Engineers and Scientists vs. CIT. (1998) 230 ITR 207 (AAR)]. But liability will be limited to the proportionate profits attributable to activities in India under Explanation 1 to section 9(1) and as provided invariably in all DTA Agreements.

Illustration 10.

A resident pays for electronic purchase of business information reports. Is the payment to be taxed as royalty?

Solution:

No. The transactions are on principal to principal basis, where there is no P.E. of the non-resident. Information is available to anyone. It is not royalty [ABC Ltd., In re, (2006) 284 ITR 1 (AAR)].

Illustration 11

A Ltd. registered in UK filed a certificate of residence in UK from Indian Revenue Authorities in UK and claimed that its entire income from shipping was exempted under Article 9(1) of the Indo-UK Convention. Can the Assessing Officer deny exemption on the ground that assessee has not established its residence in the UK so as to attract the benefit of Indo-UK Agreement?

Solution:

Where a company is incorporated in the UK filed a certificate of residence as well, the Assessing Officer has no material to question the claim of the assessee [Arabian Express Line Ltd. of UK vs. UOI (1995) 2012 ITR 31 (Guj)

Illustration 12

S&L Ltd., a foreign company has no share in an Indian company, but the holding company of S&L Ltd. has. Indian company advances loan to the foreign company. Does it attract tax as dividend under section 2(22)(e)?

Solution:

No. As S&L Ltd. is not a shareholder in the Indian company, section 2(22)(e) does not apply [Madura Coats P. Ltd., In re (2005) 274 ITR 609 (AAR)].

Illustration 13

What are the conditions for taxation of a non-resident on his salary income in India?

Solution:

There are three conditions all of which are to be satisfied, namely, residence for 183 days or more, payments from a permanent establishment of the country to which the salary is charged etc. for deduction of the same. Primarily the taxability will arise in the country where the service is rendered, unless the residence is less than 183 days in which case, there is liability [CIT vs. Elitos S.P.A. (2006) 280 ITR 495 (All.).

Where stay is more than 183 days, the liability is at the place of residence though payment is made elsewhere [Hindustan Powerplus Ltd., In re (2004) 271 ITR 433 (AAR)]. Normally, tax is to be paid where service is rendered but the exceptions are to be considered [Emmerich Jaegar vs. CIT (2005) 274 ITR 125 (Guj.).

Illustration 14

If a taxpayer is entitled to double tax relief in India, though assessable under Indian Law, could such relief be denied merely because such income is exempt from tax in the other country?

Solution:

No. There can be double non-taxation. It was so pointed out in CIT vs. Laxmi Textile Exporters Ltd. (2000) 245 ITR 521 (Mad.), in the similar situation, where income was eligible for exemption under Srilankan Law, though not taxable in India under the DTAA, it was held that relief cannot be denied. The High Court found that the DTAA is binding on the Government even [CIT vs. Visakhapatnam Port Trust (1983) 144 ITR 146 (AP)].

Study Note - 11

RETURN OF INCOME & ASSESSMENT PROCEDURE

This Study Note includes

11.1 RETURN OF INCOME

The starting point for assessment of income is furnishing of return of income. Filing of return of income is mandatory for certain category of assessees. Incidental provisions for accompaniments to the return of income, error correction and belated returns have been made. Now filing of the return electronically has been made mandatory for certain category of assessees.

Return of income is the format in which the assessee has to furnish information as to his total income and tax payable. The format for filing of returns by different assessees is notified by the CBDT.

11.1.1 Compulsory Filing of Return of Income [Section 139(1)]

(1) As per section 139(1), it is compulsory for companies and firms to file a return of income for every Previous Year.

(2) In case of a person other than a company or a firm, filing of return of income is mandatory, if his total income or the total income of any other person in respect of which he is assessable under this Act during the Previous Year exceeds the basic exemption limit.

(3) Such persons should, on or before the due date, furnish a return of income in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed.

(4) Further, every person, being an individual or a HUF or an AOP or BOI or an artificial juridical person–

- whose total income or the total income of any other person in respect of which he is assessable under this Act during the Previous Year
- without giving effect to the provisions of section 10A or 10B or 10BA or Chapter VI-A - exceeded the basic exemption limit is required to file a return of his income or income of such other person.

Every Individual, HUF, etc. must file their return of income if it's Gross Total Income exceeds the exempted income ceiling :

Assessee	Exempted Ceiling
Resident Super Senior Citizen	₹ 5,00,000
Resident Senior Citizen	₹ 3,00,000
Resident or Non-resident Individual	₹ 2,50,000
HUF	₹ 2,50,000

(5) For company and certain other assessees like firm having tax audit, filing of return in an electronic form is mandatory. (Section 139D)

(6) **Compulsory filing of return in relation to assets, etc. located outside India [Fourth proviso to section 139(1)] [W.e.f. A.Y. 2016-17]**

A person, being a resident other than not ordinarily resident in India within the meaning of section 6(6), who is not required to furnish a return under this sub-section and who at any time during the previous year,—

(a) holds, as a beneficial owner or otherwise, any asset (including any financial interest in any entity) located outside India or has signing authority in any account located outside India; or

(b) is a beneficiary of any asset (including any financial interest in any entity) located outside India,

shall furnish, on or before the due date, a return in respect of his income or loss for the previous year in such form and verified in such manner and setting forth such other particulars as may be prescribed.

Provided also that nothing contained in the fourth proviso shall apply to an individual, being a beneficiary of any asset (including any financial interest in any entity) located outside India when income, if any, arising from such asset is includible in the income of the person referred to in clause (a) of that proviso in accordance with the provisions of this Act.

Note:-

"Beneficial owner" in respect of an asset means an individual who has provided, directly or indirectly, consideration for the asset for the immediate or future benefit, direct or indirect, of himself or any other person.

"Beneficiary" in respect of an asset means an individual who derives benefit from the asset during the previous year and the consideration for such asset has been provided by any person other than such beneficiary.

(7) **Political Parties :** Political parties are under a statutory obligation to file return of income in respect of each Assessment Year in accordance with the provisions of the Income-tax Act and the total income for this purpose has to be computed without giving effect to the provision of section 13A and Chapter VI-A of the Act.

(8) **Liquidator :** Under the Companies Act, 2013, a liquidator is not exempt from making an Income-tax return on business managed by him for the beneficial winding up of the company.

(9) **Charitable Trust :** Submission of return by charitable trust is essential even if its income is exempt. If the total income of a charitable trust (without claiming exemption under section 11 and 12) exceeds the maximum amount not chargeable to tax, then submission of return by the trust is essential.

(10) No need to file return if Non-agricultural income is less than the amount of exemption limit in the case of an Individual/ HUF.

Exemption provided by the Government when taxable income of an individual is up to ₹ 5,00,000 : If the following conditions are satisfied, the taxpayer has an option to submit his return of income or not to submit his return of income –

(i) The taxpayer is an individual. He may be resident or non-resident.

(ii) His taxable income does not exceed ₹5,00,000. Taxable income should consist of salary and/ or saving bank account interest (but interest should not be more than ₹10,000).

(iii) The individual has reported to his employer his Permanent Account Number (PAN).

(iv) The individual has reported to his employer his saving bank interest for the purpose of calculating tax deductible under section 192.

(v) The Individual has received a certificate of tax deduction in Form No. 16 from his employer which mentions the PAN, details of income, tax deducted at source by the employer and deposited to the credit of the Central Government.

(vi) The individual has no claim of refund of taxes due to him for the income of the Assessment Year.

(vii) The individual has received salary from only one employer for the Assessment Year.

However, in case notice under section 142(1), 148, 153A or 153C has been issued for filing a return of income for the relevant Assessment Year, exemption is not available.

'Due date' means –

(a) ***30th November of the Assessment Year,*** where the assessee is required to furnished a report in Form No. 3CEB under section 92E pertaining to international transactions.

(b) **30th September of the Assessment Year**, where the assessee is -

- (i) a company; or
- (ii) a person (other than a company) whose accounts are required to be audited under the Income-tax Act, 1961 or any other law in force; or
- (iii) a working partner of a firm whose accounts are required to be audited under the Income-tax Act, 1961 or any other law for the time being in force.

(c) ***31st July of the Assessment Year,*** *in the case of any assessee other than those covered in (a) & (b) above.*

The return of income required to be furnished in Form No. ITR-1, ITR-2, ITR-3, ITR-4, ITR-5 or ITR-6 shall not be accompanied by a statement showing the computation of the tax payable on the basis of the return, or proof of the tax, if any, claimed to have been deducted or collected at source or the advance tax or self-assessment tax, if any, claimed to have been paid or any document or copy of any Account or Form or Report of Audit required to be attached with the return of income under any of the provisions of the Act.

The return of income referred to in sub-rule (1) may be furnished in any of the following manners, namely:—

(a) furnishing the return in a paper form;

(b) furnishing the return electronically under digital signature;

(c) transmitting the data in the return electronically and thereafter submitting the verification of the return in Form ITR-V;

(d) furnishing a bar-coded return in a paper form.

It shall be mandatory for the following assessees to file the return electronically:

(a) every person (not being a co. or a person filing return in ITR 7) having total income exceeding ₹5,00,000

(b) an individual or a Hindu Undivided Family, being a resident, having assets (including financial interest in any entity) located outside India or signing authority in any account located outside India and required to furnish the return in Form ITR-2 or ITR-3 or ITR-4, as the case may be.

(c) Every person claiming tax relief under Section 90, 90A or 91

(d) Persons who are required to get their Accounts audited under Section 44AB, 92E, 115JB.

(e) A company required to furnish the return in Form ITR-6.

(f) Other tax payers can submit their return in paper format or electronically with or without digital signature.

However, as per instruction of ITR 7 From assessment year 2013-14 onwards in case an assessee who is required to furnish a report of audit under section 10(23C)(iv), 10(23C)(v), 10(23C)(vi), 10(23C)(via), 10A, 12A(1)(b), 44AB, 80-IA, 80-IB, 80-IC, 80-ID, 80JJAA, 80LA, 92E or 115JB he shall file the report electronically on or before the date of filing the return of income.

E-filing of Income Tax Return for AY 12-13 will not be mandatory for agents of non-residents [u/s 160(1)(i) of the IT Act] as well as for Private Discretionary Trusts.

11.1.2 Interest for Default in Furnishing Return of Income [Section 234A]

(1) Interest under section 234A is attracted where an assessee furnishes the return of income after the due date or does not furnish the return of income.

(2) The interest is payable for the period commencing from the date immediately following the due date and ending on the following dates -

When the return is furnished after due date: the date of furnishing of the return

Where no return is furnished: the date of completion of assessment

(3) The interest has to be calculated on the amount of tax on total income as determined under section 143(1) or on regular assessment as reduced by the advance tax paid and any tax deducted or collected at source @ 1% for every month or part of the month.

In the case of Associated Electro Ceramics vs. Chairman, Central Board of Direct Taxes (1993) 201 ITR 501 (Karn), the Karnataka High Court held that the Board has power to condone the delay in cases having claim of carry forward of losses. The Department did not file special leave petition against this order. Subsequently the matter was taken up with the Ministry of Law who also agreed with the view that the Board has power to condone the delay in filing the return under section 119(2)(b) of the Income-tax Act, 1961, in a case having claim of carry forward of losses. In view of the above, the CBDT has [vide Circular No. 8/2001, dated 16.5.2001] clarified that delay in making claim of carry forward of losses can be condoned in cases where returned income is a loss. Further the monetary limits prescribed for condonation of delay in making refund claims, by different income-tax authorities will also apply to condonation of delay in cases of claim of carry forward of losses.

The monetary limits prescribed for condonation of delay are as under:

1	Where the loss does not exceed ₹10,000	The Assessing Officer shall obtain prior approval of Commissioner of Income-tax
2	Where the loss exceeds ₹10,000 but does not exceed ₹1,00,000	The Assessing Officer shall obtain prior approval of Chief Commissioner of Income-tax or Director General of Income-tax
3	Where the loss exceeds ₹1,00,000	The power of condonation as well as power of rejection in all cases lies with the CBDT

11.1.3 Option to Furnish Return of Income to Employer [Section 139(1A)]

(1) This section gives an option to a person, being an individual who is in receipt of income chargeable under the head "Salaries", to furnish a return of his income for any Previous Year to his employer, in accordance with such scheme as may be notified by the CBDT and subject to such conditions as may be specified therein.

(2) Such employer shall furnish all returns of income received by him on or before the due date, in such form, including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media and manner as may be specified in that scheme.

(3) In such a case, any employee who has filed a return of his income to his employer shall be deemed to have furnished a return of income under sub-section (1).

11.1.4 Income Tax Return through Computer Readable Media [Section 139(1B)]

(1) This sub-section enables the taxpayer (company or a person other than company) to file his return of income in computer readable media, without interface with the department.

(2) Such person may, on or before the due date, furnish a return of income in accordance with such scheme as may be notified by the CBDT, in such form, including on a floppy, diskette, magnetic cartridge tape, CD-ROM or any other computer readable media and manner as may be specified in that scheme.

(3) In such case, the return furnished under such scheme shall be deemed to be return furnished under sub-section (1) of section 139.

11.1.5 Return of Loss [Section 139(3)]

(1) This section requires the assessee to file a return of loss in the same manner as in the case of return of income within the time allowed under section 139(1).

(2) Under section 80, an assessee cannot carry forward or set off his loss against income in the same or subsequent year unless he has filed a return of loss in accordance with the provisions of section 139(3).

(3) A return of loss has to be filed by the assessee in his own interest and the non-receipt of a notice from the Assessing Officer requiring him to file the return cannot be a valid excuse under any circumstances for the non-filing of such return.

(4) In particular, a return of loss must be filed by an assessee who has incurred a loss under the heads "Profits and Gains from Business or Profession", "Capital Gains", and income from the activity of owning and maintaining race horses taxable under the head "Income from Other Sources".

(5) However, loss under the head "Income from House Property" under section 71B and unabsorbed depreciation under section 32 can be carried forward for set-off even though return of loss has not been filed before the due date.

Synopsis of Loss filing of return is as follows :

Section Ref.	Nature of Loss	Filing of Return
71B	Loss under the head Income from House Property	Loss return must be filed
72	Business or Profession Loss	Loss return should be filed timely
73	Speculative Business Loss	Loss return should be filed timely
74	Loss under the head Capital Gains	Loss return should be filed timely
74A	Loss from the activity of owning and maintaining race horse	Loss return should be filed timely
32(2)	Unabsorbed Depreciation Allowance	Loss return should be filed

If return of Loss is not filed timely, the losses under section 72, 73, 74, and 74A could not be carried forward to subsequent years for set off.

11.1.6 Belated Return [Section 139(4)]

(1) Any person who has not furnished a return within the time allowed to him under section 139(1) or within the time allowed under a notice issued under section 142(1) may furnish the return for any Previous Year at any time -

    (i) before the expiry of one year from the end of the relevant Assessment Year; or

    (ii) before the completion of the assessment, whichever is earlier.

(2) Interest is required to be paid under section 234A, as stated earlier.

(3) A penalty of ₹ 5,000 may be imposed under section 271F if belated return is submitted after the end of Assessment Year.

11.1.7 Return of Income of Charitable Trusts and Institutions [Section 139(4A)]

(1) Every person in receipt of income –

- (i) derived from property held under a trust or any other legal obligation wholly or partly for charitable or religious purpose; or
- (ii) by way of voluntary contributions on behalf of such trust or institution must furnish a return of income if the total income in respect of which he is assessable as a representative assessee, computed before allowing any exemption under sections 11 and 12 exceeds the basic exemption limit.

(2) Such persons should furnish the return in the prescribed form and verified in the prescribed manner containing all the particulars prescribed for this purpose.

(3) This return must be filed by the representative-assessee voluntarily within the time limit. Any failure on the part of the assessee would attract liability to pay interest and penalty.

11.1.8 Return of Income of Political Parties [Section 139(4B)]

(1) Under this section, a political party is required to file a return of income if, before claiming exemption under section 13A, the party has taxable income.

(2) The grant of exemption from Income-tax to any political party under section 13A is subject to the condition that the political party submits a return of its total income within the time limit prescribed under section 139(1).

(3) The chief executive officer of the political party is statutorily required to furnish a return of income of the party for the relevant Assessment Year, if the amount of total income of the Previous Year exceeds the basic exemption limit before claiming exemption under section 13A.

11.1.9 Return of Income of Research Associations etc. [Section 139(4C)]

Every—

(a) research association referred to in clause (21) of section 10;

(b) news agency referred to in clause (22B) of section 10;

(c) association or institution referred to in clause (23A) of section 10;

(d) institution referred to in clause (23B) of section 10;

(e) fund or institution referred to in sub-clause (iv) or trust or institution referred to in sub-clause (v) or any university or other educational institution referred to in sub-clause (iiiab) or sub-clause (iiiad) or sub-clause (vi) or any hospital or other medical institution referred to in sub-clause (iiiac) or sub-clause (iiiae) or sub-clause (via) of clause (23C) of section 10;

(ea) Mutual Fund referred to in clause (23D) of section 10;

(eb) securitisation trust referred to in clause (23DA) of section 10;

(ec) venture capital company or venture capital fund referred to in clause (23FB) of section 10;

(f) trade union referred to in sub-clause (a) or association referred to in sub-clause (b) of clause (24) of section 10;

(g) body or authority or Board or Trust or Commission (by whatever name called) referred to in clause (46) of section 10;

(h) infrastructure debt fund referred to in clause (47) of section 10,

shall, if the total income in respect of which such research association, news agency, association or institution, fund or trust or university or other educational institution or any hospital or other medical institution or trade union or body or authority or Board or Trust or Commission or infrastructure debt fund [or Mutual Fund or securitisation trust or venture capital company or venture capital fund] is assessable, without giving effect to the provisions of section 10, exceeds the maximum amount which is not chargeable to income-tax, furnish a return of such income of the previous year in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed and all the provisions of this Act shall, so far as may be, apply as if it were a return required to be furnished under sub-section (1).

11.1.10 Return of Income of University or College or Other Institution [Section 139(4D)]

Every university or college or other institution referred to in clause (ii) and clause (iii) of sub-section (1) of section 35, which is not required to furnish return of income or loss under any other provision of this section, shall furnish the return in respect of its income or loss in every Previous Year and all the provisions of this Act shall, so far as may be, apply as if it were a return required to be furnished under sub-section (1).

11.1.11 Return of income of business trust which is not covered in any other provision of the Act [Section 139(4E)]

Every business trust, which is not required to furnish return of income or loss under any other provisions of this section, shall furnish the return of its income in respect of its income or loss in every previous year and all the provisions of this Act shall, so far as may be, apply if it were a return required to be furnished under sub-section (1).

Investment fund referred to in section 115UB mandatory required to furnish return of income [Section 139(4F)] [Inserted w.e.f. A.Y. 2016-17]

Every investment fund referred to in section 115UB, which is not required to furnish return of income or loss under any other provisions of this section, shall furnish the return of income in respect of its income or loss in every previous year and all the provisions of this Act shall, so far as may be, apply as if it were a return required to be furnished under section 139(1).

11.1.12 Revised Return [Section 139(5)]

(1) If any person having furnished a return under section 139(1) or in pursuance of a notice issued under section 142(1), discovers any omission or any wrong statement therein, he may furnish a revised return at any time before the expiry of one year from the end of the relevant Assessment Year or before completion of assessment, whichever is earlier.

In other words :

Such return can be submitted at any time :-

(a) before the expiry of one year from the end of the relevant Assessment Year; or

(b) before the completion of assessment

Whichever is earlier

(2) It may be noted that a belated return cannot be revised. It has been held in Kumar Jagdish Chandra Sinha vs. CIT 1996 86 Taxman 122 (SC) that only a return furnished under section 139(1) or in pursuance of a notice under section 142(1) can be revised. A belated return furnished under section 139(4), therefore, cannot be revised.

A return cannot be revised for any kind of omission or wrong statement. Such omission or wrong statement in the original return must be due to a bona fide inadvertence or mistake on the part of the assessee [Sunanda Ram Deka vs. CIT (1994) 210 ITR 988 (Gau)].

Further, such a bona fide mistake or omission must be discovered by the assessee himself. In case such an omission or mistake is discovered by the Assessing Officer during the assessment proceedings, a revised return filed at that stage will not be a return under section 139(5) [CIT vs. Haji P. Mohammed (1981) 132 ITR 623 (Ker)].

Moreover, unless the omission or a wrong statement has a bearing on assessment, a subsequent return correcting it does not fall within section 139(5) [Halima Fancy Stores vs. CIT(1916) 104 ITR 190 (Mad)].

A revised return cannot be filed where assessee merely changes status and the accounting year or method of accounting [Deepnarain Nagu & Co. vs. CIT (1986) 157 ITR 37 (MP)].

If the assessee discovers any omission or any wrong statement in a revised return, it is possible to revise such a revised return provided it is revised within the same prescribed time [Niranjan Lai Ram Chandra vs. CIT (1982) 134 ITR 352 (All); CIT vs. Shrivastava (Dr N.) (1988) 170 ITR 556 (MP)].

Once a revised return is filed, the originally filed return must be taken to have been withdrawn and substituted by the revised return [Dhampur Sugar Mills Ltd. vs. CIT (1973) 90 ITR 236 (All)]. Thus where a return was filed under section 139(1) declaring income and later it is revised declaring a loss, the loss shall be allowed to be carried forward as the revised return shall substitute the original return which was filed within time.

Similarly, where a return is filed declaring a loss within the time allowed under section 139(1) and such loss is increased in the revised return, such higher loss will be eligible for being carried forward [CIT vs. Periyar District Co-op. Milk Producers Union Ltd (2004) 266 ITR 705 (Mad)].

As per the law, a return can be revised at any time before the expiry of one year from the end of the relevant assessment year or before the completion of assessment, whichever is earlier. Issue of notice under section 143(2) or show cause notice under section 144 means that the assessment is not yet completed. Therefore, original return, if submitted within the due date, can be revised even after issue of such notice. But the penalty under section 271(1)(c) for concealment of income may be levied on the additional income disclosed in the revised return.

To sum up, return of income can be revised if the following conditions are satisfied:

(i) a return has already been filed on or before the due date mentioned under section 139(1) or within the prescribed time in response to a notice under section 142(1);

(ii) the assessee, after filing the above return, discovers any omission/ wrong statement in the return;

(iii) revised return should be filed within one year from the end of the relevant assessment year or before completion of the assessment, whichever is earlier.

However, there is a distinction between a revised return and a correction of the return. If the assessee files some application for correcting a return already filed or making amends therein, it would not mean that he has filed a revised return. It will still retain the character of an original return but once a revised return is filed, the original return must be taken to have been withdrawn and to have been substituted by a fresh return for the purposes of assessment [Gopaldas Parshottamdas vs. CIT (1941) 9ITR 130 (All)].

A letter addressed to the Assessing Officer informing him that a certain items of income not mentioned in the original return be taken to be the income of the assessee would not be a proper revised return under sub-section (5) [Woman Padmanabh Dande vs. CIT(1952) 22 ITR 339 (Nag)].

Further, a revised return does not always spare penalty, where such revised return has been filed after concealment has been brought home. The assessee had admitted that 50% to 70% of his receipt is not recorded, but he claimed that he had admitted the same only during search in a spirit of co-operation in order to avoid penalty and prosecution. The first appellate authority deleted the penalty on the ground that the return was voluntary before proceedings were taken on the returns filed, while the Tribunal endorsed the decision on the ground that it was a matter of bargain between the assessee and the Department and that penalty is exonerated on revised return filed in pursuance of such bargain. The High Court held that the revised return could not be treated as purely voluntary especially, since the assessee had admitted concealment during search [CIT vs. Dr A. Mohd. Abdul Khadir (2003) 260 ITR 650 (Mad)].

Case Laws

(1) The original return was filed claiming depreciation as per law. A revised return was filed withdrawing claim of depreciation. It was held such a return could not be held to be a valid return under section 139(5) [CIT vs. Andhra Cotton Mills Ltd (1996) 219 ITR 404 (AP)].

(2) Where the assessee trust was statutorily required to file Auditor's Report with its return did not file the

same with the original return, there was a clear omission in the return filed and hence the assessee was entitled to file the same with a revised return [CIT vs. Sri Baldeoji Maharaj Trust (1983) 142 ITR 584 (All)].

(3) Where an application is filed by the assessee for making correction or for making some amendment in the originally filed return, it would not mean that he has filed a revised return. But once a revised return is filed, the originally filed return must be taken to have been withdrawn and substituted by the revised return [Dhampur Sugar Mills Ltd vs. CIT (1973) 90 ITR 236 (All)].

11.1.13 Particulars required to be furnished with the Return [Section 139(6)]

The prescribed form of the return shall, in certain specified cases, require the assessee to furnish the particulars of -

(i) income exempt from tax

(ii) assets of the prescribed nature, value and belonging to him

(iii) his bank account and credit card held by him

(iv) expenditure exceeding the prescribed limits incurred by him under prescribed heads

(v) such other outgoings as may be prescribed.

(vi) assets of the prescribed nature and value, held by him as a beneficial owner or otherwise or in which he is a neneficiary.

11.1.14 Defective Return [Section 139(9)]

(1) Under this sub-section, the Assessing Officer has the power to call upon the assessee to rectify a defective return.

(2) Where the Assessing Officer considers that the return of income furnished by the assessee is defective, he may intimate the defect to the assessee and give him an opportunity to rectify the defect within a period of 15 days from the date of such intimation. The Assessing Officer has the discretion to extend the time period beyond 15 days, on an application made by the assessee.

(3) If the defect is not rectified within the period of 15 days or such further extended period, then the return would be treated as an invalid return. The consequential effect would be the same as if the assessee had failed to furnish the return.

(4) Where, however, the assessee rectifies the defect after the expiry of the period of 15 days or the further extended period, but before assessment is made, the Assessing Officer can condone the delay and treat the return as a valid return.

(5) A return can be treated as defective if it is not properly filled in or the necessary enclosures are not accompanying the return or it is filed without payment of self-assessment tax.

Specific defects are only illustrative and not exhaustive - CIT vs. Rai Bahadur Bissesswarlal Motilal Malwasie Trust 195 ITR 825.

11.1.15 Permanent Account Number (PAN) [Section 139A]

(1) Where any person in the following category has not been allotted a Permanent Account Number (PAN), he should apply to the Assessing Officer within the prescribed time for allotment of a PAN -

  (i) Every person whose total income or the total income of any other person in respect of which the person is assessable under this Act during any Previous Year exceeded the basic exemption limit; or

  (ii) Every person carrying on any business or profession whose total sales, turnover or gross receipts exceeds or is likely to exceed ₹5 lakhs in any Previous Year; or

  (iii) Every person who is required to furnish a return of income under section 139(4A); or

(2) The CBDT had introduced a new scheme of allotment of computerized 10 digits PAN. Such PAN comprises of 10 alphanumeric characters and is issued in the form of a laminated card.

(3) All persons who were allotted PAN (Old PAN) earlier and all those persons who were not so allotted but were required to apply for PAN, shall apply to the Assessing Officer for a new series PAN within specified time.

(4) Once the new series PAN is allotted to any person, the old PAN shall cease to have effect. No person who has obtained the new series PAN shall apply, obtain or process another PAN.

(5) On receipt of allotment of PAN it must be mentioned on all tax payment challans, returns, correspondence.

(6) Where TDS or TCS is made, the person from whom it is made must communicate his PAN to the person deducting or collecting tax.

(7) Every person receiving any document relating to a transaction prescribed under clause (c) of sub-section (5) shall ensure that the Permanent Account Number or the General Index Register Number has been duly quoted in the document.

The Assessing Officer having regard to the nature of transactions as may be prescribed may also allot a Permanent Account Number to any other person (whether any tax is payable by him or not) in the manner and in accordance with the procedure as may be prescribed.

However, any person, not falling under any clause above, may suo moto apply to the Assessing Officer for the allotment of a Permanent Account Number and, thereupon, the Assessing Officer shall allot a permanent account number to such person forthwith.

The PAN application shall be accompanied by the following documents as proof of identity and address of the applicant:

Sl. No.	Applicant	Documents as proof of identity and address
1.	Individual	(i) Proof of identity — Copy of school leaving certificate or matriculation certificate or degree of a recognized educational institution or depository account or credit card or bank account or water bill or ration card or property tax assessment order or passport or voter identity card or driving license or certificate of identity signed by a Member of Parliament or Member of Legislative Assembly or Municipal Councillor or a Gazetted Officer, as the case may be. In case of a person being a minor, any of the above documents of any of the parents or guardian of such minor shall be deemed to be the proof of identity. (ii) Proof of address — Copy of electricity bill or telephone bill or depository account or credit card or bank account or ration card or employer certificate or passport or voter identity card or property tax assessment order or driving license or rent receipt or certificate of address signed by a Member of Parliament or Member of Legislative Assembly or Municipal Councillor or a Gazetted Officer, as the case may be. In case of a person being a minor, any of the above documents of any of the parents or guardian of such minor shall be deemed to be the proof of address.
2.	Hindu Undivided Family	Copy of any document applicable in the case of an individual, in respect of Karta of the Hindu Undivided Family, as proof of identity and address.
3.	Company	Copy of Certificate of Registration issued by the Registrar of Companies.

4.	Firm	Copy of Certificate of Registration issued by the Registrar of Firms or copy of Partnership Deed.
5.	Association of Persons (Trusts)	Copy of Trust Deed or copy of Certificate of Registration Number issued by Charity Commissioner.
6.	Association of Persons (other than Trusts) or Body of Individuals or Local Authority or Artificial Juridical Person	Copy of Agreement or Copy of Certificate of Registration number issued by Charity Commissioner or Registrar of Co-operative Society or any other Competent Authority or Any other document originating from any Central or State Government Department establishing identity and address of such person

Time limit for submitting application for allotment of PAN is as under:

Situation	**Time limit for a making application**
If his total income or the total income of any other person in respect of which he is assessable under this Act during any previous year exceeded the maximum amount which is not chargeable to income-tax.	on or before 31st May of the assessment year in which such income is assessable
If he is carrying on any business or profession whose total sales turnover or gross receipt are or is likely to exceed ₹5,00,000 in any previous year.	on or before the end of that accounting year
If he is required to furnish a return of income under section 139(4A), i.e. return of trust and charitable institutions.	on or before the end of the relevant accounting year
If he is a person who is not required to apply for PAN under any of the above clauses	application can be made at any time

With a view to progressively making PAN a common business identification number for other departments such as the Central Board of Excise and Customs and the Director General of Foreign Trade, the Act has delegated the power to the Central Government to notify class or classes of persons for whom it will be obligatory to apply for PAN, provided tax is payable by them under the Income-tax Act or any tax or duty is payable by them under any other law in force including importers and exporters whether any tax is payable by them or not.

The Central Government by Notification No. 11468, dated 29-8-2000 has notified the following class or classes of persons who shall apply to the Assessing Officer for allotment of Permanent Account Number:—

(i) Exporters and Importers as defined in section 2(20) and section 2(26) of the Customs Act, 1962, who are required to obtain an importer-exporter code under section 7 of the Foreign Trade (Development and Regulations) Act, 1992.

(ii) Assessees as defined in rule 2(3) of Central Excise Rules, 1944.

(iii) Persons who issue invoices of Cenvat i.e. traders, etc. requiring registration under Central Excise Rules, 1944.

(iv) Persons who are assessees under service tax.

The above persons shall apply for allotment of PAN within 15 days of the date of publication of the notification in the Official Gazette. However, persons who may fall in the above category, after the date of the above notification, shall apply for allotment of PAN:—

(a) in case of (i) above, before making an import or export;

(b) in case of (ii) and (iii) above, before making an application for registration under Central Excise;

(c) in case of (iv) above, before making an application for registration under service tax.

The Central Government, by Notification No. 355/2001, dated 11-12-2001 has further notified the following class or classes of persons:

(1) Persons registered under the Central Sales Tax Act, 1956 or the General Sales Tax Law of the appropriate State or Union Territory, as the case may be.

(2) As on the date of this notification, a person falling within a class or classes of persons referred to in paragraph 1, shall apply for the allotment of Permanent Account Number within thirty days of the date of publication of this notification in the Official Gazette.

(3) A person who may fall within such class or classes of persons after the date of this notification, as is referred to in paragraph 1, shall apply for the allotment of Permanent Account Number (PAN) before making any application for registration under the Central Sales Tax Act, 1956 or the General Sales Tax Law of the appropriate State or Union territory, as the case may be.

Further, the Central Government may, for the purpose of collecting any information which may be useful for or relevant to the purposes of this Act, by way of notification specify any class or classes of persons, and such persons shall within the prescribed time apply to the Assessing Officer for allotment of a Permanent Account Number.

On allotment of Permanent Account Number, every person shall:

(a) quote such number in all his returns to, or correspondence with, any income-tax authority;

(b) quote such number in all challans for the payment of any sum due under this Act;

(c) quote such number in all documents pertaining to such transactions as may be prescribed by the Board in the interests of the revenue, and entered into by him.

Following are the transactions where quoting PAN has been made compulsory as per section 139A(5)(c) and rule 114B:

(a) sale/purchase of any immovable property valued at ₹5 lakh or more.

(b) sale/purchase of motor vehicle (other than two wheeled vehicles) which requires registration under Motor Vehicles Act, 1988.

(c) Time deposit exceeding ₹50,000 with a bank/banking company/ banking institution.

(d) Deposits exceeding ₹50,000 in Post Office Savings Bank.

(e) Contract for sale/purchase of securities exceeding ₹1,00,000.

(f) Opening an account with a bank/banking company/banking institution. Where the person opening a bank account is a minor and does not have any income chargeable to income-tax, he shall quote the PAN/GIR number of his father or mother or guardian as the case may be.

(g) Application for installation of a telephone connection including cellular connection.

(h) Payment to hotels/restaurants of bills exceeding ₹25,000 at any time.

(i) payment in cash for purchase of bank draft or pay orders or banker's cheques from a banking company to which the Banking Regulation Act, 1949, applies (including any bank or banking institution referred to in section 51 of that Act) for an amount aggregating ₹50,000 or more during any one day;

(j) Deposit in cash aggregating ₹50,000 or more, with a banking company to which the Banking Regulation Act, 1949, applies (including any bank or banking institution referred to in section 51 of that Act) during any one day;

(k) Payment in cash in connection with travel to any foreign country of an amount exceeding ₹25,000 at any one time. Such payment shall include payment in cash towards fare, or to a travel agent or a tour operator, or for the purchase of foreign currency. However, travel to any foreign country does not include travel to the neighbouring countries or to such places of pilgrimage as may be specified by the Board under Explanation 3 of section 139(1).

(l) Making an application to any banking company to which the Banking Regulation Act, 1949, applies (including any bank or banking institution referred to in section 51 of that Act) or to any other company or institution, for issue of a credit card;

(m) Payment of an amount of ₹50,000 or more to a Mutual Fund for purchase of its units;

(n) Payment of an amount of ₹50,000 or more to a company for acquiring shares issued by it;

(o) Payment of an amount of ₹50,000 or more to a company or an institution for acquiring debentures or bonds issued by it;

(p) Payment of an amount of ₹50,000 or more to the Reserve Bank of India, for acquiring bonds issued by it.

Provided any person who has not been allotted a Permanent Account Number and who enters into any of the above transactions and makes the payment in cash or otherwise than by way of a crossed cheque drawn on a bank or through credit card issued by any bank shall make a declaration in Form No. 60 giving therein the particulars of such transaction.

Where a person, making an application for opening an account referred to in clause (c) and clause (f) of this rule, is a minor and who does not have any income chargeable to income-tax, he shall quote the Permanent Account Number of his father or mother or guardian, as the case may be, in the document pertaining to the transaction referred to in the said clause (c) and clause (f).

The above provisions shall not apply to as per rule 114C (1):

(a) Persons who have 'agricultural income' and are not in receipt of any other income chargeable to income-tax. Such person shall make a declaration in Form No. 61.

(b) Central Government, State Government and Consular Offices in transactions where they are the payers.

The assessee shall intimate the Assessing Officer any change in his address or in the name and nature of his business on the basis of which the Permanent Account Number was allotted to him.

The sub-sections (5A) and (5B) shall not apply in case of a person.

(a) whose total income is not chargeable to tax; or

(b) who is not required to obtain PAN under any provisions of the Income-tax Act

such person will be required to furnish a declaration referred to in section 197A in the prescribed form to the effect that the tax on his estimated total income of the previous year will be nil. However, in this case also w.e.f. 1-4-2010, quoting of PAN shall be mandatory in the declaration made in Form No. 15G or 15H, otherwise such declaration shall not be valid.

In case of PAN, the obligations of deductee / buyer and deductor/seller are as follows:

(1) Obligation of a person receiving any sum/income/amount from which tax has been deducted at source [Section 139A(5A)]: Such person (including non-resident) shall intimate his PAN to the person responsible for deducting tax.

(2) Obligation of a person who has deducted the tax at source [Section 139A(5B)]: Where any sum or income or amount has been paid after deducting tax, every such person deducting tax shall quote the PAN of the person to whom sum/income/amount has been paid by him in:

(a) the statement of perquisites furnished to the employee in accordance with the newly inserted Section 192(2C);

(b) all certificates of TDS furnished under section 203;

(c) in all quarterly statements prepared and delivered or caused to be delivered in accordance with the provisions of section 200(3).

However, the Central Government may notify different dates from which the provisions of this sub-section shall apply in respect of any class or classes of persons.

(3) Obligation of a buyer, licensee, lessee or seller of alcoholic liquor, timber or any other forest products referred to in section 206C

(a) Obligation of the buyer or licensee or lessee [Section 139A(5C)]: Every such buyer, licensee or lessee shall intimate his PAN to the seller of such goods.

(b) Obligation of the seller of such goods [Section 139A(5D)]: Every seller, collecting tax under section 206C shall quote the PAN of every buyer, licensee or lessee:—

(i) in all certificates furnished to the buyer/licensee/lessee under section 206C;

(ii) in all quarterly statements prepared and delivered or caused to be delivered in accordance with the provisions of section 206C(3).

As per section 272B(1), where any person fails to comply with the provisions of section 139A, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of ₹10,000.

As per section 272B(2), if a person who is required to—

(a) quote the Permanent Account Number in any document referred to in section 139A(5)(c); or

(b) intimate such number as required under section 139A(5A), or

(c) intimate such number as required under section 139A(5C).

quotes or intimates a number which is false, and which he either knows or believes to be false or does not believe to be true, the Assessing Officer may direct that such person shall pay, by way of penalty, a sum of ₹10,000.

11.1.16 Scheme for Submission of Returns through Tax Return Preparers [Section 139B]

(1) The Tax Return Preparer shall assist the specified class or classes of person in furnishing the return in a manner that will be specified in the Scheme, and shall also affix his signature on such return. The "specified class or classes of persons" for this purpose means any person other than a company or a person whose accounts are required to be audited under section 44AB (tax audit) or under any other existing law, who is required to furnish a return of income under the Act.

(2) A Tax Return Preparer can be an individual, other than

(i) any officer of a scheduled bank with which the assessee maintains a current account or has other regular dealings.

(ii) any legal practitioner who is entitled to practice in any civil court in India.

(iii) a chartered accountant.

(iv) an employee of the 'specified class or classes of persons'.

(3) The Scheme notified under the said section may provide for the following —

  (i) The manner in which and the period for which the Tax Return Preparers shall be authorised,

  (ii) The educational and other qualifications to be possessed, and the training and other conditions required to be fulfilled, by a person to act as a Tax Return Preparer,

  (iii) The code of conduct for the Tax Return Preparers,

  (iv) The duties and obligations of the Tax Return Preparers,

  (v) The circumstances under which the authorisation given to a Tax Return Preparer may be withdrawn, and

  (vi) Any other relevant matter as may be specified by the Scheme.

11.1.17 Power of Board to dispense with furnishing documents, etc. with the Return [Sec. 139C]

(1) The Board may make rules providing for a class or classes of persons who may not be required to furnish documents, statements, receipts, certificates, reports of audit or any other documents, which are otherwise under any other provisions of this Act, except section 139D, required to be furnished, along with the return but on demand to be produced before the Assessing Officer.

(2) Any rule made under the proviso to sub-section (9) of section 139 as it stood immediately before its omission by the Finance Act, 2007 shall be deemed to have **been made under the provisions of this section.**

11.1.18 Filing of return in electronic from [Sec. 139D]

The Board may make rules providing for —

(a) the class or classes of persons who shall be required to furnish the return in electronic form;

(b) the form and the manner in which the return in electronic form may be furnished;

(c) the documents, statements, receipts, certificates or audited reports which may not be furnished along with the return in electronic form but shall be produced before the Assessing Officer on demand;

(d) the computer resource or the electronic record to which the return in electronic form may be transmitted.

11.1.19 Return by whom to be signed [Section 140]

The return under **section 139** shall be verified as under:

Sr. No.	Assessee Category	Who can verify
1	Individual	(i) By the individual himself; (ii) Where he is absent from India, by the individual himself or by some person duly authorised by him in this behalf; (iii) Where he is mentally incapacitated from attending to his affairs, by his guardian or any other person competent to act on his behalf; and (iv) Where, for any other reason, it is not possible for the individual to verify the return, by any person duly authorised by him in this behalf
2	Hindu Undivided Family (HUF)	By the Karta or where the Karta is absent from India or is mentally incapacitated from attending to his affairs, by any other adult member of such family

3	Company	Managing director or where for any unavoidable reason, managing director is not able to verify or where there is no managing director, by any director thereof. Exceptions : (*a*) Where the company is being wound up : by the liquidator (*b*) Where the management of the company has been taken over by the Government : the principal officer thereof (*c*) Company is not resident in India : a person who holds a valid power of attorney
4	A Firm / Limited Liability Partnership (w.e.f. A.Y 2010-11)	Managing partner or where for any unavoidable reason managing partner is not able to verify the return, or where there is no managing partner, by any partner thereof
5	A Local Authority	The Principal officer thereof
6	A Political Party	The Chief Executive Officer of such party
7	Any other Association	Any Member of the Association or the Principal Officer thereof
8	Any other Person	By that person or by some person competent to act on his behalf

If the Hindu Undivided Family has no major members as its Karta, a return may validly be signed by the eldest minor member of the family who manages the affairs of the family [Sridhar Udai Narayan vs. CIT (1962) 45 ITR 577 (All)].

The General Clauses Act accepts the thumb impression, as one of the modes of signing, valid and binding [CIT vs. Kanhaiya Lai And Sons (2005) 273 ITR 425 (All)].

A return which is not signed or verified is not a defective return but an invalid return and therefore, it is no return in the eyes of law [CIT vs. Krishan Lai Goyal (Dr) (1984) 148 ITR 283 (P&H); Khialdas & Sons vs. CIT (1997) 225 ITR 960 (MP)].

A notice issued under section 143(2) in response to an unsigned and unverified return does not validate such invalid return [Electrical Instrument Company vs. CIT(2001) 250 ITR 734 (Del)].

Return of company not signed by person mentioned in section 140: Return signed and verified not by the assessee but by a person not properly authorised or empowered is an invalid return and thus void ab-initio [Behari Lai Chatterji vs. CIT (1934) 2 ITR 377 (All); Shridhar Udai Narayan vs. CIT45 ITR 577 (All)].

Where a return of income of a company was signed by a company secretary although it was supposed to sign by managing director or in the absence of managing director by any director, such a return would not be treated as invalid if inspite of defect return is in substance and effect in conformity with or according to interest and purpose of Act. Such defect can be cured by virtue of section 139(5) [Prime Securities Ltd vs. ACIT (2009) 182 Taxman 221 (Bom)].

Board has the power under section 119(2)(b) to condone the delay in filing the loss return and allowed to be carried forward [Lodhi Property Company Ltd vs. Under Secretary Department of revenue (2010) 234 CTR 99 (Del)].

Where return of income filed by assessee was neither signed by her, nor was it verified in terms of mandate of section 140, it was held that such glaring inherent defect could not be cured in spite of deeming effect of section 292B and the Assessing Officer cannot make an assessment on a invalid return [CIT vs. Harjinder Kaur (2009) 180 Taxman 23 (P&H)].

11.1.20 Prescribed Forms:

Forms	Applicability
ITR-1 (SAHAJ)	For individual having income from salary/ one house property (not being brought forward loss from Previous Years)/ income from other sources (except winning from lotteries and income from race horses)
ITR-2	For individuals and HUFs not having business or professional income
ITR-3	For individual or HUFs being partners in firms and not carrying out business or profession under any proprietorship
ITR-4	For individual and HUFs having income from a proprietary business or profession
ITR-4S(SUGAM)	For individual or HUF deriving business income and such income is computed in accordance with special provision referred to in sections 44AD and 44AE
ITR-5	For firms, AOPs and BOIs or any other person (not being individual or HUF or company or to whom ITR-7 is applicable)
ITR-6	For companies other than companies claiming exemption under section 11
ITR-7	For persons including companies required to furnished return under section 139(4A)/(4B)/(4C)/(4D)
ITR-V	Where the data of the return of income in forms ITR-1, ITR-2, ITR-3, ITR-4, ITR-5 and ITR-6 transmitted electronically without digital signature.

11.1.21 Self Assessment Tax Payment [Section 140A]

(1) Where any tax is payable on the basis of any return required to be furnished under section 139 or section 142 or section 148 or section 153A or, as the case may be, section 158BC, *after taking into account taxes paid earlier*. The assessee shall be liable to pay such tax together with interest payable under any provision of this Act for any delay in furnishing the return or any default or delay in payment of advance tax, before furnishing the return and the return shall be accompanied by proof of payment of such tax and interest.

(2) If assessee fails to pay the whole or any part of such tax or interest or both on self assessment, the assessee shall be deemed to be an assessee in default in respect of the tax or interest or both remaining unpaid. Penalty can be imposed on any assessee who is in default.

(3) **With effect from the Assessment Year 2013-14,** the amount of credit available to be set off according to the provisions of section 115JD (Alternative Minimum Tax) will also be taken into account u/s 140A for the purpose of computing the amount of tax payable and interest chargeable under section 234A, 234B and 234C before filing the return of income.

11.2 ANNUAL INFORMATION RETURN [SECTION 285BA]

11.2 OBLIGATION TO FURNISH STATEMENT OF FINANCIAL TRANSACTION OR REPORTABLE ACCOUNT [SECTION 285BA]

(1) Any person, being—

(a) an assessee; or

(b) the prescribed person in the case of an office of Government; or

(c) a local authority or other public body or association; or

(d) the Registrar or Sub-Registrar appointed under section 6 of the Registration Act, 1908; or

(e) the registering authority empowered to register motor vehicles under Chapter IV of the Motor Vehicles Act, 1988; or

(f) the Post Master General as referred to in clause (i) of section 2 of the Indian Post Office Act, 1898; or

(g) the Collector referred to in clause (g) of section 3 of the Right to Fair Compensation and Transparency in Land Acquisition, Rehabilitation and Resettlement Act, 2013; or

(h) the recognised stock exchange referred to in clause (f) of section 2 of the Securities Contracts (Regulation) Act, 1956; or

(i) an officer of the Reserve Bank of India, constituted under section 3 of the Reserve Bank of India Act, 1934; or

(j) a depository referred to in clause (e) of sub-section (1) of section 2 of the Depositories Act, 1996; or

(k) a prescribed reporting financial institution,

who is responsible for registering, or, maintaining books of account or other document containing a record of any specified financial transaction or any reportable account as may be prescribed under any law for the time being in force, shall furnish a statement in respect of such specified financial transaction or such reportable account which is registered or recorded or maintained by him and information relating to which is relevant and required for the purposes of this Act, to the income-tax authority or such other authority or agency as may be prescribed.

(2) The statement referred to in sub-section (1) shall be furnished for such period, within such time and in the form and manner, as may be prescribed.

(3) For the purposes of sub-section (1), "specified financial transaction" means any—

(a) transaction of purchase, sale or exchange of goods or property or right or interest in a property; or

(b) transaction for rendering any service; or

(c) transaction under a works contract; or

(d) transaction by way of an investment made or an expenditure incurred; or

(e) transaction for taking or accepting any loan or deposit,

which may be prescribed:

Provided that the Board may prescribe different values for different transactions in respect of different persons having regard to the nature of such transaction.

Provided further that the value or, as the case may be, the aggregate value of such transactions during a financial year so prescribed shall not be less than fifty thousand rupees.

(4) Where the prescribed income-tax authority considers that the statement furnished under sub-section (1) is defective, he may intimate the defect to the person who has furnished such statement and give him an opportunity of rectifying the defect within a period of thirty days from the date of such intimation or within such further period which, on an application made in this behalf, the said income-tax authority may, in his discretion, allow; and if the defect is not rectified within the said period of thirty days or, as the case may be, the further period so allowed, then, notwithstanding anything contained in any other provision of this Act, such statement shall be treated as an invalid statement and the provisions of this Act shall apply as if such person had failed to furnish the statement.

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

(6) If any person, having furnished a statement under sub-section (1), or in pursuance of a notice issued under sub-section (5), comes to know or discovers any inaccuracy in the information provided in the statement, he shall within a period of ten days inform the income-tax authority or other authority or agency referred to in sub-section (1), the inaccuracy in such statement and furnish the correct information in such manner as may be prescribed.

(7) The Central Government may, by rules made under this section, specify—

(a) the persons referred to in sub-section (1) to be registered with the prescribed income-tax authority;

(b) the nature of information and the manner in which such information shall be maintained by the persons referred to in clause (a); and

(c) the due diligence to be carried out by the persons for the purpose of identification of any reportable account referred to in sub-section (1).

11.3 ASSESSMENT PROCEDURE

11.3.1 Inquiry before assessment [Section 142]

Inquiry :

(1) The Assessing Officer has power to make inquiry from any person (a) who has made a return under section 139 or (b) in whose case the time allowed under sub-section (1) or sub-section (4) of section 139 for furnishing the return has expired. For this purpose a notice can be issued for :

(i) where such person has not made a return within the time allowed under section 139(1) or 139(4), to furnish a return of his income, or

(ii) to produce such accounts or documents as the Assessing Officer may require, or

(iii) to furnish in writing and verified in the prescribed manner information in such form and on such points or matters including a statement of all assets and liabilities of the assessee, whether included in the accounts or not, as the Assessing Officer may require

Provided that –

(i) Previous approval of Joint Commissioner shall be obtained before requiring the assessee to furnish a statement of all assets and liabilities not included in the accounts.

(ii) The Assessing Officer shall not require the production of any accounts relating to a period more than three years prior to the Previous Year.

(2) For the purpose of obtaining full information in respect of the income or loss of any person, the Assessing Officer may make such inquiry as he considers necessary.

Audit

If the Assessing Officer, having regard to the nature and complexity of the accounts, volume of the accounts doubts about the correctness of the accounts, multiplicity of transactions in the accounts or specialised nature of business activity of the assessee and the interests of the revenue, opines that it is necessary so to do, he may with the prior approval of the Chief Commisioner or Commisioner, direct the assessee to get the accounts audited by an accountant, as defined in the *Explanation* below section 288(2) and to furnish an audit report, within such period as may be specified, in the prescribed form. The expenses of such audit shall be paid by the assessee

These provisions of audit shall have effect notwithstanding that the accounts of the assessee have been already audited.

The direction to get accounts audited can be issued only in the course of assessment proceeding which is pending and not after the completion of assessment [Kumar Films Pvt. Ltd vs. CIT (2002) 258 ITR 257 (Patna)]. Further the assessment also includes reassessment.

The Chartered Accountant shall submit the audit report in Form No. 6B to the assessee who will in turn submit it to the Assessing Officer within such period as may be specified by the Assessing Officer [Section 142(2C)]. Such period may, however, be extended by the Assessing Officer suo motu or on the request of the assessee and for any good and sufficient reasons. The aggregate of the period originally fixed and the extended period(s) shall not, in any case, exceed 180 days from the date on which the directions for audit were received by the assessee.

As per section 142(2D), where any direction for audit under section 142(2A) is issued by the Assessing Officer on or after 1-6-2007, the expenses of and incidental to such audit (including the remuneration of the accountant) shall be determined by the Chief Commissioner or Commissioner, in accordance with such guidelines as may be prescribed and the expenses so determined shall be paid by the Central Government.

The remuneration for special auditor to be fixed by the Commissioner as per the scale approved by the ICAI, subject to maximum of ₹ 30 lakh per year. Ad hoc remuneration of ₹20 lakh fixed by the Commissioner was set aside [Dhanesh Gupta & Co. vs. CIT (2010) 42 DTR 7 (Del)].

The twin pre-conditions justifying the special audit under section 142(2A) of the Income-tax Act, 1961 are, the nature and complexity of the accounts and the interests of the Revenue. Before an approval is sought for, the assessing authority must form an opinion as regards the said twin conditions. There should be an honest attempt to understand the books of account of the assessee. There has to be an application of mind on the part of the assessing authority. Complexity of the accounts cannot be equated with doubts being entertained by the assessing authority either with regard to the correctness thereof or the need for obtaining certain vital information not ascertainable from the accounts. The satisfaction is to be based upon objective considerations [Bata India Ltd. vs. CIT (2002) 257 ITR 622 (Cal)].

Special audit can also be ordered so as to protect the interest of the revenue. Such object may or may not be achieved by the audit contemplated by section 44AB [Super Cassettes Industries Ltd. vs. Asst CIT (1999) 102 Taxman 202 (Del)].

The power under section 142(2A) can be invoked when the Assessing Officer finds that accounts are complicated. The overlapping in certain situation with regard to section 44AB and section 142(2A) do not render the provisions either void or superfluous [Narinder Singh Atwal vs. DCIT (1998)231ITR641(Cal)].

It is the duty of the Commissioner to examine whether the Assessing Officer has examined the books of accounts properly before giving his approval for the special audit under section 142(2A). Approval of special audit cannot be given by the Commissioner mechanically. In the instant case the Assessing Officer, had neither formed any opinion nor given a direction for production of the accounts. The Commissioner should have examined whether the proposal of the Assessing Officer for special audit deserved to be approved. The High Court, therefore, set aside the order for special audit under section 142(2A) [West Bengal State Co-operative Bank Ltd vs. Joint Commissioner of Income Tax (2004) 267 ITR 345 (Cal)].

The Assessing Officer shall give an opportunity to the assessee of being heard in respect of any information gathered by the Assessing Officer on the basis of the aforesaid inquiry under section 142(2) or on the basis of the audit conducted as per section 142(2A) above, where the Assessing Officer proposes to utilise such information for the purpose of any assessment. However, no such opportunity is necessary when the assessment is made under section 144.

Failure to comply with notice under section 142(1) or to get accounts audited as per directions issued under section 142(2A) may result in:

(a) Best judgment assessment under section 144;

(b) Penalty under section 271(1)(b) which has been fixed at ₹10,000;

(c) Prosecution under section 276D with rigorous imprisonment which may extend to one year or with fine which will not be less than ₹4 or more than ₹10 for every day during which the default continues, or with both;

(d) Issue of a warrant of authorisation under section 132 for conducting search.

If the assessee proves that the non-compliance with the direction under section 142(2A) was not because of his fault but negligence or refusal of the auditor, then best judgment assessment shall not be made and the proceedings shall be dropped.

In Swadeshi Polytex Ltd. vs. ITO (1983) 144 ITR 171 (SC) the Supreme Court set aside an assessment made under section 144(1)(b) because of the refusal of the nominated auditor to undertake the audit for a frivolous reason and directed the assessment to be done afresh.

Opportunity to Assessee :

The assessee shall be given an opportunity of being heard in respect of any material gathered on the basis of any inquiry or any audit and proposed to be utilised for the purposes of the assessment. Such opportunity need not be given where the assessment is made under section 144.

11. 3. 2 Estimation of value of assets by valuation officer [Section 142A]

(1) The Assessing Officer may, for the purposes of assessment or reassessment, make a reference to a Valuation Officer to estimate the value, including fair market value, of any asset, property or investment and submit a copy of report to him.

(2) The Assessing Officer may make a reference to the Valuation Officer under sub-section (1) whether or not he is satisfied about the correctness or completeness of the accounts of the assessee.

(3) The Valuation Officer, on a reference made under sub-section (1), shall, for the purpose of estimating the value of the asset, property or investment, have all the powers that he has under section 38A of the Wealth-tax Act, 1957.

(4) The Valuation Officer shall, estimate the value of the asset," property or investment after taking into account such evidence as the assessee may produce and any other evidence in his possession gathered, after giving an opportunity of being heard to the assessee.

(5) The Valuation Officer may estimate the value of the asset, property or investment to the best of his judgment, if the assessee does not co-operate or comply with his directions.

(6) The Valuation Officer shall send a copy of the report of the estimate made under sub-section (4) or sub-section (5), as the case may be, to the Assessing Officer and the assessee, within a period of six months from the end of the month in which a reference is made under sub-section (1).

(7) The Assessing Officer may, on receipt of the report from the Valuation Officer, and after giving the assessee an opportunity of being heard, take into account such report in making the assessment or reassessment.

    Explanation.—In this section, "Valuation Officer" has the same meaning as in clause (r) of section 2 of the Wealth-tax Act, 1957.

Case Law :

Assessing Officer can look into documents other than books of account for issuing directions - Submission of audited accounts per se would not oust the jurisdiction of the Assessing Officer to pass a direction for special audit. While applying his mind, the Assessing Officer need not confine himself only to the books of account submitted by the assessee, but can take into consideration such other documents related thereto which would be part of the assessment proceedings - Rajesh Kumar Ors. vs. Dy. CIT.287 ITR 91.

11.3.3 Assessment [Section 143]

Assessment means the act of assessing. After the return of income submitted by assessee, the Department will then make the assessment in order to check whether the Total Income and the tax on that total income as computed by the assessee is correct or not. It will also check whether the penalty, interest, if any, leviable, is correctly added to the tax payable or not.

11.3.3.1 Summary Assessment [Section 143(1)]

Assessing Officer can complete the assessment without passing a regular assessment order. The assessment is completed on the basis of return submitted by the assessee.

Assessing Officer has adopted a two-stage procedure of assessment as part of risk management strategy. In the first stage, all tax returns are processed to correct arithmetical mistakes, internal inconsistencies, tax calculation and verification of tax payment. At this stage, no verification of the income is undertaken. In the second stage, certain percentage of the tax returns are selected for scrutiny/ audit on the basis of the probability of deducting tax evasion. At this stage, the tax administration is concerned with the verification of the income.

Total income of the assessee shall be computed under section 143(1) after making the following adjustments to the total income in the return -

(i) any arithmetical errors in the return; or

(ii) an incorrect claim, if such incorrect claim is apparent from any information in the return.

An intimation shall be sent to the assessee specifying the sum determined to be payable by, or the amount of refund due to, the assessee after the aforesaid corrections. The amount of refund due to the assessee shall be granted to him. No intimation shall be sent after the expiry of one year from the end of the financial year in which the return is made. The acknowledgement of the return shall be deemed to be the intimation in a case where no sum is payable by, or refundable to, the assessee, and where no adjustment has been made.

"An incorrect claim" apparent from any information in the return has been defined. It means claim on the basis of an entry, in the return -

(i) of an item, which is inconsistent with another entry of the same or some other item in such return;

(ii) information required to be furnished to substantiate such entry, has not been furnished under the Act; or

(iii) in respect of a deduction, where such deduction exceeds specified statutory limit which may have been expressed as monetary amount or percentage or ratio or fraction.

As per amendment in section 143(1D) provides that processing of a return under section 143(1) shall not be necessary, where a scrutiny notice has been issued to the assessee under sub-section (2) of Section 143 (w.e.f. July 1, 2012)

Adjustment through computerised processing only : All the adjustments such as arithmetical error, incorrect claim, etc. are made only in the course of computerised processing. For this purpose, a system of centralised processing of returns has been established by the Department. A software will be designed to detect arithmetical inaccuracies and internal inconsistencies and make appropriate adjustments in the computation of total income.

To facilitate this, the Board has formulated a scheme with view to expeditiously determine the tax payable by, or refund due to, the assessee.

11.3.3.2 Notice under section 143(2)

A notice shall be served on the asessee within a period of 6 months from the end of the financial year in which return is furnished. The notice requires the assessee to produce any evidence which the assessee may rely in support of the return.

If notice is sent to the assessee by registered post on last day of the period of limitation and it is served on the assessee a few days later, beyond period of limitation, it cannot be said to be validly served.

Distinction between notice under section 142(1) and section 143(2)

SL. No.	Notice under section 142(1)	Notice under section 143(2)
1.	It is a notice to file return of income or produce accounts or documents or furnish information as the Assessing Officer may require	It is a notice for making assessment under section 143(3)
2.	No assessment is possible by issue of this notice alone	Assessment can be made only if the notice under this section is served on the assessee.
3.	No time limit is prescribed for service of this notice	Time limit of 6 months is prescribed for service of this notice.
4.	Approval of Joint Commissioner necessary if statement of all assets and liabilities not included in accounts is required.	No approval required.
5.	Books of account can be asked for a maximum period of 3 years prior to the previous year	There is no such provision in this case.
6.	Notice can be served even if no return of income is furnished	Notice can be served only if the return of income has been furnished.
7.	Non-compliance with a notice under section 142(1) is an offence for which prosecution may be launched under section 276D.	Non-compliance of notice under section 143(2) is not an offence. Hence, prosecution cannot be launched under section 276D.

There is no sequence prescribed as to what manner notices under section 142(1) and 143(2) are to be issued, therefore, there is nothing to say that notice under section 142(1) should precede notice under section 143(2) [Orissa Rural Housing Development Corporation Ltd. vs. ACIT (2012) 66 DTK 73: 247 CTR (Ori)137].

11.3.3.3 Regular Assessment [Section 143(3)]

Where a return has been furnished under section 139, or in response to a notice under sub-section (1) of section 142, the Assessing Officer shall, if he considers it necessary or expedient to ensure that the assessee has not understated the income or has not computed excessive loss or has not under-paid the tax in any manner, serve on the assessee a notice requiring him under section 143(2)(ii), either to attend his office or to produce, any evidence on which the assessee may rely in support of the return.

On the day specified in the notice issued under section 143(2) or as soon afterwards as may be, after hearing such evidence as the assessee may produce and such other evidence as the Assessing Officer may require on specified points and after taking into account all relevant material which Assessing Officer has gathered, the Assessing Officer shall, by an order in writing, make an assessment of the total income or loss of the assessee, and determine the sum payable by him or refund of any amount due to him on the basis of such assessment.

Tax has to be determined and such determination is to be made in the assessment order or computation sheet to be annexed with the assessment order. [Kalyan Kumar Ray vs. CIT]

The assessed income may be lower than the returned income. The boards circular no 549 para 5.12 dt. 31.10.1989 has been held to be ultra-vires [Gujarat Gas Co Ltd vs. JCIT(A)]

If a notice under section 143(2) is not served, an assessment cannot be made under section 143(3).

Wherever an assessment is sought to be made under section 143(3), issuing and serving of valid notice under section 143(2) is a precondition and is mandatory [Rattan Lai Tiku vs. CIT (1974) 97 ITR 553 (J&K)].

Further, burden was upon the revenue to prove that the notice under section 143(2) was served upon the assessee within the prescribed time of 6 months from the end of the financial year in which return was furnished. If the revenue failed to prove that notice under section 143(2) was served on the assessee, the assessment order is not valid [CIT vs. Lunar Diamonds Ltd (2006) 281 ITR 1 (Del)].

Where notice under section 143(2) is issued by registered post on the last day of the period of limitation, it could not be said to have been served in time [CIT vs. Inderpal Malhotra (2008) 171 Taxman 359 (Del)].

Where service of notice under section 143(2) was done by affixture on last day after office hours, it was held that it was not a valid service and hence the assessment done on the basis of such notice is not valid [CIT vs. Vishnu & Co. Pvt. Ltd (2009) 319 ITR 151 (Del)].

In the absence of any evidence that any independent person was associated with the identification of assessee's place of business at the time of service under section 143(2) by affixture or that the inspectors of IT had personal knowledge of such place of business service of notice by affixture cannot be treated as valid service. Second notice having been served beyond the specified period was otherwise invalid hence, assessment is annulled [Kohli Bros. vs. ITO (2010) 42 DTR 113 (Luck) (Trib)].

Where the revenue submitted that a notice has been duly dispatched and gave dispatch number of the notice, it was held that merely giving dispatch number would not show that notice under section 143(2) had been served on the assessee [CIT vs. Cebon India Ltd. (2009) 184 Taxman 290 (P&H)].

The Tribunal has held that there was no evidence that there was any refusal by the assessee to accept service of notice. The Tribunal had categorically held that no other mode was adopted and steps for service of notice were taken about a week before the time was expiring. The service by affixture was not proper service. High Court affirmed the order of Tribunal [CIT vs. Kishan Chand (2010) 328 ITR 173 (P&H)].

Order sheet is a very important record. As the Assessing Officer not recorded in the order sheet and the Assessing Officer is not able to show that the notice dated 08-06-2006, was issued and served, it was to be held received after statutory time limit under section 143(2) and was clearly time barred [Dy. CIT vs. Mayawati (2010) 42 SOT 59 (Del)].

No specific form has been prescribed in the Income-tax Rules, 1962 for the notice. Almost invariably a printed form is used for this purpose. Be that as it may, the notice must give the assessee an option to attend in person or to produce the relevant evidence. A notice under this subsection not giving the option is not valid.

A fresh notice under section 143(2) must be served on the assessee if he furnishes a revised return under section 139(5) [Gopaldas Parshottamdas vs. CIT (1941) 9 ITR 130 (All)]. Where the assessment is completed without issuing a fresh notice under section 143(2) in respect of the revised return, the assessment is liable to be set aside for a fresh assessment after service of such notice [Intercraft India vs. CIT (1985) 154 ITR 662 (Del)].

However, the setting aside of the assessment made under section 143(3) on the basis of the original return is not possible where the revised return is not a valid one [CIT vs. Girishchandraharidas (1992) 196 ITR 833 (Ker)].

As per section 292BB, where an assessee has appeared in any proceeding or cooperated in any inquiry relating to an assessment or reassessment, it shall be deemed that any notice under any provision of this Act, which is required to be served upon him, has been duly served upon him in time in accordance with the provisions of this Act and such assessee shall be precluded from taking any objection in any proceeding or inquiry under this Act that the notice was—

(a) not served upon him; or

(b) not served upon him in time; or

(c) served upon him in an improper manner.

However, nothing contained in this section shall apply where the assessee has raised such objection before the completion of such assessment or reassessment.

As per section 80A(5) inserted by the Finance (No. 2) Act, 2009, where the assessee fails to make a claim in his return of income for any deduction under section 10A or section 10AA or section 10B or section 10BA or under any provision of Chapter VIA under the heading 'C.— Deductions in respect of certain incomes', no deduction shall be allowed to him there under.

Procedure of assessment under section 143(3) of institutions which are claiming exemption under Section 10:

In the case of an institution or association which is required to furnish a return of income under section 139(4C), the Assessing Officer shall not make an assessment order of the total income or loss of such scientific research association referred under section 10(21), news agency referred under section 10(22B), association or institution or fund or trust or university or other educational institution or any hospital or other medical institution referred under section 10(23A) or 10(23B) or 10(23C)(iv), (v), (vi) and (via) without giving effect to the provisions of section 10, unless—

(i) he has intimated the Central Government or the prescribed authority, the contravention of the provisions contained in such clauses where in his view such contravention has taken place, and

(ii) the notification issued or approval granted to such a body has been rescinded or withdrawn.

Generally the income of the above institution is exempt under the various clauses of section 10 mentioned above. However, the Assessing Officer can deny the exemption to them in the assessment order to be passed by him if the conditions mentioned in clauses (i) and (ii) are satisfied.

The Finance Act, 2012 has inserted third proviso to section 143(3).

As per the third proviso, first and second proviso to section 143(3) shall not be applicable where in any previous year commercial receipt of such trust exceed ₹25,00,000. In other words, Assessing Officer shall not give exemption to such trust covered under section 10(23C)(iv) or (v) even if approval has not been withdrawn or rescinded.

Procedure of assessment under section 143(3) of university or college which has received donation for carrying on scientific research or research in statistics or in social science:

Where the Assessing Officer is satisfied that the activities of the university, college or other institution referred to in clause (ii) and clause (iii) of sub-section (1) of section 35 are not being carried out in accordance with all or any of the conditions subject to which such university, college or other institution was approved, he may, after giving a reasonable opportunity of showing cause against the proposed withdrawal to the concerned university, college or other institution, recommend to the Central Government to withdraw the approval and that Government may by order, withdraw the approval and forward a copy of the order to the concerned university, college or other institution and the Assessing Officer.

The proceedings of assessment u/s 143(3) are described as quasi-judicial because they have certain, though not all the attributes of a judicial proceeding and the conclusions or decisions taken by the officer have some attributes of judicial decisions. These attributes can be discussed in three principal aspects.

(1) The Assessing Officer should act in a judicial manner, proceed with a judicial spirit, and come to a judicial conclusion. He should not exercise his powers only in a manner beneficial to the revenue and adverse to the assessee [CIT vs. Simon Carves Ltd. (1976) 105 ITR 212 (SC)].

(2) A second requirement is that the officer should act independently and arrive at his own conclusions [Dinshaw Darab Shaw Shroff vs. CIT (1943) 11 ITR 172 (Bom)].

(3) A third important requirement is that he should give a fair hearing to the assessee before deciding against him [Chockalingam (M.) & Meyyappam (M.) vs. CIT (1963) 48 ITR 34 (SC)].

Again, the proceedings for assessment before the Assessing Officer are described as quasi-judicial in character. It has been observed that, before the stage when he issues a notice under sub-section (2) of section 143, his proceedings are purely administrative.

After the receipt of the return also the Assessing Officer is entitled to make private enquiries as to whether there is reason to suspect that the return is incorrect or incomplete. No objection can be taken to such enquiries behind the back of the assessee at that stage, as they are all administrative. They assume a quasi-judicial character only after the issue of notice under sub-section (2) of this section. This is so because the Assessing Officer is not a court, civil or revenue (though he has the same powers as are vested in a court for the limited purposes mentioned in section 131) and the proceedings before him are not strictly judicial proceedings, though they are deemed to be such for limited purposes [Indian & Eastern Newspaper Society vs. CIT (1979) 119 ITR 996 (SC); Gurmukh Singh (Seth) vs. CIT (1944) 12 ITR 393].

Importance of the material gathering and evidence hearing for assessment u/s 143(3):

For the purpose of making assessment under section 143(3), the Assessing Officer is allowed to gather the material but he is also duty bound to give opportunity of being heard to the assessee.

(A) Gathering of material

(1) **Officer may make private inquiries to gather material:** Such enquiries may be carried out privately or confidentially. He can also summon witnesses and record their statements in the presence of the assessee or even behind his back. Only, he should satisfy himself as to the correctness of the information and as has already been pointed out, the substance of any information sought to be used against the assessee should be put to him and he should have a fair opportunity. It is up to the assessee to avail of it. Constant with the principles of natural justice, to rebut the same. It is, however, not always essential that a personal hearing should be given to the assessee [Chiranji Lai Steel Rolling Mills vs. CIT (1972) 84 ITR 222 (P&H); Namasivayam Chettiar (S.N.) vs. CIT (1960) 38 ITR 579 (SC); Abdul Razak vs. CIT (1935) 3 ITR 361 (Pat); Balasubramanian (P.N.) vs. ITO (1978) 112 ITR 512 (AP); Bagsu Devi Bafna vs. CIT (1966) 62 ITR 506 (Cal); Kashmir Vastralaya vs. CIT (197'8) 112 ITR 630 (Pat)].

(2) **Reference to Valuation Officer only in pending cases:** There should be a pending assessment for exercising the power to issue commission. Where a return had been processed u/s 143(1) and no notice u/s 143(2) had been issued, there can be no inference of any pendency of proceedings, so that reference to the District Valuation Officer to estimate the cost of construction was not valid. The reassessment based upon such report would also be consequently invalid [Arjun D. Bharad (Dr) vs. ITO (2003) 259 ITR (AT) (Nag) 1].

(3) **Officer cannot rely on third party statement without giving the assessee copies and right to cross-examine the deponent:** Where the Assessing Officer relies on the statement of a witness, or evidence allegedly given or a copy of accounts allegedly produced before some other authority by the assessee, the assessee be given, if he requires it and the circumstances warrant it, an opportunity to cross-examine the witness or official [Vasantlal & Co. (C) vs. CIT (1962) 45 ITR 206 (SC)].

(4) **Summons to witness for examination:** For the purpose of gathering relevant material, the Assessing Officer can issue summons under section 131 for the examination of witnesses and production of documents from third parties to ascertain the assessee's income. He can secure information and guidance by examining rivals in the trade of the assessee, or experts or past employees under the assessee, or managers who are acquainted either with the particular business of the assessee or the class of business in the neighbourhood. He may examine his own inspectors or surveyors if they can aid him and give information. He can rely upon his local knowledge and the previous history of the case. He can take into account the capital employed in the business. This, however, as pointed out in CIT vs. Radha Kishna Nandlal (1975) 99 ITR 143 (SC) will be relevant but not conclusive as profits do not always or wholly depend on the amount of capital employed.

(5) **Kinds of material which the Assessing Officer may use:** He can refer to materials gathered by him in the course of an earlier assessment which has been set aside but for being re-done. He can refer to the assessment proceedings of previous years for a standard to be applied to the assessee, though such assessment might have been made on a best judgment estimate. He can take into

consideration the volume of the business turned over by the assessee and in a money-lending business, the volume of the loans advanced on mortgage or simple bonds and the probability of normal recoveries and collections. He may also take into account the quantity of stocks carried by the assessee from year to year and whether the same is increasing or decreasing, the local reputation that the assessee holds in the business field and the position that he occupies in the market, the style of living of the assessee and any acquisition of property by him during recent years, the increase in his total resources and lastly, the rate of profit earned generally in the business by other businessmen in the line. Where the Assessing Officer relies upon this last-mentioned basis, he should furnish to the assessee details of the cases which he considers comparable, such as, the magnitude of the turnover, or the nature of the contracts entered into by them whether forward or ready, etc. It is not enough that he chooses comparable cases and puts them to the assessee. This principle has now been statutorily declared [Joseph Thomas & Bros, vs. CIT (1968) 68 ITR 796 (Ker)].

Where the additions were made Assessing Officer only by relying on the findings of the custom authorities and the said findings, which were the basis for making additions, had been set aside by the Appellate Authority. The Assessing Officer had not made any independent enquiry and also there was no corroborating evidence to support the case of the revenue. It was also found that even the assessee, whose statement was recorded by the Department of Central Excise, had not been examined by the Assessing Officer. Further, the assessee was not given an opportunity to cross-examine them. It was held that both the authorities were correct in deleting the additions made by the Assessing Officer [CIT vs. Vignesh Kumar Jewellers (2009) 180 Taxman 18 (Mad)].

(B) Assessee should be heard:

An assessment under section 143(3) can be made only after the assessee has been heard fully in three respects:

(a) he should be given an opportunity to produce the evidence on which he relies in support of the return;

(b) if, in respect of the evidence so produced or in view of other material gathered by the officer, he requires any clarifications or evidence on any specific points he should give the assessee an opportunity to furnish or produce the same; and

(c) if the Assessing Officer has gathered material on which he desires to rely, he should disclose to the assessee the substance of such material and give him an opportunity to have his say in regard thereto.

Nature of evidence that can be accepted for the assessment under section 143(3)

The language of section 143(3) makes it clear that the assessment order should be based on the evidence before the officer.

(1) **Material and evidence:** The material or evidence on which taxing authorities may rely under the Income-tax Act is not confined to direct testimony by witnesses. Though the word used in the section is evidence, it is not necessary, as already pointed out, that only evidence that would pass musters in a civil or criminal court should be relied on by the Assessing Officer. All relevant circumstances which have a bearing on the issue which are revealed during the course of assessment would be covered by the statement material or evidence on which the Assessing Officer could rely [Mangalchand Gobardhan Das vs. CIT (1954) 26 ITR 706 (Assam)].

(2) **Assessing Officer not fettered by technical rules of evidence:** The word material, it has been held, clearly shows that the Assessing Officer is not fettered by the technical rules of evidence and the like and that may act on material which may not strictly speaking be accepted as evidence in a court of law. Such evidence need not necessarily be direct evidence.

(3) **Suspicion not tantamount to evidence:** However, the mere existence of reasons for suspicion would not tantamount to evidence. But it should not be based on mere suspicion, conjecture

or guess work or on irrelevant or inadmissible material [Dhirajlal Girdharilal vs. CIT (1954) 26 ITR 736(SC)].

(4) **Past history:** The past history of an assessee is legitimate material that can be made use of in making an assessment but that may not be sufficient by itself, without more, to justify assessment in a particular year. There must be some material relatable to the accounting year which, taken with the past history, may reasonably entitle the income-tax authorities to hold that there must be some concealed income during the accounting year which is liable to assessment.

(5) **Comparable cases:** One of the standards generally applied in estimating the profits of an assessee is the rate of profit disclosed (or applied) in comparable cases. But in such cases, though the assessee need not be told the identity of the comparable cases, he is entitled to get so much of the information regarding the same as can be possibly disclosed by the Department and as may be necessary to enable him to show cause why the rate disclosed or applied in the comparable case should not be applied to his case [Dhakeswari Cotton Mills Ltd vs. CIT (1954) 26 ITR 775(SC)].

(6) **Affidavits:** Evidence may be tendered on an affidavit before the Assessing Officer. Such evidence is legal and can be acted upon by the Assessing/Appellate Authorities. Should the Assessing Officer, or the Deputy Commissioner (Appeals) or the Appellate Tribunal regard the same as not sufficient proof of the contents thereof, they should cross-examine the deponent and, if dissatisfied, call upon the assessee to produce documentary evidence in support of the contents of the affidavit. If no such thing is done, the affidavit by itself should be regarded as sufficient proof. This was so held by the Supreme Court in Mehta Parikh & Co vs. CIT (1956) 30 ITR 181 (SC).

The rule laid down by the Supreme Court in Mehta Parikhs case cannot be construed to lay down the proposition that unless the deponent is cross-examined, the affidavit cannot be rejected. That decision only lays down that if there is no material whatsoever on record for doubting the veracity of the statements made in the affidavit and if the deponent has also not been subjected to cross-examination for bringing out the falsity of his statements, then the tribunal will not be justified in doubting the correctness of the statements made by the deponent in the affidavit [Gunwanthibai Ratilal (Smt.) vs. CIT (1984) 146 ITR 140 (MP)].

The finding arrived at in such a case would, according to the Supreme Court, be a finding based on pure surmise. Where the affidavit itself constituted the evidence for a particular act such as, for example, a declaration that certain property in the assessee's hands is joint family property, it cannot be rejected without valid reason [Lakshmi Narain Gadodia & Co. In re (1943) 11 ITR 491 (Lah)].

It cannot be rejected merely on the ground that it is not supported by documentary evidence unless there is material to suggest that some documentary evidence exists and has not been produced by the assessee despite his being required to do so [Sohan Lai Gupta (L.) vs. CIT (1958) 33 ITR 786 (All)].

(7) **Books of Account:** Books of account maintained in the regular course of business are relevant and constitute a very good piece of evidence of their contents. They need not be formally proved as in a court of law [CIT (Addl) vs. Jay Engineering Works Ltd (1978) 113 ITR 389 (Del)].

Their probative value would however, depend on the circumstances and the manner of their maintenance.

(8) **Photostat copies and tapes:** The photostat copy of a document in the absence of the original or evidence regarding the circumstances in which it was taken, has very little evidentiary value [Moosa S. Madha & Azam S. Madha vs. CIT (1973) 89 ITR 65 (SC)].

There will be similar difficulty in acting upon what purports to be a tape recorded conversation. These types of material have, therefore, to be acted upon with great care and circumspection.

The assessment order should determine not only the total income of the assessee but also the amount payable by him. The Assessing Officer should apply his mind to the facts before him, apply the relevant law and come to a positive conclusion that the income assessed belongs to the assessee before him. The assessments under the Act have to be made every year and even if there is a dispute regarding the ownership of the income, the officer must come to a conclusion and cannot hold up his decision till the dispute is resolved in the ordinary courts [CIT vs. Hirjee (H.) (1953) 23 ITR 427 (SC)].

Piecemeal or Tentative Assessment

The officer must assess the total income of the assessee in accordance with the provisions of the Act. It is not open to him to assess the income from one or more sources and leave the others undetermined. He cannot make piecemeal assessments nor can he make a provisional or tentative assessment [Asharfi Lai vs. ITO (1967) 66 ITR 63 (All)].

Completion of Assessment:

An assessment is complete only when tax is computed by the Assessing Officer under his signature. Mere determination of income or wealth does not complete an assessment, if tax is not computed. Computation of tax however may have been done not as part of assessment order but as part of the record. Even an initial would do in the place of signature but the basic requirement is that the tax should have been computed under the signature of the Assessing Officer and if it is not done the assessment could not be treated as having been completed [CWT vs. Dhansukhlal J. Gajjar (1999) 237 ITR 537 (Guj)].

The determination of the tax payable by the assessee is as much mandatory as the determination of his income. Where the order determining the total income is passed within the prescribed time limit but the tax payable is not determined within the prescribed time limit, assessment would be time barred [CIT vs. Purshottamdas T. Patel (1994) 209 ITR 52 (Guj)].

As interest under sections 234B & 234C is mandatory it is not necessary that it should be given in the assessment order. The mention of interest in the computation sheet in this case would be adequate [CIT vs. Assam Mineral Development Corporation Ltd (2010) 320 ITR 149 (Gau)].

An entry in the order sheet could be an order of assessment. If the order is not a speaking one, it may violate the principles of natural justice. A cryptic entry in the order sheet merely recording the fact of completion of the assessment of a particular sum as income is against the requirement of law [Sewduttoy Rambullav & Son vs. CIT (1993) 204 ITR 580 (Cal)].

Section 143(3) contemplates two processes — one, the assessment of the total income and second, the determination of the sum payable by the assessee. It also requires the officer to make an order in writing. It should also be signed by the officer though the statute does not explicitly say so, as no order in writing can be ascribed to a person unless he has subscribed his signature or initial thereto.

Section 143(3) contemplates that the Assessing Officer shall pass an order of assessment in writing. If the assessment order is signed then because the computation of tax is a ministerial act, ITNS-150 need not be signed by the Assessing Officer. However, if the assessment order is not signed, then the fact that he has signed the tax computation form and the notice of demand is irrelevant. The omission to sign the assessment order cannot be explained by relying on section 292B [Vijay Corporation vs. ITO (2012) 18 Taxmann.com 88 (Mum)(Trib)].

Assessment on the basis of an invalid or non est return is void ab initio [Maya Debt Bansal vs. CIT (1979) 117 ITR 125 (Cal)]. However, such order remains in effect and continues to operate until its invalidity is declared by the court. Upon such declaration, the order goes out of existence as from the date on which it was made. But until then, void order is voidable and it continues to operate against the person against whom it was made and he is bound by the consequences flowing from the order [Indomarine Agencies (Kerala) (P.) Ltd vs. STO (1980) 45 STC 163 (Ker)].

11.3.4 Best Judgement Assessment [Section 144]

Best judgement assessment that is popularly known as ex-parte assessment can be made if the assessee fails to comply with the requirement of law as following :-

(1) The assessee fails to file a return u/s 139 and has not made a return or a revised return under sub-section (4) or (5) of Section 139.

(2) He fails to comply with the terms of the notice issued u/s 142(1) or fails to comply with a direction issued u/s 142(2A).

(3) After filing a return he fails to comply with all the terms of the notice issued u/s 143(2).

The non-compliances are independent and not cumulative. A single non compliance can lead to best judgement u/s 144. In such a situation the A.O. after taking into account all relevant materials which he has gathered and after giving the assessee an opportunity of being heard shall make an assessment of income or loss to the best of his judgement and determine the sum payable by him. However, where a notice u/s 142(1) has already been issued to the assessee it will not be necessary to give him such opportunity of being heard.

Provided that such opportunity shall be given by the Assessing Officer by serving a notice calling upon the assessee to shaw cause, on a date and time to be specified in the notice, why the assessment should not be completed to the best of his judgment.

Best judgement assessment is mandatory for any one of the defaults u/s 144 - CIT vs. Segn. Buchiah Sethy [1970] 77 ITR 539 (SC).

Where Assessing Officer, on finding that assessee had not maintained and kept any quantitative details/ stock register for goods traded in by it; that there was no evidence on record or document to verify basis of valuation of closing stock shown by assessee; and that GP rate declared by assessee during Assessment Year did not match result declared by assessee itself in previous Assessment Years, rejected assessee's books of account and resorted to best judgment assessment under section 144, it was held that since cogent reasons had been given by Assessing Officer for doing so, there was no reason to take a different view - Kachwala Gems vs. Jt. CIT 158 Taxman 71.

The assessments made on the basis of the assessee's accounts and those made on 'best judgment' basis are totally different types of assessments - *CST* vs. *H.M. Esufali H.M. Abdulai* 90 ITR 271.

The mere fact that the material placed by the assessee before the Assessing Officer is unreliable does not empower the officer to make an arbitrary order. The power to make a best judgment assessment is not an arbitrary power - *State of Orissa* vs. *Maharaja Shri B.P. Singh Deo* 76 ITR 690.

Where the jurisdiction of a notice under section 143(2) is not valid and there has been non-compliance with the same by the assessee, the Assessing Officer cannot resort to section 144 and make an assessment to the best of his judgment [Rajmani Devi vs. CIT (1937) 5 ITR 631 (All)].

An ex parte best judgment assessment under section 144 can only be made for defaults specified in that section. Non-compliance with a summons requiring production of books of account and other documents, etc. is not such a specified default and, therefore, it cannot result in an ex parte best judgment assessment [ITO vs. Luxmi Prasad Goenka (1977) 110 ITR 674 (Cal)].

Rejection of Books of Accounts

Section 145(3) empowers the Assessing Officer to reject the books of account which are unreliable, false or incorrect or incomplete. The Assessing Officer can reject the books of account on the following grounds and may make the assessment in the manner provided in section 144:

(a) He is not satisfied about the correctness or completeness of the accounts of the assessee.

(b) Although the accounts of the assessee are correct and complete to the satisfaction of the Assessing Officer but the method of accounting employed is such that, in the opinion of the Assessing Officer, profits cannot be correctly arrived therefrom.

(c) Where the method of accounting adopted by the assessee has not been regularly followed by him, or

(d) Where the income computation and disclosure standards notified by the Central Government from time to time have not been regularly followed by the assessee.

In view of the above, the Assessing Officer may reject the books, even if the method of accounting is acceptable to him, if the entries in the books are found to be false or fabricated. Conversely the books of account may be accepted as true but the method of accounting may be rejected by the Assessing Officer as improper.

The expression 'method of accounting' in the section has reference to the pattern, system or principles on the basis of which the accounts of an assessee are maintained and not to its other aspects, such as, language, currency, etc. The assessee may keep his accounts in any language he chooses. Accounts in India are maintained in English, Hindi or other regional languages and in certain scripts employed by certain communities, such as Modi and the like.

Section 144 prescribes for best judgment assessment only in case of 3 failures mentioned in the said section. In case, the Assessing Officer rejects the accounts on any of the grounds mentioned under section 144, the Assessing Officer has to make the assessment under the relevant section i.e. 143(3) or 147 in which the assessment proceedings were going on. But such assessment has to be done in the manner provided under section 144 i.e. he will have to make the assessment to the best of his judgment. The assessment in this case is not to be done under section 144 but in the manner provided in section 144.

The assessment that has to be made after rejection under section 145(3) of the evidence or books produced is not an assessment under section 144 but it is only an assessment under section 143(3) which is to be made in the manner provided in section 144. In such cases, the Assessing Officer has to give an opportunity to the assessee to contradict the material upon which the former wants to base his estimate [Addl. ITO vs. Ponkunnam Traders (1976) 102 ITR 366 (Ker)].

Following are the cases where rejection of books held justified:

(1) The presence of unexplained cash credits may justify not only their treatment as income from disclosed or undisclosed sources but also, in appropriate cases, the rejection of the book results [Abdul Khadar Pvt. Ltd vs. CIT (1960) 38 ITR 341 (Mad)].

(2) Where there was a huge difference between stock of goods as per the accounts and the stock position as shown to the bank for securing overdrafts and there was no material to corroborate the figures shown in the books of account, the rejection of accounts was held to be justified [Murugappa Chettiar (S.) vs. CIT (1988) 174 ITR 245 (Ker)].

(3) Where the assessee engaged in bidi manufacturing business having several factories and branches did not record day-to-day production of bidis and could not produce day-to-day registers showing the quantity of bidis manufactured and of bidi leaves consumed in each factory, his accounts were liable to be rejected [Bastiram Narayandas Maheshri vs. CIT (1994) 210 ITR 438 (Bom)].

(4) Detection of fictitious purchase invoices involving large amounts justifies rejection of books of account [Vijay Proteins Ltd vs. ACIT (1996) 55 TTJ 76 (Ahd) (AT)].

(5) There was a search in assessee's premises as well as at the premises of its directors and other related concerns and persons. The Settlement Commission found that books were not complete and were defective and inspired little confidence about their veracity. Hence, net profit had to be estimated [I.T. Settlement Commission vs. Saraf Textile Mills (P.) Ltd (1996) 130 Taxation 550 (Del) (ITSC)].

(6) Non-maintenance of stock register, coupled with other factors, rejection may be held justified [Namasivayam Chettiar (S.N.) vs. CIT (1960) 38 ITR 579 (SC)].

(7) It is not only the right but the duty of the Assessing Officer to consider whether or not the books disclose the true state of accounts and the correct income can be deducted there from. It is incorrect to say that the officer is bound to accept the system of accounting regularly employed by the assessee the correctness of which had not been questioned in the past. There is no estoppel in these matters and the officer is not bound by the method followed in the earlier years [CIT vs. British Paints India Ltd (1991) 188 ITR 44 (SC)].

(8) Where the payments were made by the assessee by way of post dated cheques, it does not amount to actual payment and the books are unreliable if they incorporate these payments. The books of accounts were rightly rejected under section 145 [Oriental Textiles vs. CIT (2005) 273 ITR 47(A11)].

Following are the cases where rejection of books held not justified:

(1) The fact that the Assessing Officer has found some faults with the accounts will not necessarily bring the case within the scope of the first proviso to this section. In CIT vs. Padamchand Ramgopal (1970) 76 ITR 719 (SC), the Supreme Court observed that insignificant mistakes cannot afford a ground for resorting to this section. So long as it is not impossible to deduce the true income from the accounts maintained by the assessee, its computation cannot be made in any other way. The fact that the assessee's accounts did not contain the income from paddy and miscellaneous produces, which was negligible, did not stand in the way of accepting the assessee's rubber accounts, and likewise it did not justify the rejection of the pepper accounts of the assessee.

(2) Assessing Officer cannot reject the method of accounting merely because, in his view, a different system of accounting would be better suited [CIT vs. Margadarsi Chit Funds Pvt. Ltd (1985) 155 ITR 442 (AP)].

(3) The assessee, according to the Assessing Officer, showed low gross profits. But he neither recorded a clear finding that the assessee's system of accounting was such that correct profit could not be deduced from its books, nor pointed out inherent defects in the system of accounting, which the assessee could rebut. [ITO vs. Highway Service Station (1991) 58 Taxman 254 (ASR) (AT)].

(4) The assessee, an LIC agent, maintained regular books of account. No defects were shown in the maintenance of books. The accounts were rejected whimsically, and income estimated. Unless the system of accounts is rejected or books of account are rejected on proper basis or no books of account are maintained, the income disclosed cannot be disturbed [ITO vs. Amar Singh Jain (1992) 43 TTJ 11 (Jp)(AT)].

(5) The Income-tax Authorities and the Tribunal made addition to gross profit mainly on the ground that the assessee could not have sustained a loss in supply of rice to Government under levy orders to the extent claimed because according to them, quality of rice supplied by dealers was always much inferior. The addition on this ground without any acceptable reason was not justified [Shree Ambikaji Rice Mills vs. CIT (1991) 192 ITR 189 (Pat)].

(6) In case a stock register of goods is not maintained, it may normally not be taken as a defect justifying rejection of books of account. It may be a reason for the Assessing Officer to scrutinise the case with caution [Pandit Bros. vs. CIT (1954) 26 ITR 159 (Punj)].

(7) Where, in a wholesale business, the weight-wise record was not maintained but a number-wise quantitative stock tally was maintained, the rejection of book profits was not justified [Durai Raj (M.) vs. CIT (1972) 83 ITR 484 (Ker)].

11.3.5 Power of Joint Commissioner to issue directions in certain cases [Sec. 144A]

A Joint Commissioner may, on his own motion or on a reference being made to him by the Assessing Officer or on the application of an assessee, call for and examine the record of any proceeding in which an assessment is pending and, if he considers that, having regard to the nature of the case or the amount involved or for any other reason, it is necessary or expedient so to do, he may issue such directions as he thinks fit for the guidance of the Assessing Officer to enable him to complete the assessment and such directions shall be binding on the Assessing Officer.

Provided that no directions which are prejudicial to the assessee shall be issued before an opportunity is given to the assessee to be heard.

11.3.6 Reference to Commissioner in certain cases [Section 144BA] [Applicable w.e.f. 1.4.2014]

(1) If, the Assessing Officer, at any stage of the assessment or reassessment proceedings before him having regard to the material and evidence available, considers that it is necessary to declare an arrangement as an impermissible avoidance arrangement and to determine the consequence of such an arrangement within the meaning of Chapter X-A, then, he may make a reference to the Commissioner in this regard.

(2) The Commissioner shall, on receipt of a reference u/s 144BA (1), if he is of the opinion that the provisions of Chapter X-A are required to be invoked, issue a notice to the assessee, setting out the reasons and basis of such an opinion, for submitting objections, if any, and providing an opportunity of being heard to the assessee within such period, not exceeding sixty days, as may be specified in the notice.

(3) If the assessee does not furnish any objection to the notice within the time specified in the notice issued under sub-section (2) of this section, the Commissioner shall issue such directions as it deems fit in respect of declaration of the arrangement to be an impermissible avoidance arrangement.

(4) In case the assessee objects to the proposed action, and the Commissioner, after hearing the assessee in the matter, is not satisfied by the explanation of the assessee, then, he shall make a reference in the matter to the Approving Panel for the purpose of declaration of the arrangement as an impermissible avoidance arrangement.

(5) If the Commissioner is satisfied, after having heard the assessee that the provisions of Chapter X-A are not to be invoked, he shall by an order in writing communicate the same to the Assessing Officer with a copy to the assessee.

(6) The Approving Panel, on receipt of reference from the Commissioner u/s 144BA (4) shall issue such directions, as it deems fit, in respect of the declaration of the arrangement as an impermissible avoidance arrangement in accordance with the provisions of Chapter X-A including specifying the Previous Year or Years to which such declaration of an arrangement as an impermissible avoidance arrangement shall apply.

(7) No direction under sub-section (6) shall be issued unless an opportunity of being heard is given to the assessee and the Assessing Officer on such directions which are prejudicial to the interest of the assessee or the interest of the revenue, as the case may be.

(8) The Approving Panel may, before issuing any direction u/s 144BA (6),—

  (i) if it is of the opinion that any further inquiry in the matter is necessary, direct the Commissioner to make such further inquiry or cause to make such further inquiry to be made by any other income-tax authority and furnish a report containing the results of such inquiry to it; or

  (ii) call for and examine such records related to the matter as it deems fit; or

  (iii) require the assessee to furnish such document and evidence as it may so direct.

(9) No direction u/s 144BA (6) shall be issued after a period of six months from the end of the month in which the reference u/s 144BA (4) was received by the Approving Panel.

(10) The Board shall, for the purposes of this section constitute an Approving Panel consisting of not less than three members, being—

  (i) income-tax authorities not below the rank of Commissioner; and

  (ii) an officer of the Indian Legal Service not below the rank of Joint Secretary to the Government of India.

11.3.7. Provision for constitution of alternate dispute resolution mechanism for order of the Transfer Pricing Officer, and foreign company (Section 144C) [W.e.f. 1-10-2009]

The dispute resolution mechanism presently in place is time consuming and finality in high demand cases is attained only after a long drawn litigation till Supreme Court. Flow of foreign investment is extremely sensitive to prolonged uncertainty in tax related matter. Therefore, the Act has amended the Income-tax Act to provide for an alternate dispute resolution mechanism, which will facilitate expeditious resolution of disputes in a fast track basis.

The salient features of the alternate dispute resolution mechanism are as under:—

1. The Assessing Officer shall not withstanding anything to the contrary contained in this Act, forward a draft of the proposed order of assessment (hereinafter in this section referred to as the draft order) to the eligible assessee if he proposes to make, on or after 1-10-2009, any variation in the income or loss returned which is prejudicial to the interest of such assessee.
2. On receipt of the draft order, the eligible assessee shall, within thirty days of the receipt by him of the draft order,
   (a) File his acceptance of the variations to the Assessing Officer; or
   (b) File his objections, if any, to such variation with,—
      (i) The Dispute Resolution Panel; and
      (ii) The Assessing Officer.
3. The Assessing Officer shall complete the assessment on the basis of the draft order, if—
   (a) The assessee intimates to the Assessing Officer the acceptance of the variation; or
   (b) No objections are received within the period specified in sub-section (2) i.e. 30 days of the receipts of draft order by the eligible assessee.
4. The Assessing Officer shall, notwithstanding anything contained in section 153 or section 153B, pass the assessment order under section 144C(3) within one month from the end of the month in which,—
   (a) The acceptance is received; or
   (b) The period of filing of objections under sub-section (2) expires.
5. The Dispute Resolution Panel shall, in a case where any objections are received under sub-section (2), issue such directions, as it thinks fit, for the guidance of the Assessing Officer to enable him to complete the assessment.
6. The Dispute Resolution Panel shall issue the directions referred to in sub-section (5), after considering the following, namely:—
   (a) Draft order;
   (b) Objections filed by the assessee;
   (c) Evidence furnished by the assessee;
   (d) Report, if any, of the Assessing Officer, Valuation Officer or Transfer Pricing Officer or any other authority;
   (e) Records relating to the draft order;
   (f) Evidence collected by, or caused to be collected by, it; and
   (g) Result of any enquiry made by, or caused to be made by it.
7. The Dispute Resolution Panel may, before issuing any directions referred to in sub-section (5),—
   (a) Make such further enquiry, as it thinks fit; or
   (b) Cause any further enquiry to be made by any Income Tax Authority and report the result of the same to it.

8. The Dispute Resolution Panel may confirm, reduce or enhance the variations proposed in the draft order so, however, that it shall not set aside any proposed variation or issue any direction under sub-section (5) for further enquiry and passing of the assessment order.

   Explanation- For the removal of doubts, it is hereby declared that the power of the Dispute Resolution Panel to enhance the variation shall include and shall be deemed always to have included the power to consider any matter arising out of the assessment proceedings relating to the draft order, notwithstanding that such matter was raised or not by the eligible assessee.

Case Laws

(I) Order cannot be passed by Dispute Resolution Panel if no transfer pricing adjustments made by TPO. Where no transfer pricing adjustments had been made by the TPO, the assessee was not an "eligible assessee" and the Assessing Officer had no jurisdiction to pass the draft assessment order [Pankaj Extraction Ltd. vs. ACIT (Gujarat High Court)].

(II) The Dispute Resolution Panel is an authority created under a statute and conferred with the powers, which has the obligation to act as a body living to the expectations which the law mandates. It was held that section 144C empowers the Dispute Resolution Panel to issue directions to the Assessing Officer and cannot be treated as totally redundant or absolutely inefficacious remedy to the assessee. Thus, no assessee can have any kind of apprehension that the approach to the Dispute Resolution Panel is perfunctory [Ericsson AB vs. ADIT (Delhi High Court)].

(III) Dispute Resolution Panel while issuing directions under section 144C must not pass "laconic" orders but must deal with assessee's objections. It was held in Sahara India (Farms) vs. CIT 300 ITR 403 (SC) that even "an administrative order has to be consistent with the rules of natural justice" [GAP International Sourcing India Pvt. Ltd. vs. Dy. CIT (ITAT-Delhi)].

(IV) Dispute Resolution Panel must give "cogent and germane reasons" in support of section 144C directions [Vodafone Essar Ltd vs. Dispute Resolution Panel (Delhi High Court)].

(V) Where there was no variation in income or loss returned which is prejudicial to the interest of the assessee on account of order of TPO under section 92CA, it was held that the assessee cannot be said to be an eligible assessee under section 144C(15), hence there is no need for draft order and taking further steps under section 144C. [Pankaj Extrusion Ltd. vs. ACIT (2011) 56 DTR 32 (Guj)].

9. If the members of the Dispute Resolution Panel differ in opinion on any point, the point shall be decided according to the opinion of the majority of the members.

10. Every direction issued by the Dispute Resolution Panel shall be binding on the Assessing Officer.

11. No direction under sub-section (5) shall be issued unless an opportunity of being heard is given to the assessee and the Assessing Officer on such directions which are prejudicial to the interest of the assessee or the interest of the revenue, respectively.

12. No direction under sub-section (5) shall be issued after nine months from the end of the month in which the draft order is forwarded to the eligible assessee.

13. Upon receipt of the directions issued under sub-section (5), the Assessing Officer shall, in conformity with the directions, complete, notwithstanding anything to the contrary contained in section 153 or section 153B, the assessment without providing any further opportunity of being heard to the assessee, within one month from the end of the month in which the direction is received.

14. The Board may make rules for the efficient functioning of the Dispute Resolution Panel and expeditious disposal of the objections filed, under subsection (2), by the eligible assessee.

15. According to sub-section 14A of section 144C [w.e.f. 1.4.2013], the provisions of this section shall not apply to any assessment or reassessment order passed by the Assessing officer with the prior approval of the commissioner u/s 144BA(12).

16. For the purposes of this section,—
    (a) "Dispute Resolution Panel" means a collegium comprising of 3 Commissioners of Income Tax constituted by the Board for this purpose;
    (b) "eligible assessee" means,—
        (i) Any person in whose case the variation referred to in sub-section (1) arises as a consequence of the order of the Transfer Pricing Officer passed under sub-section (3) of section 92CA; and
        (ii) any foreign company.

    Further, the following consequential amendments have been made—

    (i) Section 131(1) so as to provide that "Dispute Resolution Panel" shall have the same powers as are vested in a Court under the Code of Civil Procedure, 1908;
    (ii) Section 246(1)(a) has been amended so as to exclude the order of assessment passed under section 143(3) or order of re-assessment under section 147 in pursuance of directions of "Dispute Resolution Panel" as an appealable order.
    (iii) Section 253(1) has been amended to insert clause (d) so as to include an order of assessment passed under section 143(3) or order of re-assessment under section 147 in pursuance of directions of "Dispute Resolution Panel" as an appealable order.

An order passed under section 154 rectifying such order shall also be appealable to IT Act.

11.3.8 Income Escaping Assessment [Sec. 147]

If the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any Assessment Year, he may, subject to the provisions of section 148 to 153, assess or reassess such income and also any other income chargeable to tax which has escaped assessment and which comes to his notice subsequently in the course of the proceedings under this section, or recompute the loss or the depreciation allowance or any other allowance, as the case may be, for the Assessment Year concerned.

Where an assessment under section 143(3) or section 147 has been made for the relevant Assessment Year, no action shall be taken under this section after the expiry of four years from the end of the relevant Assessment Year, unless any income chargeable to tax has escaped assessment for such Assessment Year by reason of the failure on the part of the assessee to make a return under section 139 or in response to the notice issued under section 142 or section 148 or to disclose fully and truly all material facts necessary for his assessment, for that Assessment Year.

Nothing contained in the first proviso shall apply in a case where any income in relation to any assets (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment for any Assessment Year.

The Assessing Officer may assess or reassess such income, other than the income involving matters which are the subject matters of any appeal, reference or revision, which is chargeable to tax and has escaped assessment.

Reassessment of income in relation to any asset located outside India :

The existing time limit for reassessment of 4 years from the end of the Assessment Year, shall not apply in a case where any income in relation to any asset (including financial interest in any asset located outside India) which is chargeable to tax, has been escaped assessment for any Assessment Year.

Assessing Officer empowered to touch upon any other issue for which no reasons have been recorded notwithstanding that the reasons for such issue have not been included in the reasons recorded [Section 147] [W.r.e.f. Assessment Year 1989-90]

The existing provisions of section 147 provides, inter alia, that if the Assessing Officer has reason to believe that any income chargeable to tax has escaped assessment for any Assessment Year, he may assess or reassess such income after recording reasons for re-opening the assessment. Further, he may also assess or reassess such other income which has escaped assessment and which comes to his notice subsequently in the course of proceedings under this section.

Sonic Courts have held that the Assessing Officer has to restrict the reassessment proceedings only to issues in respect of which the reasons have been recorded for reopening the assessment. He is not empowered to touch upon any other issue for which no reasons have been recorded. The above interpretation is contrary to the legislative intent.

With a view to further clarifying the legislative intent, the Act has inserted Explanation 3 in section 147 to provide that the Assessing Officer may assess or reassess income in respect of any issue which comes to his notice subsequently in the course of proceedings under this section, notwithstanding that the reason for such issue has not been included in the reasons recorded under section 148(2).

Case Laws :

(1) A writ petition challenging reassessment, cannot be thrown out at the threshold on the ground that it is not maintainable - Techspan India (P.) Ltd. vs. ITO 283 ITR 212 .

(2) If the direction by the Commissioner is to reopen the assessment under section 147 by passing the statutory formalities, that would probably amount to dictating his subordinate to act in a particular way thereby taking away the discretion vested in the subordinate - CIT vs. Abdul Khader Ahamed 156 Taxman 206.

(3) Disclosure in wealth-tax proceedings will not suffice - Arun Kumar Maheshwari vs. ITO 144 Taxman 651.

(4) Income cannot be said to have escaped assessment if the proceedings have not culminated in a final assessment [CIT vs. Sayed Rafiqur Rahman (1991) 189 ITR 476 (Pat)].

(5) Where an order of remand has been passed, the assessment proceedings become pending and pending such proceedings, notice under section 148 cannot be issued [Jhunjhunwala Vanaspati Ltd. vs. ACIT (2004) 137 Taxman 335 (All)].

(6) Reassessment under section 147 cannot be made within the time available for issuing notice under section 143(2) and for completion of assessment under section 143(3) [CIT vs. Abad Fisheries (2012) 65 DTR 370: 204 Taxman 267/246 CTR 513 (Ker)].

(7) Original assessments for Assessment Years 2010-11 to 2012-13 were completed, otherwise than in the status of HUF. The Income-tax Officer reopened the assessments and assessed the assessee in the status of HUF. It was held that the issue of status was already decided finally and reopening of the assessments was without jurisdiction [CIT vs. Lakshmikutty Amma (T.) (1995) 211 ITR 1014 (Ker)].

(8) The assessment order was set aside by the Appellate Assistant Commissioner. But the Assessing Officer issued notice under section 148. Held that Assessing Officer was not justified in initiating reassessment proceedings [Saqi Brothers vs. ITO (1996) 54 TTJ 306 (Chd) (AT)].

(9) Where the Assessing Officer's comes into possession of fresh information or new facts, which lead him to form a reasonable belief that income has escaped assessment, he can reopen the assessment [Phool Chanel Bajrang Lai vs. ITO (1993) 203 ITR 456 (SC)].

(10) The Assessing Officer must make independent enquiries for arriving at the prima facie conclusion that income of the assessee had escaped assessment. The Assessing Officer acted merely on the basis of information received from another officer by result of a survey conducted by such officer. The Assessing Officer without forming any opinion/belief of his own and without gathering any further material or enquiry initiated proceedings for reopening. It was held that the Assessing

Officer had not made an independent enquiry for arriving at the prima facie conclusion that income of the assessee had escaped assessment and therefore the proceedings under section 148 were not valid [Jt. CIT vs. George Williamson (Assam) Ltd (2003) 258 ITR 126 (Gau)].

(11) Where the assessee was allowed depreciation on certain leased vehicles and subsequently the Assessing Officer had determined that the relevant agreements were with a view to finance the vehicles and not leasing agreements. This finding of the Assessing Officer was also affirmed by the CIT (Appeals). It was held that the Assessing Officer had sufficient reasons to believe that income of the assessee had escaped assessment to issue notice under section 148 of the Act [Syal Leasing Ltd vs. Assistant Commissioner of Income-tax (2004) 266 ITR 639 (P&H)].

(12) Reassessment proceedings may be taken more than once under this section in respect of the same assessee for the same assessment year [R. Kakkar Glass and Crockery House vs. CIT (2002) 254 ITR 273 (P&H)]. But second assessment proceedings cannot be started while the first are pending [Comunidado of Chicalim vs. ITO (2001) 247 ITR 271 (SC)].

11.3.9 Issue of notice where income has escaped assessment [Section 148]

(1) Before making the assessment, reassessment or recomputation under section 147, the Assessing Officer shall serve on the assessee a notice requiring him to furnish within specified period, a return of his income or the income of any other person in respect of which he is assessable.

(2) The Assessing Officer shall, before issuing any notice under this section, record his reasons for doing so.

Legal Notes

- Notice under this section is to be mandatorily served by the Assessing Officer before initiating proceedings u/s 147. The notice is served on the assessee when it is received by him.
- Notice is to be issued within the time limits prescribed by section 149. Section 149(2) states that issue of such notice is subject to the provisions of section 151. Thus, approval for the issue of such notice is to be taken u/s 151 before its issue.
- Such notice can be issued by the Assessing Officer only after he records his reasons for doing so.
- The return to be furnished in response to such notice is treated as a return required to be furnished u/s 139 and the provisions of this Act, so far as may be, apply accordingly.
- Return in response to a notice under this section is to be furnished even if a return has been furnished earlier by the assessee under other provisions of the Act.
- Notice under this section can be issued even where an assessment u/s 143(3) has not been made but related intimations have been sent. [Ranchi Club Ltd. vs. CIT214 ITR 643]

Case Laws :

(1) If reasons are supplied along with the notice under section 148(2), it shall obviate unnecessary harassment to the assessee as well as to the revenue by avoiding unnecessary litigation which will save courts also from being involved in unproductive litigation. Above all, it shall be in consonance with the principles of natural justice - *Mitilesh Kumar Tripathi* vs. *CIT* 280 ITR 16.

(2) The notice prescribed by section 148 cannot be regarded as a mere procedural requirement. It is only if the said notice is served on the assessee that the ITO would be justified in taking proceedings against the assessee. If no notice is issued or if the notice issued is shown to be invalid, then the proceedings taken by the ITO would be illegal and void - *Y. Narayana Chetty* vs. *ITO* 1959 35 ITR 388; *CIT* vs. *Thayaballi Mulla Jeevaji Kapasi* 66 ITR 147 ; *CIT* vs. *Kurban Hussain Ibrahimji Mithiborwala* 82 ITR 821.

(3) Where the Appellate Assistant Commissioner set aside the reassessment on the only ground that the assessee was not afforded opportunity to put forward his case, but did not hold that the notice issued under section 148 was invalid, there would be no need for the ITO to issue a fresh notice to the assessee - *CIT* vs. *T.S.PL.P. Chidambaram Chettiar* 80 ITR 467.

(4) Notice cannot be issued unless the return which has already been filed has been disposed of - *CIT* vs. *M.K.K.R. Muthukaruppan Chettiar* 78 ITR 69 ; *Bhagwan Das Sita Ram (HUF)* vs. *CIT* 146 ITR 563.

11.3.10 Time limit for notice [Section 149]

(1) No notice under section 148 shall be issued for the relevant Assessment Year —

  (a) if four years have elapsed from the end of the relevant Assessment Year, unless the case falls under clause (b) or clause (c);

  (b) if four years, but not more than six years, have elapsed from the end of the relevant Assessment Year unless the income chargeable to tax which has escaped assessment amounts to or is likely to amount to one lakh rupees or more for that year.

  (c) If four years, but not more than sixteen years, have elapsed from the end of the relevant Assessment Year unless the income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment.

  - Time-limit applies for 'Issue' and not for service - R.K. Upadhyaya vs. Shanabhai P Patel 1987 166 ITR 163 (SC).
  - Amended law will apply only if limitation has not already expired - Chandiram vs. ITO 1996 87 Taxman 418 (Raj.).

The word 'issued' in section 149 should be given its natural meaning and not the strained wider meaning of 'served'. Consequently, where the notice was issued within time but was served on the assessee after the expiry of the time-limit, it could not be held to be invalid - *R.K. Upadhyaya* vs. *Shanabhai P. Patel* 166 ITR 163 (SC); *CIT* vs. *Sheo Kumari Debi* 157 ITR 13 and *Jai Hanuman Trading Co. (P.) Ltd.* vs. *CIT* 110 ITR 36.

Circumstances where time limit given under section 149(1) is not relevant:

(1) Action cannot be taken under section 147 after 4 years in some cases if assessment is made under section 143(3)/147 [Proviso to section 147 and Explanation 1 to section 147]: Where an assessment under section 143(3) or 147 has already been made for the relevant assessment year, no action under section 147 is possible after the expiry of 4 years from the end of the relevant assessment year unless any income chargeable to tax has escaped assessment by reason of the failure on the part of the assessee to:

  (a) make a return under section 139 or in response to a notice under section 142(1) or 148; or

  (b) disclose fully and truly all material facts necessary for his assessment for that assessment year.

However, nothing contained in the first proviso (relating to reopening of assessment upto 4 years) shall apply in a case where any income in relation to any asset (including financial interest in any entity) located outside India, chargeable to tax, has escaped assessment for any assessment year.

Production before the Assessing Officer of books of account or other evidence from which material evidence could, with due diligence have been discovered by the Assessing Officer, will not necessarily amount to disclosure of material facts.

Proviso to section 147 presupposes an assessment under section 143(3) or section 147. In the absence of such assessment, benefit of this proviso cannot be taken by the assessee.

If the return under section 139/142(1)/148 has been furnished and all material facts relating to the assessment for that previous year have been disclosed fully and truly, then notice cannot be served after the expiry of 4 years if the assessment of that assessment year has been made under section 143(3) or 147.

Where a notice under section 148 was issued after the expiry of 4 year from the end of the assessment for which income escaped assessment, it was held that "full and true disclosure of material facts" means that the disclosure should not be garbled or hidden in the crevices of the documentary material which has been filed by the assessee with the AO. The assessee must act with candor. A full disclosure is a disclosure of all material facts which does not contain any hidden material or suppression of fact. It must be truthful in all respects.

On facts, though the AO enquired into the matter relating to exemption of capital gain and the assessee furnished a copy of the section 54EC bonds (from which the dates of allotment/investment were evident), there was no (specific) reference by the assessee to the dates on which the amounts were invested in the section 54EC bonds. Also, it was evident that the AO had not applied his mind to the issue of section 54EC exemption. Accordingly, the AO was justified in reopening the assessment. [The Indian Hume Pipe Co. Ltd. vs. ACIT (2012) 204 Taxman 347 (Bom)].

(2) Agent of a non-resident [Section 149(3)]: If the person on whom a notice under section 148 is to be served is a person treated as the agent of a non-resident under section 163 and the assessment, reassessment or recomputation to be made in pursuance of the notice is to be made on him as the agent of such non-resident, the notice shall not be issued after the expiry of a period of six years from the end of the relevant assessment year.

(3) No time limit for issue of notice for assessment in pursuance of order on appeal, etc. [Section 150(1)]: Notice under section 148 may be issued at any time for the purpose of making an assessment or reassessment or re-computation in consequence of or to give effect to any finding or direction contained in an order passed:

(a) by any authority in any proceeding under this Act by way of appeal or revision under section 250/254/260A/262/263/264, or

(b) by a court in any proceeding under any other law.

It may be noted that a judgment given by a Court under any other law can also lead to reassessment and the time limit prescribed under section 149 shall not be applicable. In other words, such notice can be issued at any time to make assessment or reassessment in consequence of or in order to give effect to the finding or direction contained in the order of:

(i) The Supreme Court passed under the provisions of Income-tax Act or any other law;

(ii) A High Court passed under the provisions of Income-tax Act or any other law;

(iii) CIT (Appeal) under section 250/ITAT under section 254/ Commissioner under section 263 or 264 of the Income-tax Act.

Further, order passed by Supreme Court will apply generally to all assessees and the order passed by the High Court may apply only to the assessees who fall in the jurisdiction of the High Court but the order under section 250 or 254 or 263 and 264 will apply for the specific assessee.

Exception to section 150(1) [Section 150(2)]: The above provision that there will be no time limit to issue notice under section 149(1) shall, however, not apply where any such assessment or reassessment as is referred to in sub-section (1) to section 150 relates to an assessment year in respect of which an assessment or reassessment could not have been made at the time the order which was the subject matter of appeal, reference or revision, as the case may be, was made by reason of any other provision limiting the time within which any action for assessment or reassessment may be taken.

Although section 150 appears to be of a very wide amplitude, but it would not mean that recourse to reopening of proceedings in terms of sections 147 and 148 can be initiated at any point of time whatsoever; such a proceeding can be initiated only within a period of limitation prescribed therefore as contained in section 149 [CIT, Shimla vs. Greenworld Corporation (2009) 181 Taxman 111 (SC)].

Although the time limits prescribed in section 149 of the Income-tax Act, 1961, will not apply where assessment proceedings are initiated by a notice to give effect to any finding or direction under section 150(1), but under section 150(2), the period of limitation as laid down in section 149 shall come into play, if the action for assessment or reassessment could not be initiated for an assessment year on the date of order which was the subject matter of appeal, reference or revision. Thus, where the High Court by order dated 1-6-1977, enhanced compensation and a further sum of ₹10,30,320 was paid to him as interest for the period 21-10-1966 to 30-6-1979 and the Assessing Officer treated the interest taxable in the assessment year 1980-81, in an order passed on 19-7-1983. On appeal, the Commissioner (Appeal) by his order dated 16-1-1984 accepted the claim of the assessee that such interest was assessable only on accrual basis and directed the Assessing Officer to recompute the addition accordingly. While giving effect to the order of Commissioner (Appeal), the Assessing Officer issued the notice under section 148 dated 27-3-1984, to assess the interest on accrual basis in the corresponding assessment years 1967-68 to 1979-80.

On a writ petition against the reassessment proceedings, it was held by the Punjab and Haryana High Court that in this case, the question of limitation had also to be considered. In the present case, the assessment order which was subject matter of appeal before the Commissioner (Appeal) for the assessment year 1980-81 was passed by the Assessing Officer on 19-7-1983. Hence no proceeding under section 147 could be initiated in the assessment years for which the period of limitation of 4 years prescribed under section 149 had expired on that date. The years involved in the present writ petitions were assessment years 1967-68 to 1979-80. The period of limitation of four years prescribed under section 149 for the assessment years 1967-68 to 1978-79 had expired on or before 31-3-1983, which was prior to the date of order dated 19-7-1983. These assessment years were clearly covered within the exception provided by section 150(2). Consequently, the notice issued under section 148 dated 27-3-1984, in respect of these years were clearly barred by limitation. The notice has to be quashed. However, as far as interest for the assessment year 1979-80 was concerned; the notice is not barred by limitation [Col. Sir Harindar Singh Brar vs. ITO (2006) 282 ITR 371 (P&H)].

11.3.11 Provision for cases where assessment is in pursuance of an order on appeal, etc. [Section 150]

(1) Notwithstanding anything contained in section 149, the notice under section 148 may be issued at any time for the purpose of making an assessment or reassessment or recomputation in consequence of or to give an effect to any finding or direction contained in an order passed by any authority in any proceeding under this Act by way of appeal, reference or revision or by a Court in any proceeding under any other law.

(2) The provisions of sub-section (1) shall not apply in any case where any such assessment, reassessment or recomputation as is referred to in that sub-section relates to an Assessment Year in respect of which an assessment, reassessment or recomputation could not have been made at the time the order which was the subject-matter of the appeal, reference or revision, as the case may be, was made by reason of any other provision limiting the time within which any action for assessment, reassessment or recomputation may be taken.

- This section prescribes the time limit for issuance of notice u/s 148 in a special case. This section overrides the provisions of section 149. Section 149 vide sub-section (2) provides that issue of notice u/s 148 is subject to the provisions of section 151. Thus, approval u/s 151 for issue of notice u/s 148(1) is not required in a case covered by section 150 [Sukhdayal Pahwa vs. CIT [1983] 140 ITR 206 (MP)].
- Notwithstanding the time limits prescribed by section 149, notice u/s 148 can be issued at any time for making assessment, etc., to give effect to any finding or direction referred to in sub-section (1). The order referred to therein may be an order u/s 250, 254, 260, 262, 263 or 264.
- The power conferred by sub-section (1) to the revenue for making assessment, etc., is withdrawn in a special case covered by sub-section (2). This covers a case where the order for an Assessment Year is made such order being the subject matter of an appeal, reference or revision, the finding or direction of which results in an assessment, etc., referred to in sub-section (1). However, at the time such order is made, the assessment etc, in respect of that A.Y. is itself time barred by virtue of any other provision of this Act. Sub-section (2) applies to such cases.
- Also see Explanations 2 and 3 to section 153.

11.3.12 Sanction for issue of notice [Section 151]

(1) No notice shall be issued under section 148 by an Assessing Officer, after the expiry of a period of four years from the end of the relevant assessment year, unless the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner is satisfied, on the reasons recorded by the Assessing Officer, that it is a fit case for the issue of such notice.

(2) In a case other than a case falling under sub-section (1), no notice shall be issued under section 148 by an Assessing Officer, who is below the rank of Joint Commissioner, unless the Joint Commissioner is satisfied, on the reasons recorded by such Assessing Officer, that it is a fit case for the issue of such notice.

(3) For the purposes of sub-section (1) and sub-section (2), the Principal Chief Commissioner or the Chief Commissioner or the Principal Commissioner or the Commissioner or the Joint Commissioner, as the case may be, being satisfied on the reasons recorded by the Assessing Officer about fitness of a case for the issue of notice under section 148, need not issue such notice himself.

11.3.13 Other provisions [Section 152]

(1) In an assessment, reassessment or recomputation made under section 147, the tax shall be chargeable at the rate or rates at which it would have been charged had the income not escaped assessment.

(2) Where an assessment is reopened under section 147, the assessee may, if he has not impugned any part of the original assessment order for that year either under sections 246 to 248 or under section 264, claim that the proceedings under section 147 shall be dropped on his showing that he had been assessed on an amount or to a sum not lower that what he would be rightly liable for even if the income alleged to have escaped assessment had been taken into account, or the assessment or computation had been properly made.

Provided that in so doing he shall not be entitled to reopen matters concluded by an order under section 154, 155, 260, 262 or 263.

11.3.14 Time limit for completion of assessment and reassessment [Section 153]

Regular assessment u/s 143 or 144 must be made within two years of the relevant Assessment Year or one year from the end of the Financial Year in which the return was filed whichever is later.

The provisions of Section 153 and 153B has been amended to provide an additional 3 months time limit for completion of assessment over the previous time line. The present position is appended below :

Proceeding under section	Previous allowed time limit	Amended time limit
143 or 144	21 months from the end of the Assessment Year	24 months from the end of the Assessment Year
143 or 144 and 92CA (Transfer pricing)	33 months from the end of the Assessment Year	36 months from the end of the Assessment Year
148	9 months from the end of the financial year in which notice was issued	12 months from the end of the financial year in which notice was issued
148 & 92CA	21 months from the end of the financial year in which notice was issued	24 months from the end of the financial year in which notice was issued
250, 254 or 263	9 months from the end of the financial year in which order was received	12 months from the end of the financial year in which order was received
250,254,263 & 92CA	21 months from the end of the financial year in which order was received	24 months from the end of the financial year in which order was received

The Finance Act, 2013 has made the following changes in sections 153 and 153B:

(i) Where a reference is made to TPO under section 92CA(1) during the course of proceeding for assessment of A.Y. 2009-10 and subsequent assessment years, the period of completion of assessment under section 143(3)/144 shall be 3 years whether reference is made to TPO before or after 1.7.2012.

(ii) Where notice under section 148 was served on or after 1.4.2010 and during the course of proceeding for the assessment/reassessment, etc. a reference in made to T.P.O. under section 92CA(1), the period of completion of assessment/ reassessment shall be two years whether reference is made to T.P.O. before or after 1-7-2012.

(iii) Where fresh assessment/reassessment has to be made on directions given under sections 254, 263 or 264 and during the course of such assessment or reassessment a reference is made to T.P.O. under section 92CA the period of completion of assessment/reassessment shall be two years whether reference to T.P.O. is made before or after 1.7.2012.

(iv) Clause (iii) of Explanation 1 to section 153 has been amended so as to provide that the period commencing from the date on which the Assessing Officer directs the assessee to get his accounts audited under section 142(2A) and

  (a) ending with the last date on which the assessee is required to furnish a report of such audit under that sub-section; or

  (b) where such direction is challenged before a court, ending with the date on which the order setting aside such direction is received by the Commissioner,

  shall be excluded in computing the period of limitation for the purposes of section 153.

  "(v) Clause (iv) of Explanation 1 to section 153 has been newly inserted by Finance (No. 2) Act, 2014 so as to provide that the period commencing from the date on which the Assessing Officer makes a reference to the Valuation Officer under sub-section (1) of section 142A and ending with the date on which the report of the Valuation Officer is received by the Assessing Officer, or".

(v) clause *(viii)* of *Explanation* 1 to section 153 has also been amended so as to provide that the period commencing from the date on which a reference or first of the references for exchange of information is made by an authority competent under an agreement referred to in section 90 or section 90A and ending with the date on which the information requested is last received by the Commissioner or a period of one year, whichever is less, shall be excluded in computing the period of limitation for the purposes of section 153.

Similar amendments have also been made in the *Explanation* to section 153B of the Income-tax Act relating to time limit for completion of search assessment and exclusion of time.

As per Explanation 1 to section 153, in computing the period of limitation for the purposes of this section the following period shall be excluded:

(i) the time taken in reopening the whole or any part of the proceeding or in giving an opportunity to the assessee to be reheard under the proviso to section 129 relating to change of incumbent of an office, or

(ii) the period during which the assessment proceeding is stayed by an order or injunction of any court, or

(iii) the period commencing from the date on which the Assessing Officer intimates the Central Government or the prescribed authority, the contravention of the provisions of clause (21) or clause (22B) or clause (23A) or clause (23B) or sub-clause (iv) or sub-clause (v) or sub-clause (vi) or sub-clause (via) of clause (23C) of section 10, under clause (i) of the proviso to sub-section (3) of section 143 and ending with the date on which the copy of the order withdrawing the approval or rescinding the notification, as the case may be, under those clauses is received by the Assessing Officer; or

(iv) the period commencing from the date on which the Assessing Officer directs the assessee to get his accounts audited under sub-section (2A) of section 142 and ending with the last date on which the assessee is required to furnish a report of such audit under that sub-section, or

(v) in a case where an application made before the Income-tax Settlement Commission under section 245C is rejected by it or is not allowed to be proceeded with by it, the period commencing from the date on which such application is made and ending with the date on which the order under section 245D(1) is received by the Commissioner, or

(vi) the period commencing from the date on which an application is made before the Authority for Advance Ruling under sub-section (1) of section 245Q and ending with the date on which the order rejecting the application is received by the Commissioner under sub-section (3) of section 245R, or

(vii) the period commencing from the date on which an application is made before the Authority for Advance Rulings under sub-section (1) section 245Q and ending with the date on which the advance ruling pronounced by it is received by the Commissioner under sub-section (7) of section 245R.

(viii) the period commencing from the date on which a reference for exchange of information is made by an authority competent under an agreement referred to in section 90 or section 90A and ending with the date on which the information so requested is received by the Commissioner or a period of 1 year, whichever is less.

(ix) the period commencing from the date on which a reference for declaration of an arrangement to be impermissible avoidance arrangement is received by the Commissioner under sub-section (1) of section 144BA and ending on the date on which a direction under sub-section (3) or sub-section (6) or an order under sub-section (5) of the said section is received by the Assessing Officer.

If, after the exclusion of the aforesaid period, the period of limitation available to the Assessing Officer for making an order of assessment or reassessment, as the case may be, is less than sixty days, such remaining period shall be extended to sixty days and the period of limitation shall be deemed to be extended accordingly.

Further, where a proceeding before the Settlement Commission abates under section 245HA, the period of limitation available under this section to the Assessing Officer for making an order of assessment, reassessment or re-computation, as the case may be, shall, after the exclusion of the period under section 245HA(4), be not less than one year; and where such period of limitation is less than one year, it shall be deemed to have been extended to one year; and for the purposes of determining the period of limitation under sections 149, 153B, 154, 155, 158BE and 231 and for the purposes of payment of interest under section 243 or section 244 or, as the case may be, section 244A, this proviso shall also apply accordingly.

The period during which the stay order staying the assessment proceedings was in operation is to be excluded for the purpose of computing the period of limitation for making the order of assessment [Auto & Metal Engineers vs. Union of India (1998) 229 ITR 399 (SC)].

11.3.15 Assessment in case of search or requisition [Section 153A]

Notwithstanding anything contained in section 139, section 147, section 148, section 149, section 151 and section 153, in the case of a person where a search is initiated under section 132 or books of account, other documents or any assets are requisitioned under section 132A after the 31st day of May, 2003, the Assessing Officer shall—

(a) issue notice to such person requiring him to furnish within such period, as may be specified in the notice, the return of income in respect of each Assessment Year falling within six Assessment Years referred to in clause (*b*), in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed and the provisions of this Act shall, so far as may be, apply accordingly as if such return were a return required to be furnished under section 139;

(b) assess or reassess the total income of six Assessment Years immediately preceding the Assessment Year relevant to the Previous Year in which such search is conducted or requisition is made.

The Assessing Officer shall assess or reassess the total income in respect of each Assessment Year falling within such six Assessment Years.

It is provided that assessment or reassessment, if any, relating to any Assessment Year falling within the period of six Assessment Years referred to in section 153A(1) pending on the date of initiation of the search under section 132 or making of requisition under section 132A, as the case may be, shall abate.

Provided also that the Central Government may by rules made by it and published in the Official Gazette (except in case where any assessment or reassessment has abated under the second proviso), specify the class or classes of cases in which the Assessing Officer shall not be required to issue notice for assessing or reassessing the total income for six Assessment Years immediately preceding the Assessment Year relevant to the Previous Year in which search is conducted or requisition is made.

Except as otherwise provided in this section, section 153B and section 153C, all other provisions of this Act shall apply to the assessment made under this section;

In an assessment or reassessment made in respect of an Assessment Year under this section, the tax shall be chargeable at the rate or rates as applicable to such Assessment Year.

Assessment of income of any other person [Section 153C]

(1) Notwithstanding anything contained in section 139, section 147, section 148, section 149, section 151 and section 153, where the Assessing Officer is satisfied that,—

(a) any money, bullion, jewellery or other valuable article or thing, seized or requisitioned, belongs to; or

(b) any books of account or documents, seized or requisitioned, pertains or pertain to, or any information contained therein, relates to,

a person other than the person referred to in section 153A, then, the books of account or documents or assets, seized or requisitioned shall be handed over to the Assessing Officer having jurisdiction over such other person and that Assessing Officer shall proceed against each such other person and issue notice and assess or reassess the income of the other person in accordance with the provisions of section 153A, if, that Assessing Officer is satisfied that the books of account or documents or assets seized or requisitioned have a bearing on the determination of the total income of such other person for the relevant assessment year or years referred to in sub-section (1) of section 153A.

Provided that in case of such other person, the reference to the date of initiation of the search under section 132 or making of requisition under section 132A in the second proviso to sub-section (1) of section 153Ashall be construed as reference to the date of receiving the books of account or documents or assets seized or requisitioned by the Assessing Officer having jurisdiction over such other person :

Provided further that the Central Government may by rules made by it and published in the Official Gazette, specify the class or classes of cases in respect of such other person, in which the Assessing Officer shall not be required to issue notice for assessing or reassessing the total income for six assessment years immediately preceding the assessment year relevant to the previous year in which search is conducted or requisition is made except in cases where any assessment or reassessment has abated.

(2) Where books of account or documents or assets seized or requisitioned as referred to in sub-section (1) has or have been received by the Assessing Officer having jurisdiction over such other person

after the due date for furnishing the return of income for the assessment year relevant to the previous year in which search is conducted under section 132 or requisition is made under section 132A and in respect of such assessment year—

(a) no return of income has been furnished by such other person and no notice under sub-section (1) of section 142 has been issued to him, or

(b) a return of income has been furnished by such other person but no notice under sub-section (2) of section 143 has been served and limitation of serving the notice under sub-section (2) of section 143 has expired, or

(c) assessment or reassessment, if any, has been made,

before the date of receiving the books of account or documents or assets seized or requisitioned by the Assessing Officer having jurisdiction over such other person, such Assessing Officer shall issue the notice and assess or reassess total income of such other person of such assessment year in the manner provided in section 153A.

11.3.16 Prior approval necessary for assessment in cases of search or requisition [Section 153D]

No order of assessment or reassessment shall be passed by an Assessing Officer below the rank of Joint Commissioner in respect of each Assessment Year referred to in clause (*b*) of section 153A or the Assessment Year referred to in clause (*b*) of sub-section (1) of section 153B, except with the prior approval of the Joint Commissioner."

QUESTIONS & ANSWERS

RETURN OF INCOME:

Question 1. What is the due date of filling of return of income in case of a non-working partner of a firm whose accounts are not liable to be audited?

Answer : Due date of furnishing return of income in case of non-working partner shall be 31st July of the Assessment Year whether the accounts of the firm are required to be audited or not.

A working partner for the above purpose shall mean an individual who is actively engaged in conducting the affairs of the business or profession of the firm of which he is a partner and is drawing remuneration from the firm.

Question 2. What do you mean by annexure less return? What is the manner of filling the return of income?

Answer : The return of income required to be furnished in Form No. ITR-1, ITR-2, ITR-3, ITR-4, ITR-5, ITR-6 or ITR-7 shall not be accompanied by a statement showing the computation of the tax payable on the basis of the return, or proof of the tax, if any, claimed to have been deducted or collected at source or the advance tax or tax on self-assessment, if any, claimed to have been paid or any document or copy of any account or Form or report of audit required to be attached with the return of income under any of the provisions of the Act.

Manner of filling the return: The return of income referred to in sub-rule (1) may be furnished in any of the following manners, namely:-

(i) Furnishing the return in a paper form;

(ii) Furnishing the return electronically under digital signature;

(iii) Transmitting the data in the return electronically and thereafter submitting the verification of the return in Form ITR-V;

(iv) Furnishing a bar-coded return in paper form.

Question 3. Is e-filling of return mandatory? State the assessee's for whom e-filling of returns is mandatory?

Answer : CBDT has vide notification No. 34/2013 dated 01.05.2013 has made it mandatory for the following category of the Assesses to file their Income Tax Return Online from A.Y. 2013-14 :-

(a) It is mandatory for every person (not being a co. or a person filing return in ITR 7) to e-file the return of income if its total income exceeds ₹5,00,000

(b) an individual or a Hindu Undivided Family, being a resident, having assets (including financial interest in any entity) located outside India or signing authority in any account located outside India and required to furnish the return in Form ITR-2 or ITR-3 or ITR-4, as the case may be.

(c) Every person claiming tax relief under Section 90, 90A or 91 shall file return in electronic mode.

(d) Those who are required to get their Accounts audited under Section 44AB, 92E, 115JB.

(e) A company required to furnish the return in Form ITR-6.

However, as per instruction of ITR 7 From assessment year 2013-14 onwards in case an assessee who is required to furnish a report of audit under section 10(23C)(iv), 10(23C)(v), 10(23C)(vi), 10(23C)(via), 10A, 12A(1)(b), 44AB, 80-IA, 80-IB, 80-IC, 80-ID, 80JJAA, 80LA, 92E or 115JB he shall file the report electronically on or before the date of filing the return of income.

Question 4. Can unabsorbed depreciation be carried forward even if the return is filed after due date?

Answer : Unabsorbed depreciation can be carried forward even if the return of loss is submitted after the due date, as it is not covered under Chapter VI of set off or carry forward of losses but covered u/s 32(2).[East Asiatic Co.(India) Pvt. Ltd. vs.CIT (1986) 161 ITR 135(Mad.)]

Question 5. Can a belated return of income filed u/s 139(4) be revised?

Answer : There was a difference of opinion among various courts regarding filling of revised return in respect of belated returns. However, it has been held that a belated return filed u/s 139(4) cannot be revised as section 139(5) provides that only return filed u/s 139(1) or in pursuance to a notice u/s 142(1) can be revised [Kumar Jagdish Chandra Sinha vs.CIT(1996) 220 ITR 67(SC)].

Question 6. Can a revised return be further revised?

Answer : If the assessee discovers any omission or any wrong statement in a revised return, it is possible to revise such a revised return provided it is revised within the same prescribed time [Niranjan Lal Ram Chandra vs.CIT (1982) 134 ITR 352 (All.)]

Question 7. Can an Assessing Officer himself allot Permanent Account Number to an assessee?

Answer: The Assessing Officer having regard to the nature of the transactions as may be prescribed may also allot a Permanent Account Number to any other person(whether any tax is payable by him or not) in the manner and in accordance with the procedure as may be prescribed.

Question 8. What are the consequences if a person fails to comply with the provisions of Sec.139A i.e. quoting of PAN?

Answer : As per Sec. 272B(2), if a person fails to comply with the provisions of Sec.139A, the Assessing Officer may direct that such person shall have to pay, by way of penalty, a sum of ₹10,000.

Question 9. Who can verify the return of HUF, if HUF does not have a major member?

Answer : If the HUF has no major members as its Karta, a return may validly be verified by the eldest minor member of the family who manages the affairs of the family [Sridhar Udai Narayan vs.CIT(1962) 45 ITR 577 (All.)]

ASSESSMENT PROCEDURE:

Question 10: What is a protective assessment under Income-tax law? What is the procedure followed for the recovery of tax in such cases?

Answer: A protective assessment is made in a case where there are doubts relating to the true ownership of the income. If there is an uncertainty about the taxing of an income in the hands of Mr. A or Mr. B, then at the discretion of the Assessing Officer, the same may be added in the hands of one of them on protective basis. This is to ensure that on finality, the addition may not be denied on the ground of limitation of time. Once finality regarding the identity of the tax payer to be taxed is established, the extra assessment is cancelled. But the Department cannot recover the tax from both the assessees in respect of the same income. Penalty cannot be imposed on the strength of a protective assessment.

Question 11: Joseph, engaged in profession, filed his return of income for Assessment Year 2016-17 on 15th November, 2016. He disclosed an income of ₹4,00,000 in the return. In February, 2017 he discovered that he did not claim certain expenses and filed a revised return on 3rd February, 2017 showing an income of ₹1,80,000 and claiming those expenses. Is the revised return filed by Joseph acceptable?

Answer: Joseph is engaged in profession. The due date for filing income tax return for Assessment Year 2016-17 as per section 139(1) of the Income-tax Act is 30th September, 2016 if his accounts are required to be audited under any law. The due date is 31st July, 2016 if the accounts are not required to be audited under any law.

The return was filed beyond the due date prescribed in section 139(1). The return so filed is covered by section 139(4) and the time limit is one year from the end of the relevant Assessment Year. The Apex court in *Kumar Jagadish Chandra Sinha vs. CIT 220 ITR 67 (SC)* has held that a return filed under section 139(4) is not eligible for revision and hence a revised return cannot be filed.

Hence, the revised return filed by Joseph is not valid as the original return was not filed before the due date mentioned in section 139(1).

Question 12: An assessee filed a return of income on 31.8.2016 in respect of Assessment Year 2016-17 disclosing an income of ₹5 lakhs from business. It was not accompanied by proof of payment of tax due on self-assessment. Discuss the validity of such a return.

Answer : As per Explanation to sub-section (9) of section 139 a return is regarded as defective unless it is accompanied by proof of tax deducted at source, advance tax and tax on self-assessment, if any, claimed to have been paid. Therefore, the return is prima facie defective. It is not invalid at that stage. On receipt of the return, the Assessing Officer has to intimate the defect to the assessee and give him an opportunity to rectify the defect within a period of 15 days from the date of such intimation or within such further period which, on application by the assessee, he may, in his discretion, allow. If the defect is not rectified within the said period, the return will be treated as an invalid return and the provisions of the Income-tax Act shall apply, as if the assessee has failed to furnish the return.

Also, it may be noted that section 140A(3) says that if an assessee fails to pay tax or interest on self assessment he shall be deemed to be an assessee in default in respect of the tax or interest or both remaining unpaid and all the provisions of the Act shall apply accordingly.

Question 13: If an assessment is remanded back to Assessing Officer, can he introduce new sources of income for assessment?

Answer: Where the assessment is set aside by the Tribunal and the matter remanded to the Assessing

Officer, it is not open to him to introduce into the assessment new sources of income so as to enhance the assessment. Any power to enhance is confined to the old sources of income which were the subject matter of appeal [Kartar Singh vs.CIT (1978) 111 ITR 184 (P &H)].

Question 14: Can Department make fresh computation, once the assessment is made final?

Answer: It is now a well settled principle that an assessment once made is final and that it is not open to the department to go on making fresh computation and issuing fresh notices of demand to the end of all time. [ITO vs.Habibullah (S.K.) (1962) 44 ITR 809 (SC)]

Question 15: Can an Assessing Officer make an assessment for a year other than the assessment year for which the return is filed?

Answer: It is not open to the Assessing Officer to make assessment in respect of a year other than the Assessment Year for which the return is filed. Thus, in respect of a return filed for Assessment Year 2014-15, assessment cannot be made for the Assessment Year 2015-16. [CIT vs. Amaimugan Transports Pvt. Ltd. (1995) 215 ITR 553 (Mad.)]

Question 16: Can an Assessing Officer assess the income below the returned income or assess the loss higher than the returned loss?

Answer: The Assessing Officer cannot assess income under section 144 for an assessment below the returned income or cannot assess the loss higher than the returned loss.

Question 17: Can incomplete, unsigned or unverified return lead to best judgement assessment?

Answer: Incomplete, unsigned or unverified return may lead to best judgement assessment. A best judgement assessment can be made when the return is filed woefully incomplete or not signed and verified. [Behari Lal Chatterji vs.CIT (1934) 2 ITR 377 (All.)]

Question 18: Can assessee follow different method of accounting for different businesses?

Answer: If an assessee is carrying on more than one business, he can follow cash system of accounting for one business and mercantile system (accrual system) of accounting for other business. Similarly, if he had more than one sources of income under the head Income from Other Sources, he can follow accrual system for one source of income under the head Income from Other Sources, and cash system for other sources of income.

Question 19: What can Assessing Officer do when the assessment is not set aside for fresh assessment but annulled?

Answer: Where an assessment is not set aside for fresh assessment but annulled, no extended limitation is available. However, if the original time limit is available, the Assessing Officer may proceed from the stage at which illegality which resulted into the annulment of the assessment supervened and make the assessment afresh. [CIT vs.Mrs.Ratanbai N.K. Dubhash (1998) 230 ITR 495(Bom.)]

Question 20: An assessment was made on S originally in the status of a nonresident. In the re-assessment made under section 147, he is assessed as resident and ordinarily resident on the ground that the correct status was not disclosed in the return of income filed originally. Is the change of status valid in a re-assessment?

Answer: This case is based on a case decided by the Punjab & Haryana High Court in CIT vs. Surmukh Singh Uppal (Dr) (1983) 144 ITR 191(P&H) in which the court held that if an assessee fails to disclose fully and truly all the material facts at the time of original assessment then the question of status could be determined in reassessment proceedings if, on account of the non-disclosure of the facts fully and truly, there had been an escapement of income.

In view of the aforesaid case, the action taken by the Assessing Officer in assessing S as a resident and ordinarily resident is correct.

Question 21: A non-resident individual was assessed originally on income arising in India on 8-3-2014 in respect of assessment year 2013-14. The Assessing Officer discovered an omission in the assessment and issued notice to the statutory agent on 10-12-2015 for re-assessment of the omitted income under section 147. Assuming that the statutory agent has been given notice of his appointment and has been heard u/s 163, how will he contest the validity of the re-assessment?

Answer: Section 163(2) provides that no person shall be treated as the agent of a non-resident unless he had an opportunity of being heard by the Assessing Officer as to his liability to be treated as such.

In the present case, the assessee has been given an opportunity of being heard and also the notice has been issued within the time limits laid down under section 148. Hence, the reassessment proceedings are valid.

Question 22: An assessee filed a return showing, inter alia, a sum of ₹35,000 as capital receipt and hence not liable to tax. The Assessing Officer accepted the claim of the assessee and made the assessment on the income disclosed. Subsequently, a successor to the Assessing Officer came across a judgment of the High Court under which the amount claimed as exempt was held to be liable to tax, under identical circumstances. The assessment was re-opened under section 147. The assessee wants you to contend that the notice under section 147 is not valid. What is your opinion?

Answer: This case is based on Explanation 2 to section 147 which provides that where an assessment has been made, but income chargeable to tax has been under-assessed then it shall be deemed that income has escaped assessment. In the present case, the successor to the Assessing Officer came across a High Court judgment according to which ₹35,000 was taxable in similar circumstances. Thus, clearly the Assessing Officer has reason to believe that income chargeable to tax has been under assessed. Hence, the income of ₹35,000 could be re-assessed within the time limit.

Question 23: T Ltd effected purchases of stock-in-trade of the value of ₹1,50,000 from A and Co. during the financial year 2015-16. Vouchers in support of the purchases were produced before the Assessing Officer, who accepted the claim. Subsequently, the Assessing Officer received specific information that the said purchases were not genuine and A and Co. had denied the transaction. The Assessing Officer thereafter re-opened the assessment under section 147. T Ltd challenges the validity of the re-assessment on the ground that it had disclosed all the primary facts and the Assessing Officer ought to have verified the genuineness of the claim at the time of the original assessment?

Answer: This case is based on Explanation 1 to section 147 which provides that production before the Assessing Officer of books of account or other evidence from which material evidence could with due diligence have been discovered by the Assessing Officer will not necessarily amount to disclosure within the meaning of the first proviso. Re-assessment proceedings may be started either on the ground that some fresh facts have come to light which were not previously disclosed or some information with regard to the facts previously disclosed come to light which tends to expose the untruthfulness of those facts.

In view of the aforesaid provisions, the contention of T Ltd is not correct. The action of the Assessing Officer is justified.

Question 24: Raj files the return of income disclosing an income of ₹4,00,000. The full tax payable on the declared income is covered by tax deducted at source, advance tax and tax on self assessment. The Assessing Officer, through oversight, does not pass any order thereon and the assessment becomes barred by limitation. The assessee claims that since no assessment has been made, on him, the entire tax paid by him is refundable. Discuss the correctness or otherwise of the claim?

Answer: This case is based on a case decided by the Gujarat High Court in ITO vs. Saurashtra Cement & Chemical Industries Ltd. (1992) 194 ITR 659 in which the court held that liability to pay income-tax chargeable under section 4(1) of the Act does not depend upon the assessment being made by the Income-tax Officer but depends on the enactment by any Central Act prescribing rate or rates for any assessment year. Thus, as soon as the rates are prescribed by the appropriate legislation, the liability to pay tax arises on the total income which is to be computed by the assessee in accordance with the provisions of the Act, if it exceeded the maximum amount not chargeable to tax.

On the filing of returns under section 139, the provisions of self-assessment contained in section 140A come into operation and it becomes obligatory on the part of the assessee to discharge his liability which has arisen to pay the tax together with the interest that may be payable for late furnishing of returns. The tax payable on the basis of the returns filed by the assessee is treated as 'assessed tax'. It is not at all made dependent on any regular assessment being made though, in the event of regular assessment, the amount paid under sub-section (1) of section 140A is deemed to have been paid towards the regular assessment. Therefore, by no stretch of imagination, can the tax paid and collected under section 140A be described as a mere ad hoc or interim payment which can be said to fall in the absence of a regular assessment. The procedure of assessment by the Income-tax Officer is essentially to check the computation of total income done by the assessee and to find out whether the computation made is correct or not. Where the return has been accepted by the Income-tax Officer who may not assess the total income, it cannot be said that the liability to pay the tax under the Act on the basis of the admitted total income as reflected from the returns would vanish.

In view of the aforesaid case, the claim of the assessee is not valid.

Study Note - 12

SEARCH AND SEIZURE

This Study Note includes

12.1 SEARCH AND SEIZURE

Search and seizure can be authorised by—

(a) The Director General of Income Tax, or
(b) The Director of Income Tax, or
(c) The Chief Commissioner of Income Tax, or
(d) The Commissioner of Income Tax, or
(e) The Additional Director or Additional Commissioner, or
(f) The Joint Director or Joint Commissioner of Income Tax.

The Director General or Director or the Chief Commissioner or Commissioner may authorise any officer subordinate to him but not below the rank of Income Tax Officer to conduct such search. Similarly, Additional Commissioner, Joint Commissioner or Additional Director/Joint Director can authorise any officer subordinate to him but not below the rank of Income Tax Officer to do so.

However, no authorization shall be issued by the Additional Director or Additional Commissioner or Joint Director or Joint Commissioner on or after 1.10.2009, unless he has been empowered by the Board to do so.

The Officer so authorised is referred as Authorised Officer. The authorisation is done by issuing a search warrant in Form 45.

Authorisation for search and seizure can take place if the above authority, in consequence of information in his possession, has reason to believe that:

(a) any person to whom summons under section 131(1) or notice under section 142(1), was issued to produce or cause to be produced any books of account, or other documents has wilfully omitted or failed to produce or caused to produce such books of account or other documents as required by such summons or notice;

(b) any person to whom summons or notice, as aforesaid, has been or might be issued, will not or would not produce any books of account or other documents which will be useful or relevant to any proceeding undertaken under the Income Tax Act;

(c) any person is in possession of any money, bullion or jewellery, or other valuable article or things and these assets represent either wholly or partly the income or property which has not been or would not be disclosed by the person concerned for the purposes of this Act.

From the above it is clear that the persons to be searched are persons:

(a) who have books of account or documents which have not been produced or are not likely to be produced in response to notices or/summons, or

(b) persons who are likely to be in possession of undisclosed income or property.

Case Laws

(1) Clauses (a), (b) and (c) of section 132(1) spell out the circumstances under which the Authorising Authority may issue a warrant of authorization. Under clause (a) action may be taken if a person is served inter alia with a summons u/s 131 or notice u/s 142(1) to produce or cause to be produced specified books of account or other documents and he fails to comply. Such non-compliance affords a surer base for the issuance of the authorization. Under clause (b), a formal notice is not essential. The Authorising Officer must have reason to believe that the person, whether or not a notice has been served on him, is not likely to produce his books, etc. The basic, in such a case, is that the person will suppress books of account and other documents which may be useful and relevant to an income-tax proceeding. Here the Authorising Authority, if challenged, has to prove the basis of his belief. [Mamchand and Co. vs. CIT (1970) 76 ITR 217 (Cal) ; Kusum Lata vs. CIT (1989) 180 ITR 365 (Raj)].

(2) In order to attract clause (c) there must be information with the Authorising Authority relating to two matters. Firstly, that any person is in possession of money, etc. and Secondly, that such money, etc. represents either wholly or partly income or property which has not been or would not be, disclosed for the purposes of the Act. [CIT vs. Ramesh Chander (1974) 93 ITR 450 (Pun)]. In cases under clause (c), a stiffer burden lies on the Authorising Authority to justify the ground of his belief.

It may be observed that before invoking the provisions of section 132(1), the Director General or the Director or the Chief Commissioner or Commissioner or Joint Director or Joint Commissioner must have reasons to believe that there is justification for such search and seizure as one of the conditions mentioned in section 132(1)(a), (b) or (c) is satisfied. He must, before taking such action, record his reason to believe that the Case is fit for such action. 'Reason to believe' means that the Officer has faith or accepts a fact to exist. Belief must be genuine and not a mere pretence and has to be held in good faith and not a reason to suspect. [ITO vs. Lakshman Mewal Das (1976) 103 ITR 437 (SC)].

In this case disclosure of the material or the information to the person against whom the action is taken u/s 132(1) is not mandatory, because such disclosure might affect or hamper the investigation [Southern Herbals Ltd. vs. DIT (Investigations) (1994) 207 ITR 55 (Karn)]. Only the High Courts and the Supreme Court have the jurisdiction to call for and look into the reasons recorded to decide whether the issue of the search warrant was called for. [Dr. Pratap Singh vs. Director of Enforcement (1985) 155 ITR 166 (SC)].

There is no mandate of section 132 or any other provision in Act that reasonable belief recorded by Designated Authority before issuing warrant of authorization must be disclosed to assessee. Therefore, fact that a copy of information received or satisfaction note recorded by Designated Authority has not been furnished to assessee, cannot be a ground to hold that search and seizure proceedings against assessee are bad in law. [Genom Biotech Pvt. Ltd. vs. Director of Income Tax, (Investigation) (2009) 180 Taxman 395 (Bom)].

Where search or seizer conducted illegally or irregularly, the materials so obtained during the search or seizure can nevertheless be utilised for the purpose of an ordinary assessment. [Pooran Mai vs. Director of Inspection (Investigation), Income-tax (1974) 97 ITR 505 (SC)].

Search can be authorised by a CCIT/CIT other than jurisdictional CCIT/CIT:

(1) The Chief Commissioner/Commissioner of Income Tax has the power to authorise a search of any building, place, vessel, vehicle or aircraft of a person which is under his jurisdiction and also in cases where such building, place, vessel, vehicle or aircraft is in his area of jurisdiction but he has no jurisdiction over the persons concerned, if he has reason to believe that any delay in obtaining authorisation from the Commissioner having jurisdiction over the person would be prejudicial to the interests of revenue. Such authorization shall be given in Form 45A. [First proviso to section 132(1)].

For example, if the search is to be conducted in the premises of a person in Mumbai but such person is an assessee in Kolkata i.e. the jurisdiction of the assessee is with Chief Commissioner of Kolkata, then the Chief Commissioner/Commissioner of Income Tax Mumbai can authorise such search instead of getting authorisation from jurisdictional Chief Commissioner i.e. Chief Commissioner Kolkata.

(2) Where a search for any books of account or other documents or assets has been authorised by any authority who is competent to do so, and some other Chief Commissioner / Commissioner in consequence of information in his possession has reason to suspect that such books of account or other documents and asset, etc. of the assessee are kept in any building, place, vessel, vehicle or aircraft not specified in the search warrant issued by such authority, he may authorise the Authorised Officer to search such other building, place, vessel, vehicle or aircraft [Section 132(1A)]. Such authorization shall be given in Form 45B.

For example, if a search warrant is issued by the Director of Income Tax, Channai, authorising the search of a premises in Mumbai and the Authorised Officer finds that the books of account or other documents and/or assets have been secreted in a building or place not specified in the search warrant, he could request any of the local Commissioner of Mumbai to authorise him to search that building or place.

The Authorised Officer for search and seizure, shall have the powers to —

(a) enter and search any building, place, vessel, vehicle or aircraft where he has reason to suspect that such books of account, other documents, money, bullion, jewellery or other valuable article or thing are kept;

(b) break to open the lock of any door, box, locker, safe, almirah or other receptacle for exercising the powers conferred where the keys thereof are not available;

(c) search any person who has got out of, or is about to get into, or is in the building, place, vessel, vehicle or aircraft, if the Authorised Officer has reason to suspect that such person has secreted about his person any such books of account, other documents, money, bullion, jewellery or other valuable article or thing;

(d) require any person who is found to be in possession or control of any books of account or other documents maintained in the form of electronic records, to afford the necessary facility to the Authorised Officer to inspect all such books of account or other documents;

(e) seize any such books of account, other documents, money, bullion, jewellery or other valuable article or thing found as a result of such search. However, w.e.f. 1.6.2003, the Authorised Officer shall have no power to seize any bullion, jewellery or other valuable article or thing being stock-in-trade of the business found as a result of search. He shall make a note or inventory of such stock-in-trade of the business,

(f) place marks of identification on any books of account or other documents or make or cause to be made extracts or copies therefrom;

(g) make a note or an inventory of any such money, bullion, jewellery or other valuable article or thing.

If any person searched holds any bullion, jewellery or any other valuable article or things is held as stock-in-trade of the business, it cannot be seized, whether or not the person is able to explain the source of acquisition of such stock. Whether such stock is disclosed or undisclosed, it is immaterial and the same cannot be seized in any circumstance. However, the restriction on seizure of stock-in-trade does not apply to cash. Unaccounted cash can be seized even if it forms part of stock-in-trade of the assessee. For example for a person carrying on business of money lending or exchange of currency, cash in hand is stock-in-trade but it can still be seized.

Case Laws:

(1) Where the client of the auditor was subject to search and the audit firm itself had not been subject to search, on a writ petition by the auditors, it was held the search party does not have access to data of the other clients contained in the laptops of the auditor. [S. R. Batliboi & Co. vs. Department of Income-tax (Investigation) (2009) 315 ITR 137 (Del)].

(2) Survey of Chartered Accountant's office and impounding the books of accounts of the assessee would not constitute breach of privilege to which professional like a practicising accountant or lawyer would be entitled. Hence, both survey and consequent impounding of documents would be in order. [U.K. Mahapatra and Co. vs. Income-tax Officer (2009) 308 ITR 133 (Ori)].

Additional power and duties of Autliorised Officer are as follows:

(1) Deemed seizure [Second proviso to section 132(1)]: Where it is not possible or practicable to take physical possession of any valuable article or thing and remove it to a safe place due to its volume weight or other physical characteristics or due to its being of a dangerous nature, the Authorised Officer may serve an order on the owner or the person who is in immediate possession thereof that he shall not remove, part with or otherwise deal with it except with the previous permission of such Authorised Officer and such action of the Authorised Officer shall be deemed to be seizure of such valuable article or thing. However, w.e.f. 1.6.2003 in the case of such deemed seizure also, the Authorised Officer shall have no power to seize any valuable article or thing, being stock in trade of the business.

(2) Restraint order [Section 132(3) with Explanation and section 132(8A)]: In case it is not possible or practicable to seize any books of account, or other documents, or money, bullion jewellery or other valuable articles or things for reasons other than those mentioned in (1) above, the Authorised Officer may serve an order on the owner or a person who is in immediate possession or control thereof that he shall not remove or part with or otherwise deal with it except with the previous permission of such Officer and such Officer may take such steps as may be necessary for compliance of this sub-section. However, in this case serving of such order shall not be deemed to be seizure of such books of account, etc. Such order is commonly known as an attachment order. The order u/s 132(3) shall not be in force for a period exceeding sixty days from the date of the order.

    Sub-section (3) can be resorted to only if there is any practical difficulty in seizing the item that is liable to be seized. Where the assessee has deposited the money in a bank, a prohibitory order under section (3) should be served not on the bank but on the assessee and a copy thereof may be sent to the bank. Attachment under sub-section (3) should be made only when the officer is satisfied that the asset is undisclosed.

(3) Power to requisition service of a Police Officer or Officer of the Central Government [Section 132(2)]: The Authorised Officer may requisition the services of any Police Officer or any of the Officer of the Central Government or of both to assist him for all or any of purposes specified in sub-section (1) and (1A) and it will be duty of every such Officer to comply with such requisition.

(4) Examination of any person on oath [Section 132(4) with Explanation]: The Authorised Officer may, during the course of the search or seizure, examine on oath any person who is found to be in possession or control of any books of account, documents, money, bullion, jewellery or other valuable article or thing and any statement made by such person during such examination may thereafter be used in evidence in any proceeding under the Income Tax Act, 1961. The statement can be recorded during the course of search and seizure or when it is over. Further, an explanation has been added to provide that the examination of any person may be not merely be in respect of any books of account, other documents or assets found as a result of the search, but also in respect of all matters relevant for the purposes of any investigation connected with any proceeding under the Income Tax Act, 1961.

The Authorised Officer may record statement wherein he may question on all matters which he may deem to be relevant for the purpose of the assessment, unearthing of concealed assets, source of income, investments made during different years, source of investments, marriages performed, expenses incurred on marriages and other ceremonial occasions, sources of expenditure incurred, household expenses and similar other aspects.

The person giving the statement has to be cautious while giving the statement. The admission of any fact therein will entail the financial liabilities and legal consequences resulting thereof in respect of taxation and penalties and prosecution in view of amended provision as per the Finance Act, 2003 with effect from 1.6.2003 for making assessment of search Cases. However, this statement, if no further indiscriminating documents have been found in the search, can be retracted later on but there should be a reasonable ground for the same. The retraction of statement recorded later on has been subject-matter of many judicial pronouncements and conflicting judgments over the same issue are there. But the majority of the Courts including the Agra Bench of the Tribunal have taken the decision favouring assesses that, in the circumstances where there is no undiscriminating material found in the search justifying the surrender in the statement, the same can be retracted.

(5) Presumption of ownership of books of account and asset and its truthfulness [Section 132(4A)]: Where any books of account, other documents, money, bullion, jewellery and other valuable article is found in possession or control of any person in the course of search, it may be presumed that—

(a) the books of account or other documents and assets found in the possession of any person in the course of a search belong to such person;

(b) the contents of such books of account and other documents are true; and

(c) the signature and every other part of such books of account and other documents which purports to be in the handwriting of any particular person are in handwriting of that person or which may reasonably be assumed to have signed or written the books of account or other documents are in that person's handwriting. In case of documents stamped, executed or attested that it was duly stamped and executed or attested by the person by whom it purports to have been so executed or attested.

(6) Retention of books of account and other documents [Section 132(8)]: The books of account or other documents seized under this section shall not be retained by the Authorised Officer (if he is himself a Assessing Officer) for a period exceeding 30 days from the date of the order of assessment u/s 153A or u/s 158BC(c) (relating to assessment of search cases/block assessment) unless the reasons for retaining the same are recorded by him in writing and the approval of the Chief Commissioner, Commissioner, Director General or Director for such retention is obtained.

However, that the Chief Commissioner, Commissioner, Director General or Director shall not authorise the retention of the books of account and other documents for a period exceeding thirty days after all the proceedings under the income Tax Act, in respect of the years for which the books of account or other documents are relevant are completed.

According to Section 132(10) if a person, legally entitled to the books of account or other documents seized, objects for any reason to the approval of extension given by Chief Commissioner, etc. as above, he may make an application to the Board for return of such books of account and documents and the Board may, after giving the applicant an opportunity of being heard, pass such order as it thinks fit.

The following two conditions must be fulfilled before the retention of books for the extended period is permissible:

(a) The Authorised Officer or the concerned Assessing Officer seeking the Commissioner's approval should record the reasons for retaining the books in writing.

(b) He should obtain the approval of CIT for the extended period. [CIT vs. Oriental Rubber Works (1984) 145 ITR 477 (SC)].

(7) Copies of extract of books of account and documents [Section 132(9)]: The person from whose custody any books of account or documents are seized under this section may make copies thereof, or take extracts there from, in the presence of the Authorised Officer or any person empowered by him in this behalf, at such place and time as the Authorised Officer may appoint in this behalf.

Right of copies and taking extracts from the account books is available only to the person from whose custody the books are seized. Others shall be entitled to the copies as and when the same are used by the Tax Authorities against him. [Manickchand Gupta vs. CIT (1988) 173 ITR 662 (All)].

(8) Handing over of seized books and assets to Assessing Officer [Section 13 2(9A)]: The Authorised Officer, if he is not the Assessing Officer, is required to hand over the books of account or other documents or any money, etc., seized by him to the Assessing Officer having jurisdiction over the person searched within a period of 60 days from the date on which the last of the authorisation for search was executed; and thereafter, the powers and functions of the Authorised Officer under section 132(8) and (9) would be exercised by the Assessing Officer.

Power to requisition books of account etc. [Section 132A]

(1) Requisitioning of books of account, etc. taken into custody under any other law. Section 132A provides that in case where any books of account or other documents and assets have been taken into custody by the Officer or authority under any other law e.g., by the Collector of Customs, the Sales Tax Commissioner, etc., the Director General or Director or the Chief Commissioner or Commissioner of Income-tax may, in such circumstances as are covered by section 132 for search and seizure, authorise in Form No. 45C any Additional Director, Additional Commissioner, Joint Commissioner, Joint Director, Deputy Director, Deputy Commissioner, Assistant Commissioner, Assistant Director or the Assessing Officer (Requisitioning Officer) to require such Officer or authority to deliver to him such books of account or other documents and assets.

In case where such a requisition is made the officer or the authority concerned would be required to deliver the books of account or other document and assets to the Requisitioning Officer either forthwith or, when such Officer or the Authority is of the opinion that it is no longer necessary to retain the same in his custody.

This section empowers the Income Tax Authorities to requisition assets and documents which are in the custody of any Officer or Authority under any other law but not those which are in the custody of the court, since the words Officer or Authority would not include a Court. [CIT vs. Balbar Singh (Decd.) (1993) 203 ITR 650 (P&H)].

A bank draft voluntarily sent to a banker for realization is not an asset in custody. Thus, the banker has no control or authority over the draft. It only accepts the instrument for a limited purpose. When it is in the custody of the banker, the banker retains it on behalf of the customer. The banker cannot utilise the draft for any purpose other than what has been desired by the customer. The bank draft when presented for clearing by the customer to the bank cannot be said to have been taken into custody by the bank to attract the applicability of section 132A. [Samta Construction Co. vs. Pawan Kumar Sharma, Deputy Director of Income Tax (Investigation) (2000) 244 ITR 845 (MP)].

(2) Cases when can such power be invoked [Rule 112D]: Powers under section 132A of Income Tax Act, 1961, to requisition books of account, etc. can be invoked by the Director General or Director or the Chief Commissioner or Commissioner, when he, in consequence of information in his possession, has reason to believe that—

(a) any person to whom summons u/s 131(1) or a notice u/s 142(1) was issued to produce, or cause to be produced, any books of account or other documents has omitted or failed to produce, or cause to be produced, such books of account or other documents, as required by such summons or notice and the said books of account or other documents have been taken into custody by any Officer or Authority under any other law for the time being in force; or

(b) any books of account or other documents will be useful for, or relevant to, any proceeding under the Act and any person to whom a summons or notice as aforesaid has been or might be issued will not, or would not, produce or cause to be produced, such books of account or other documents on. the return of such books of account or other documents by any Officer or Authority by whom or which such books of account or other documents have been taken into custody under any other law for the time being in force; or

(c) any assets represent either wholly or partly income or property which has not been, or would not have been disclosed for the purposes of the Act, by any person from whose possession or control such assets have been taken into custody by any Officer or Authority under any other law for the time being in force. [Section 132A(1)].

The Authorised Officer requisitioning the books of account shall make the order of requisition in writing. Such requisition shall be accompanied by a copy of authorisation in Form No. 45C.

Application of seized or requisitioned assets [Section 132B]

(1) According to section 132B(1) where the assets seized under section 132 or requisitioned under section 132A may be dealt with in the following manner, namely:—

(i) The amount of any existing liability under this Act, the Wealth Tax Act, 1957 the Expenditure Tax Act, 1987 the Gift Tax Act, 1958 and the Interest Tax Act, 1974, and the amount of the liability determined on completion of the assessment under section 153A or under Chapter XIV-B for the block period (including any penalty levied or interest payable in connection with such assessment) and in respect of which such person is in default or is deemed to be in default, or the amount of liability arising on an application made before the Settlement Commission under sub-section (1) of Section 245C, may be recovered out of such assets.

Provided that where the person concerned makes an application to the Assessing Officer within 30 days from the end of the month in which asset was siezed, for release of asset and the nature and source of acquisition of any such asset is explained to the satisfaction of the Assessing Officer, the amount of any existing liability referred to in this clause may be recovered out of such asset and the remaining portion, if any, of the asset may be released, with the prior approval of the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner, to the person from whose custody the assets were seized.

Provided further that such asset or any portion thereof as is referred to above shall be released within a period of 120 days from the date on which the last of the authorisations for search u/s 132 or for requisition u/s 132A, as the case may be, was executed.

(ii) If the assets consist solely of money, or partly of money and partly of other assets, the Assessing Officer may apply such money in the discharge of the liabilities referred to in clause (i) and the assessee shall be discharged of such liability to the extent of the money so applied.

(iii) The assets other than money may also be applied for the discharge of any such liability referred to in clause (i) as remains undischarged and for this purpose such assets shall be deemed to be under distraint as if such distraint was effected by the Assessing Officer or, as the case may be, the Tax Recovery Officer under authorisation from the Principal Chief Commissioner or Chief Commissioner or Principal Commissioner or Commissioner u/s 226(5) and the Assessing Officer or, as the case may be, the Tax Recovery Officer may recover the amount of such liabilities by the sale of such assets and such sale shall be effected in the manner laid down in the Third Schedule.

(2) According to section 132B(3) any assets or proceeds thereof which remain after the liabilities (existing and future) referred to in clause (i) of subsection (1) are discharged, shall be forthwith made over or paid to the persons from whose custody the assets were seized.

Nothing contained in section 132A shall preclude the recovery of the amount of liabilities aforesaid by any other mode laid down in this Act. [Section 132B(2)]

Section 132B(4)(a) of the Income Tax Act, 1961, refers to payment of simple interest on the aggregate amount of money seized under section 132 of the Act. In other words, where the money is seized by the Revenue, it would be obliged to pay interest thereon if the conditions laid down in section 132B are fulfilled but this provision is inapplicable to bullion or jewellery that is so seized. [Puran Mal and Sons and Another vs. Union of India and Others (2009) 313 ITR 347 (Del)].

Section 132B(4) provides that interest at the rate of 1/2% for every month or part of a month shall be paid by Central Government on the aggregate amount of—

(a) the money seized u/s 132 or requisition u/s 132A as reduced by the amount of money if any released under the above proviso; and

(b) the proceeds of assets sold towards the discharge of existing liability referred to section 132B(1)(i)

which exceeds the aggregate of the amount required to meet the liabilities (both existing and liability determined u/s 153A, including penalty and interest) referred to in section 132B(1)(i).

In other words, the interest will be computed on the following amount—

Amount of money seized under section 132 or requisitioned under section 132A	—
Add: Proceeds of assets sold towards the discharge of existing liabilities referred to in section 132(1)(i)	—
	—
Less: Money released under the first proviso to section 132B(1)(i)	—
Less: Aggregate of the amount required to meet the liability (both existing and liability under section 153A including penalty and interest) referred to in section 132B(1)(i)	—
Amount on which interest payable	—

This interest shall be payable from the expiry of the period of 120 days from the execution of the last of the authorizations for search till the date of completion of assessment under section 153A or block assessment.

For the removal of doubts, Explanation 2 to the section has been inserted by the Finance Act, 2013 so as to clarify that the existing liability does not include advance tax payable in accordance with the provisions of Part C of Chapter XVII.

Procedure for assessment of search cases [Sections 153A, 153B and 153C]

Section 153A(1)(b) provides that notwithstanding anything contained in section 139, section 147, section 148, section 149, section 151 and section 153, in the case of a person where a search is initiated under section 132 or books of account, other documents or any assets are requisitioned under section 132A after 31.5.2003, the Assessing Officer shall assess or reassess the total income of six assessment years immediately preceding the assessment year relevant to the previous year in which such search is conducted or requisition is made.

According to section 153A(1)(a) where a search is initiated u/s 132 or books of account, or other documents or any assets are requisitioned u/s 132A after 31.5.2003, the Assessing Officer shall issue notice to such person requiring him to furnish, within such period as may be specified in the notice, return of income in respect of six assessment years immediately preceding the assessment year relevant to the previous year in which the search was conducted u/s 132 or requisition was made u/s 132A.

Such return of income shall have to be furnished in the prescribed form and verified in the prescribed manner and setting forth such other particulars as may be prescribed. Further, in the case of such return, all the provision of the Act shall, as far as may be, apply accordingly as if such return were a return required to be furnished u/s 139.

Example: Suppose a search is conducted on 15.7.2014. The Assessing Officer shall issue notice to file return of income for six assessment years prior to assessment year 2015-16 (i.e. assessment year relevant to previous year 2014-15 in which search was conducted). Hence the return shall have to be furnished for assessment years 2009-10 to 2014-15.

Although the return u/s 153A has to be filed within the time specified in the notice but no time limit is prescribed for issue of such notice u/s 153A. Notice u/s 153A, can be issued at any time. Such time limit would however, be circumscribed by the limitation period for making an assessment u/s 153B.

Section 153A contemplates issue of notice for 6 years preceding the search but does not contemplate a notice for the year of search or requisition. Therefore, no return is required to be filed for the year of search under section 153A. Regular return for the year of search has to be filed as per the provisions of section 139.

As per proviso 1 to section 153A, the Assessing Officer shall assess or reassess the total income of each of such six assessment years.

Assessment or reassessment, if any, relating to any assessment year falling within the period of six assessment years pending on the date of initiation of the search under section 132 or requisition u/s 132A, as the case may be, shall abate. [Second proviso to section 153A]

The words mentioned here are assessment or reassessment pending on that date shall abate and as such the appeal or revision or rectification if pending on the date of initiation of search u/s 132 or requisition u/s 132A shall not abate.

Where on the date on which the search was initiated, the assessment proceeding was pending on the basis of return furnished by the petitioner and instead of complying with requirement of section 153A regarding issue of notice, the Assessing Officer proceeded with the pending assessment proceedings and passed an assessment order, it was held that entire action of Assessing Officer to proceed with assessment proceedings was a nullity. [Abhay Kumar Shroff vs. CIT (2007) 290 ITR 114 (Jharkhand)].

Issuance of notice under section 153A to file return of income for six assessment years is mandatory for the purpose of making an assessment. Though section 153A refers only to issue of notice, a valid assessment cannot be made unless there is a service of the notice under section 153A.

After the search, the total income of the assessee is to be recomputed on the basis of the undisclosed income unearthed during search and the same is to be added with regular income assessed under section 143(3) or computed under section 143(1) for each of the six preceding assessment years. Where any prepaid taxes are there, the same are required to be given credit for computing the further tax payable by the assessee. Thus, assessments or reassessments which were already completed shall not abate.

Save as otherwise provided in section 153A, section 153B and section 153C, all other provisions of this Act shall apply to the assessment or reassessment made under section 153A and as such the assessee shall be liable to pay tax and interest as per the provisions of section 140A at the time of filing the return under section 153A. He shall also be liable to penalty u/s 271(1)(c) for concealment of income, penalty for non-filing of return u/s 271F and interest under section 234A, 234B and prosecution u/s 276CC and all other provisions of the Act shall also apply in his case.

Since, the return furnished, pursuant to a notice issued u/s 153A, shall be deemed to be governed by the provisions of section 139, this would not only pre-suppose a right to fill a revised return but, it shall be incumbent upon the Assessing Officer to issue notice u/s 143(2) for framing the assessment under section 143(3) or 144 read with section 153A. The notice u/s 143(2) would have to be served within a period of 6 months from the end of the financial year in which the return is filed by the assessee in response to notice under section 153A.

In the assessment or reassessment made in respect of an assessment year under this section, the tax shall be chargeable at the rate or rates as applicable to such assessment year.

Return under section 153A shall be required to be furnished even if:—

(a) the assessee was not required to furnish the return of any assessment year as it was below taxable limit.

(b) return has already been filed under section 139/142(1) or 148.

(c) assessmen or reassessment of such assessment year have been already completed.

(d) assessment or reassessment for any of these years is pending.

No order of assessment or reassessment shall be passed by an Assessing Officer below the rank of Joint Commissioner in respect of each assessment year referred to in section 153A(1)(b) or the assessment year referred to in section 153B(1)(b), except with the prior approval of the Joint Commissioner. [Section 153D]

Section 153B provides the time limit for completion of assessment as follows:

(a) Time limit of completion of assessment of 6 assessment years [Section 153B(1)(a)]: The Assessing Officer shall make an order of assessment or reassessment in respect of each assessment year, falling within six assessment years under section 153A within a period of 24 months (36 months, in case a reference is made u/s 92CA(1) to TPO) from the end of the financial year in which the last of the authorisations for search u/s 132 or for requisition under section 132A was executed.

(b) Time limit of completion of assessment year relevant to the previous year in which search is conducted, or requisition is made [Section 153B(1)(b)]: This section also provides that the time-limit for completion of assessment in respect of the assessment year relevant to the previous year in which the search is conducted u/s 132 or requisition is made u/s 132A shall be a period of 24 months [36 months, in case a reference is made u/s 92CA(1) to TPO] from the end of the financial year in which the last of the authorisations for search u/s 132 or for requisition u/s 132A, as the case may be, was executed.

Although the return of income of the previous year in which search was conducted shall be filed as per the normal provisions but the assessment of assessment year relevant to such previous year shall have to be completed within 24 months [36 months, in case a reference is made u/s 92CA(1) to TPO] from the end of the financial year (not the assessment year) in which the search was conducted.

The authorisation of search u/s 132 is executed when the last panchnama is drawn up and in case of requisition u/s 132A, when the books of account or other documents or assets have been actually received by the Authorised Officer.

Time limit for assessment in a post-search case starts from the date of completion of the search, which is understood as the date of which the last panchnama was prepared. But where after this date, a carton found during the search was opened and an inventory was prepared, the date of preparation of such inventory cannot be understood as extending the search, so as to entail longer time limit for completion of the assessment. [CIT vs. Rajhans Aromatics (2011) 336 ITR 68 (Del)].

(c) Time limit for completion of assessment of other person referred to in section 153C [Proviso to section 153B(1)]: In case of such other person, the time limit for making assessment or reassessment of total income of the assessment years referred to in clause (a) i.e. block period of six assessment years and clause (b) i.e. assessment year of search of the said sub-section, shall be the either:

(i) 24 months [36 months, in case a reference is made u/s 92CA(1) to TPO] from the end of the financial year in which the last of authorisations for search u/s 132 or for requisition u/s 132A was executed; or

(ii) 12 months [24 months, in case a reference is made u/s 92CA(1) to TPO] from the end of the financial year in which books of account or documents or assets seized or requisitioned are handed over under section 153C to the Assessing Officer having jurisdiction over such other person,

whichever is later.

Example: Suppose a search was conducted in case of Aman on 25.7.2015 and was completed (executed) on 5.8.2015. Certain books of account, money, bullion, etc. were proved to belong to Asin which were handed to Assessing Officer of Asin on 28.1.2018. In this case, time limit for making assessment under section 153A in case of Aman and Asin shall be as under:

In case of Aman

(1) For assessment years 2010-11 to 2014-15 — The assessment or re-assessment will have to be completed under section 153A by 31.12.2017 (i.e. 21 months after the end of the financial year 2015-16 in which search was executed).

(2) For assessment year 2015-16 — The assessment or re-assessment will have to be completed u/s 153A by 31.03.2018 (i.e. 24 months after the end of the financial year 2015-16 in which search was executed.

(3) For assessment year 2016-17 — Regular assessment under section 143(3) or 144 will have to completed by 31.03.2018 (i.e. 24 months after the end of the relevant financial year in which search was executed).

In case of Asin

(1) For assessment 2010-11 to 2014-15 — The assessment or re-assessment shall have to be completed u/s 153A by 31.12.2017 or 31.12.2018 (i.e. 9 months from the end of the financial year in which books of account documents or assets seized were handed over to jurisdictional Assessing Officer under section 153C) whichever is later i.e. upto 31.12.2018.

(2) For assessment year 2015-16 — The assessment or re-assessment will have to be completed u/s153A by 31.03.2018 or 31.03.2019 (i.e. 12 months after from the end of the financial year in which books of account documents or assets seized were handed over to the jurisdiction Assessing Officer u/s153C) whichever is later i.e. 31.03.2019.

(3) For assessment year 2016-17 — assessment or reassessment u/s 153A will have to completed by 31.03.2018 or 31.03.2019 whichever is later i.e. it should be completed upto 31.03.2019.

However, in computing the period of limitation for the purposes of this section the following period shall be excluded:

(i) the time taken in reopening the whole or any part of the proceeding or in giving an opportunity to the assessee to be reheard under the proviso to section 129 relating to change of incumbent of an office, or

(ii) the period during which the assessment proceeding is stayed by an order or injunction of any court, or

(iii) the period commencing from the date on which the Assessing Officer directs the assessee to get his accounts audited u/s 142(2A) and ending with the last date on which the assessee is required to furnish a report of such audit under that sub-section, or

(iv) in a case where an application made before the Income Tax Settlement Commission u/s 245C is rejected by it or is not allowed to be proceeded with by it, the period commencing from the date on which such application is made and ending with the date on which the order u/s 245D(1) is received by the Commissioner, or

(v) the period commencing from the date on which an application is made before the Authority for Advance Ruling under section 245Q(1) and ending with the date on which the order rejecting the application is received by the Commissioner u/s 245R(3), or

(vi) the period commencing from the date on which an application is made before the Authority for Advance Rulings under section 245Q(1) and ending with the date on which the advance ruling pronounced by it is received by the Commissioner u/s 245R(7), or

(vii) the period commencing from the date of annulment of a proceeding or order of assessment or reassessment referred to in section 153A(2) till the date of the receipt of the order setting aside the order of such annulment, by the Commissioner, or

(viii) the period commencing from the date on which a reference for exchange of information is made by an authority competent under an agreement referred to in section 90 or section 90A and ending with the date on which the information so requested is received by the Principal Commissioner or Commissioner or a period of six months, whichever is less, or

(ix) the period commencing from the date on which a reference for declaration of an arrangement to be an impermissible avoidance arrangement is received by the Principal Commissioner or Commissioner under sub-section (1) of section 144BA and ending on the date on which a direction under sub-section (3) or sub-section (6) or an order under sub-section (5) of the said section is received by the Assessing Officer.

If, after the exclusion of the aforesaid period, the period of limitation available to the Assessing Officer for making an order of assessment or reassessment, as the case may be, is less than sixty days, such remaining period shall be extended to sixty days and the period of limitation shall be deemed to be extended accordingly.

Assessment of income of any other person [Section 153C]

(1) Notwithstanding anything contained in section 139, section 147, section 148, section 149, section 151 and section 153, where the Assessing Officer is satisfied that,—

(a) any money, bullion, jewellery or other valuable article or thing, seized or requisitioned, belongs to; or

(b) any books of account or documents, seized or requisitioned, pertains or pertain to, or any information contained therein, relates to,

a person other than the person referred to in section 153A, then, the books of account or documents or assets, seized or requisitioned shall be handed over to the Assessing Officer having jurisdiction over such other person and that Assessing Officer shall proceed against each such other person and issue notice and assess or reassess the income of the other person in accordance with the provisions of section 153A, if, that Assessing Officer is satisfied that the books of account or documents or assets seized or requisitioned have a bearing on the determination of the total income of such other person for the relevant assessment year or years referred to in sub-section (1) of section 153A.

Provided that in case of such other person, the reference to the date of initiation of the search under section 132 or making of requisition under section 132A in the second proviso to sub-section (1) of section 153A shall be construed as reference to the date of receiving the books of account or documents or assets seized or requisitioned by the Assessing Officer having jurisdiction over such other person.

Provided further that the Central Government may by rules made by it and published in the Official Gazette, specify the class or classes of cases in respect of such other person, in which the Assessing Officer shall not be required to issue notice for assessing or reassessing the total income for six assessment years immediately preceding the assessment year relevant to the previous year in which search is conducted or requisition is made except in cases where any assessment or reassessment has abated.

(2) Where books of account or documents or assets seized or requisitioned as referred to in sub-section (1) has or have been received by the Assessing Officer having jurisdiction over such other person after the due date for furnishing the return of income for the assessment year relevant to the previous year in which search is conducted under section 132 or requisition is made under section 132A and in respect of such assessment year—

(a) no return of income has been furnished by such other person and no notice under sub-section (1) of section 142 has been issued to him, or

(b) a return of income has been furnished by such other person but no notice under sub-section (2) of section 143 has been served and limitation of serving the notice under sub-section (2) of section 143 has expired, or

(c) assessment or reassessment, if any, has been made,

before the date of receiving the books of account or documents or assets seized or requisitioned by the Assessing Officer having jurisdiction over such other person, such Assessing Officer shall issue the notice and assess or reassess total income of such other person of such assessment year in the manner provided in section 153A.

Case Laws

(1) Notice u/s 153C can be issued only where the money, bullion, jewellery or other valuable article or thing or books of account or documents seized or requisitioned actually belong to assessee. Notice issued on the basis of loose papers which bear the name of assessee actually not belong to assessee was without jurisdiction. [Vijaybhai N. Chandrani vs. ACIT (2010) 38 DTR 225/231 CTR 474 (Guj)j.

(2) The provisions of sections 153A and 153C are constitutionally valid in as much as the deal with two categories of persons whose books of account assets, etc. have been seized or requisitioned though from different locations. Further, principles of natural justice are incorporated in section 153C as it provides for issuing a notice for the purpose of assessee his income. [Saraya Industries Ltd. vs. Union of India (2008) 171 Taxman 194 (Del)].

(3) For purpose of attracting section 153C, the document seized must not only be a 'speaking one', but also prima facie 'incriminating one'. The documents cannot be said "incriminating one", merely because it contains the noting of entries which are already recorded in books of accounts or is subjected to scrutiny of Assessing officer in the past in regular assessment u/s. 143(3) of the Act. [Sinhgad Technical Education Society vs. ACIT (Pune)(Trib)]

According to section 246A an appeal against the order of assessment or reassessment u/s 153A shall lie with the Commissioner of Income Tax (Appeals).

An appeal before the Tribunal [or even before the Commissioner (Appeal)] does not take within its fold, questions touching the validity of the search. It is only the assessment proceedings u/s 158BC (now section 153A) that can be challenged in appeal. The satisfaction of the conditions precedent for a search, detailed in section 132(1)(a), (b) or (c) are beyond the scope of assessment proceedings. The validity of search may be questioned only in writ proceedings. [M.B. Lai vs. CIT (2005) 279 ITR 298 (Del)].

The assessee in case of assessment of search and seizure cases shall be liable for penalty u/s 271(1)(c) for concealment of income—

(A) Explanation 5A to section 271: Explanation 5A shall be applicable where the due date of filing of return of income of the previous year to which the undisclosed income belongs has expired and the assessee has/has not filed the return of income of that previous year before the search is initiated.

Where in the course of a search initiated under section 132 on or after 1.6.2007, the assessee is found to be the owner of,—

(i) any money, bullion, jewellery or other valuable article or thing (hereinafter in this Explanation referred to as assets) and the assessee claims that such assets have been acquired by him by utilizing (wholly or in part) his income for any previous year; or

(ii) any income based on any entry in any books of account or other documents or transactions and he claims that such entry in the books of account or other documents or transactions represents his income (wholly or in part) for any previous year,

which has ended before the date of the search and the due date for filing the return of income for such year has expired and the assessee has not filed the return, then, notwithstanding that such income is declared by him in any return of income furnished on or after the date of the search, he shall, for the purposes of imposition of a penalty under section 271(1)(c) of this section, be deemed to have concealed the particulars of his income or furnished inaccurate particulars of such income.

Explanation 5A is also applicable for search initiated u/s 132 on or after 1.6.2007. It is not applicable for requisition of books of account under section 132A.

(B) Penalty under section 271AAA:

(a) Penalty @ 10% of the undisclosed income [Section 271AAA(1)]: The Assessing Officer may, notwithstanding anything contained in any other provisions of this Act, direct that, in a case where search has been initiated u/s 132 on or after 1.6.2007, the assessee shall pay by way of penalty, in addition to tax, if any, payable by him, a sum computed at the rate of 10% of the undisclosed income of the specified previous year.

(b) Penalty under section 271AAA shall not be levied in the following case [Section 271AAA(2)]: Where the assessee,--

(i) in the course of the search, in a statement u/s 132(4), admits the undisclosed income and specifies the manner in which such income has been derived;

(ii) substantiates the manner in which the undisclosed income was derived; and

(iii) pays the tax, together with interest, if any, in respect of the undisclosed income the penalty u/s 271AAA shall not be levied.

(c) Penalty under section 271(1)(c) shall not be levied in this case [Section 271AAA(3)]: No penalty under the provisions of section 271(1)(c) shall be imposed upto the assessee in respect of the undisclosed income referred to in section 271AAA(1).

The provisions of sections 274 and 275 shall, so far as may be, apply in relation to the penalty referred to in this section (i.e. section 271AAA).

Penalty under section 271AAA is applicable for search initiated u/s 132 on or after 1.6.2007. It is not applicable for requisition of books of account u/s 132A. In case of section 132A penalty shall be leviable u/s 271(1)(c).

Section 153A(2) provides that if any proceeding initiated or any order of assessment or reassessment made u/s 153A(1) has been annulled in appeal or any other legal proceeding, then, notwithstanding anything contained in section 153(1), the assessment or reassessment relating to any assessment year which has abated, shall stand revived with effect from the date of receipt of the order of such annulment by the Commissioner.

Further, as per section 153(4), if such assessment/reassessment, which was abated earlier, stands revived, the time limit for making such assessment/reassessment shall be-

(i) one year from the end of the month in which revival order is received by the CIT or

(ii) the time prescribed under section 153 or 153B

whichever is later.

However, such revival shall cease to have effect, if such order of annulment is set aside.

Example: Suppose search is conducted on 5.7.2015 and is completed on 15.7.2015.

In this case, assessment of assessment years 2010-11 to assessment year 2015-16 shall be made u/s 153A.

Suppose for assessment year 2011-12, the notice under section 148 was issued which was served on 3.4.2015 and the reassessment under section 147 of the same is pending on 5.7.2015.

Further, suppose for assessment year 2013-14, the assessment under section 143(3) is pending on 5.7.2015.

In the above cases, the assessment of assessment year 2011-12 and assessment year 2013-14 which were pending on 5.7.2015 shall abate *i.e.* come to end.

Let us assume the Assessing Officer made assessment/reassessment under section 153A for assessment years 2010-11 to 2015-16.

The assessee filed appeal against the said assessment orders made under section 153A.

Let us assume that ITAT on 15.10.2020, annulled the assessment/reassessment made u/s 153A for assessment years 2010-11 to 2015-16.

Since the assessment/reassessment orders passed under section 153A for the assessment year 2010-11 to assessment year 2015-16 were annulled, the reassessment of the assessment year 2011-12 which was abated shall stand revived on the receipt of order by CIT. Similarly, the assessment proceeding of assessment year 2013-14 abated earlier shall also stand revived.

The above assessments as per section 153(4) should be completed by Assessing Officer within one year from the end of month in which revival order is received by CIT.

However, if the High Court set aside the order of annulment, then revived proceeding of assessment year 2011-12 and assessment year 2013-14 shall cease to have effect as the assessment made under section 153A will become valid.

Procedure for assessment of search cases not applicable to survey cases

The procedure as laid down under section 153A-153C/158BC is to be followed in a case where any search has been conducted u/s 132 or where section 132A has been invoked to requisition books of account, documents or assets. This procedure will not apply to any case where no such action u/s 132 or 132A has been taken. Specifically in any case where a survey has been done under powers exercised u/s 133A, this procedure u/s 153A-153C/158BC is not applicable.

12.2 SURVEY

'Survey' contemplates a comprehensive and extensive view of the business activities of an assessee, subject to the limitations laid down in the Income Tax Act.

The survey is conducted by the Income Tax Department to achieve the following 3 objects:

(1) To bring those into tax net who have taxable income but are not filing returns of income.

(2) To do a surprise check whether books of accounts are maintained properly, regularly, and correctly.

(3) To call and to collect information during survey proceedings as may be relevant to the assessment/re-assessment.

The survey can be of two types:

(a) Specific survey of business premises [Section 133A(1) to (4)].

(b) Survey in connection with functions, etc. [Section 133A(5)]

Besides the above, another type of survey called door to door survey is also done under section 133B to collect certain information.

Specific survey to business premises [Section 133A (1) to (4)]

The survey of the business premises can be conducted by any Income Tax Authority.

According to Explanation (a) to section 133A Income Tax Authority means a Commissioner, a Joint Commissioner, a Director, a Joint Director, an Assistant Director or a Deputy Director or an Assessing Officer, or a Tax Recovery Officer, and for the purposes of *clause (i) of* sub-section (1), *clause (i) of* sub-section (3) and sub-section (5), includes an Inspector of Income Tax.

No action under section 133A(1) shall be taken by an Assistant Director or a Deputy Director or an Assessing Officer or a Tax Recovery Officer or an Inspector of Income Tax without obtaining the approval of the Joint Director or the Joint Commissioner, as the case may be.

The Inspector conducting survey even if so authorized by any such other authority specified under this section cannot exercise all the rights and powers conferred on higher authorities. His power is limited to the inspection of books of account or other documents as may be available at the place visited by him. He is entitled to place identification marks on the books of account or other documents inspected by him and is also entitled to make extracts there from. He, however, has no power to verify cash, stock or other valuables or articles. He neither has a right to issue summons to elicit any further information nor a right to record a statement. It is hence necessary to verify the identity card and the status of the official who has visited the premises. [Kamal & Co. vs. ACIT (1999) 104 Taxman (Mag) 79].

Material collected during illegal survey by inspector who was not authorized to verify the inventory, can be used by Assessing Officer for making additions. [CIT vs. Kamal & Co (2009) 308 ITR 129 (Raj)].

It may be clarified that if an inspector visits the premises as an assistant to or a subordinate of a higher authority who has accompanied him, he can certainly perform the verification of stock, cash and valuable articles or things as an assistant of the higher authority.

According to section 133A(1), Notwithstanding anything contained in any other provision of this Act, an Income Tax Authority may enter

(a) any place within the limits of the area assigned to him, or

(b) any place occupied by any person in respect of whom he exercises jurisdiction, or

(c) any place in respect of which he is authorised for the purposes of this section by such Income Tax Authority, who is assigned the area within which such place is situated or who exercises jurisdiction in respect of any person occupying such place,

at which a business or profession is carried on, whether such place be the principal place or not of such business or profession.

The Income Tax Authority who has entered the premises, where the business or profession is carried on, may require any proprietor, employee or any other person who may at that time and place be attending in any manner to, or helping in, the carrying on of such business or profession

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

(ii) to afford him the necessary facility to check or verify the cash, stock or other valuable article or thing which may be found therein, and

(iii) to furnish such information as he may require as to any matter which may be useful for, or relevant to, any proceeding under this Act.

For the purposes of this sub-section, a place where a business or procession is carried on shall also include any other place, whether any business or profession is carried on therein or not, in which the person carrying on the business or profession states that any of his books of account or other documents or any part of his cash or stock or other valuable article or thing relating to his business or profession are or is kept.

Section 133A(2) provides that an Income Tax Authority may enter:

(a) any place of business or profession referred to in section 133A(1) only during the hours at which such place is open for the conduct of business or profession and,

(b) any other place, only after sunrise and before sunset.

The object of survey is not the same as that of search or seizure u/s 132 of the Act. This section empowers the Income Tax Authority to enter only a place at which a business or profession is carried on by the assessee, he cannot enter the residential premises of the assessee or the premises of the lawyer or chartered accountant of the assessee. [Board Circular No. 7-D (LXIII 7) of 1967, dated 3.5.1967].

The entry into the business premises must be during business hours but survey operation can continued after business hours. [N.K. Mohnot vs. DCIT (1995) 215 ITR 275 (Mad) affirmed in (1999) 240 ITR 5621.]

As per sub-section (2A) Without prejudice to the provisions of sub-section (1), an income-tax authority acting under this sub-section may for the purpose of verifying that tax has been deducted or collected at source in accordance with the provisions under sub-heading B of Chapter XVII or under sub-heading BB of Chapter XVII, as the case may be, enter, after sunrise and before sunset, any office, or any other place where business or profession is carried on, within the limits of the area assigned to him, or any place in respect of which he is authorised for the purposes of this section by such income-tax authority who is assigned the area within which such place is situated, where books of account or documents are kept and require the deductor or the collector or any other person who may at that time and place be attending in any manner to such work,—

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

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

Section 133A(3) provides that an Income Tax Authority acting under this section may,

(a) if he so deems necessary, place marks of identification on the books of account or other documents inspected by him and make or cause to be made extracts or copies therefrom,

(b) retain in his custody any such books of account or other documents for a period exceeding fifteen days (exclusive of holidays) without obtaining the approval of the Principal Chief Commissioner or the Chief Commissioner or the Principal Director General or the Director General or the Principal Commissioner or the Commissioner or the Principal Director or the Director therefore, as the case may be.

  Provided that no action under clause (ia) or clause (ii) shall be taken by an income-tax authority acting under sub-section (2A).

(c) make an inventory of any cash, stock or other valuable article or thing checked or verified by him,

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

Case Laws:

(1) Whatever statement is recorded under section 133A is not given any evidentiary value obviously for the reason that the officer is not authorized to administer oath and to take any sworn statement which alone has evidentiary value as contemplated under law. [CIT vs. Khader Khan Son (2008) 300 ITR 157 (Mad)].

(2) Confession made during survey is not conclusive and can be retracted. [CIT vs. Dhingra Metal Works (Delhi High Court)]

(3) Confession made during survey cannot be the sole basis for making an addition, without considering the explanation of assessee. [Bubulal Gangwal, Jaipur vs. Addl. CIT (2010) Tax World December, 10 Vol. XLIV, Part-6, P. No. 222].

(4) Section 133A enables the Income Tax Authority only to record any statement of any person which may be useful but does not authorise for taking any sworn-in statement. On the other hand, such power to examine a person on oath is specifically conferred on the authorised officer only u/s 132(4) in the course of any search or seizure, Thus, the Act whenever it thought fit and necessary to confer such power to examine a person on oath, the same has been expressly provided whereas section 133A does not empower any ITO to examine any person on oath. In contradistinction to the power u/s 133A, section 132(4) enables the authorised officer to examine a person on oath and any statement made by such person during such examination can also be used in evidence under the Act. On the other hand, whatever statement recorded under section 133A is not given any evidentiary value obviously for the reason that the officer is authorised to administer oath and to take any sworn in statement which alone has the evidentiary value as contemplated in the law. [Paul Mathew & Sons vs. CIT (2003) 129 Taxman 416 (Ker)].

Section 133A(4) provides that an Income Tax Authority acting under this section shall, on no account, remove or cause to be removed from the place wherein he has entered, any cash, stock or other valuable article or thing.

Survey in connection with any function, etc. [Section 133A(5)]

Where, having regard to the nature and scale of expenditure incurred by an assessee, in connection with any function, ceremony or event, the Income Tax Authority is of the opinion that it is necessary or expedient so to do, he may, at any time after such function, ceremony or event, require the assessee by whom such expenditure has been incurred or any person who, in the opinion of the Income Tax Authority, is likely to possess information as respects the expenditure incurred, to furnish such information as he may require as to any matter which may be useful for, or relevant to, any proceeding under this Act and may have the statements of the assessee or any other person recorded and any statement so recorded may thereafter be used in evidence in any proceeding under this Act.

Consequences if facilities are not provided [Section 133A(6)]

According to section 133A(6) if a person under this section is required to afford facility to the Income Tax Authority to inspect books of account or other documents or to check or verify any cash, stock or other valuable article or thing or to furnish any information or to have his statement recorded either refuses or evades to do so, the Income Tax Authority shall have all the powers under section 131(1) for enforcing compliance with the requirement made.

Further, the visiting officer may approach the higher authority with a view to obtaining a proper warrant of authorisation to convert the survey action into a search and seizure action and the higher authority will be justified in issuing warrant of authorisation for a full scale raid action on the basis of first hand details and information given by the survey party.

As per section 292C where any books of account, other documents, money, bullion, jewellery or other valuable article or thing are or is found in the possession or control of any person in the course of a search under section 132 or survey under section 133A, it may, in any proceeding under this Act, be presumed--

(i) that such books of account, other documents, money, bullion, jewellery or other valuable article or thing belong or belongs to such person;

(ii) that the contents of such books of account and other documents are true; and

(iii) that the signature and every other part of such books of account and other documents which purport to be in the handwriting of any particular person or which may reasonably be assumed to have been signed by, or to be in the handwriting of, any particular person, are in that person's handwriting, and in the case of a document stamped, executed or attested, that it was duly stamped and executed or attested by the person by whom it purports to have been so executed or attested.

Where any books of account, other documents or assets have been delivered to the requisitioning officer in accordance with the provisions of section 132A, then, the above provisions shall apply as if such books of account, other documents or assets which had been taken into custody from the person referred to in section 132A(1)(a), (b) or (c), had been found in the possession or control of that person in the course of a search u/s 132.

The above presumption can be made for any proceeding under the Act relating to assessment of search conducted under section 132 or books of account and other document requisitioned under section 132A or survey conducted under section 133A.

Assessee disclosed an amount of ₹25 lakhs vide letter dated 11-2-2005, which was submitted after two months from the date of survey in the light of various documents and papers found at the time of survey. In the return of income, the said amount was not disclosed. The Assessing Officer rejected the book results and made addition of ₹25 lakhs. The Tribunal also confirmed the addition on the ground that it was not a case of the assessee that the assessee has wrongly understood the contents of the documents, burden on assessee to explain the contents of the documents as the assessee has not discharged the burden addition was justified. [Seasons Catering Services (P) Ltd. vs. Dy. CIT (2010) 127 ITD 50 (Del)]

Study Note - 13

CLUBBING OF INCOME

This Study Note includes

13.1 Clubbing of Income

13.1 CLUBBING OF INCOME

Certain provisions are included in the act as anti tax avoidance measures. Provisions for inclusion in assessee's income, income of some other person, which is not at arm's length, are a kind of such provisions. Such provisions arrest tax leakage likely to result from certain transactions with relatives or diversion of title without losing control over the same, etc.

ENCOMPASS OF CLUBBING PROVISIONS

1	Clubbing of income where control over assets or income is retained while title is transferred	Sections 60, 61, 64(1)(iv),(vi),(vii),(viii)
2	Clubbing of income of relatives under certain circumstances.	Sections 64(ii)
3	Clubbing of income of minor child	Section 64(1A)

TRANSFER OF ASSETS [Sec. 60]

Where any person transfers income without transferring the ownership of the asset, such income is taxable in the hands of the transferor. Such transfer may be revocable or irrevocable. The provision applies irrespective of the time when the transfer has been made i.e. it may be before or after the commencement of the Income-tax Act.

REVOCABLE TRANSFER OF ASSETS [Sec. 61]

Any income arising to any person by virtue of revocable transfer of assets is chargeable to tax as the income of transferor. For this purpose, transfer may include any settlement or agreement.

The transfer is said to be revocable if it contains any provision for the re-transfer of the whole or any part of the income or assets to the transferor or a right to re-assume power over the whole or any part of the income or assets.

If any settlement contains a clause for forfeiture of rights of beneficiaries under certain circumstances, the settlement will be regarded as revocable – CIT *vs.* Bhubaneshwar Kuer 53 ITR 195 (SC).

IRREVOCABLE TRANSFER OF ASSETS FOR SPECIFIED PERIOD [Sec. 62]

(1) The provisions of Section 61 shall not apply to any income arising to any person by virtue of a transfer—

   (i) by way of trust which is not revocable during the lifetime of the beneficiary, and, in the case of any other transfer, which is not revocable during the lifetime of the transferee ; or

   (ii) made before the 1st day of April, 1961, which is not revocable for a period exceeding six years.

   Provided that the transferor derives no direct or indirect benefit from such income in either case.

(2) Notwithstanding anything contained in Sub-section (1), all income arising to any person by virtue of any such transfer shall be chargeable to Income-tax as the income of the transferor as and when the power to revoke the transfer arises, and shall then be included in his total income.

TRANSFER AND REVOCABLE TRANSFER DEFINED UNDER SECTION 63

For the purposes of sections 60, 61 and 62 and of this section,—

(a) A transfer shall be deemed to be revocable if—

   (i) it contains any provision for the re-transfer directly or indirectly of the whole or any part of the income or assets to the transferor, or

   (ii) it, in any way, gives the transferor a right to re-assume power directly or indirectly over the whole or any part of the income or assets ;

(b) "Transfer" includes any settlement, trust, covenant, agreement or arrangement.

REMUNERATION OF SPOUSE [Sec. 64(1)(ii)]

An individual assessee is chargeable to tax in respect of any remuneration received by the spouse from a concern in which the individual has substantial interest. However, remuneration, which is solely attributable to technical or professional knowledge and experience of the spouse, will not be clubbed. Where both the spouses have a substantial interest in the concern and both are in receipt of the remuneration for such concern, such remuneration will be included in the total income of the husband or wife whose total income excluding such remuneration is greater.

The individual is deemed to have substantial interest, if the beneficiary holds equity share carrying not less than 20% voting power in the case of a company or is entitled to not less than 20% of the profits, in any other concern, not being a company at any time during the Previous Year.

The words technical or professional qualification occurring in the first part of the proviso of the section 64(1)(ii) of the Income Tax Act,1961, do not necessarily relate to technical or professional qualifications acquired by obtaining a certificate, diploma or a degree or in any other form from a recognized body like university or an institute. The intention of the legislature is clear from the use of the expression knowledge and experience in the latter part of the proviso, as otherwise it would have been permissible for the Legislature to use the same expression as occurring in the first part of the proviso to section 64(1)(ii). A harmonious construction of the two parts of the proviso shows that if a person possesses technical or professional knowledge and the income is solely attributable to the application of such technical or professional knowledge and experience, the requirements for the application of the proviso is satisfied, although the person concerned may not possess any qualification issued by a recognized body [Batta Kalyani vs. CIT (1985) 154 ITR 59 (AP)].

Where the spouse was drawing salary as nurse-cum-supervisor from a nursing home in which her husband was a partner, although she was B.Sc. in Bio-science but did not possess any professional or basic qualification as nurse from any recognized Institute, it was held that in view of the nature of employment of the spouse, a degree, a certificate or diploma in some cases may be insisted upon [CIT vs. Pratima Saha (Smt.) (1999) 239 ITR 570 (Gau)].

In CIT vs. Rajagopal (D.) (1985) 154 ITR 375 (Karn), the assessee was getting salary as managing director of a firm. His wife became a partner of that firm subsequently. It was found by the Tribunal that the assessee was only a graduate and did not possess any technical or professional qualification within the meaning of the proviso to section 64(1) (ii). It was held that the salary of the assessee was to be included in the hands of his wife who was a partner of that firm having substantial interest therein. But, in CIT vs. Sarabji Dorabji (1987) 168 ITR 598 (Ker), the Tribunal recorded a finding that the assessee-wife has acquired sufficient professional experience by virtue of her experience as a director for a large number of years. Such finding being one of the fact, was sufficient to hold that the salary received by the assessee-wife could not be included in the income of her husband by virtue of the provisions of Sec.64(1)(ii).

In CIT vs. Madhubala Shrenik Kumar (1990) 181 ITR 180 (MP), it was found by the Tribunal that the husband of the assessee had requisite experience as a salesman, that the firm, wherein the assessee-wife was a partner, was entirely dependent upon the salesmanship of the husband of the assessee as the firm had not employed any other salesman and that the amount of salary paid to the husband of the assessee by the firm was for his professional experience which was utilized by the firm in the conduct of the business of the firm. In view of these findings, it was held that the conditions requisite for the applicability of the proviso to section 64(1)(ii) are satisfied and the remuneration paid to the husband of the assessee could not be clubbed with the income of the assessee-wife.

Where the assessee (the wife) having previous experience as managing director as also requisite professional experience, is functioning as managing director of a company where her husband and the HUF to which she belonged were the majority shareholders, it was held that the case did not fall within the ambit of section 64(1)(ii). Remuneration was received by her by virtue of her professional experience and therefore, the same should be taxed in her hands separately. [Ashaben Rohitbhai vs. CIT (1999) 103 Taxman 296 (Guj)].

The Assessing Officer added salary paid to the wife out of husband's income from scooter agency as husband's income. It was held that such clubbing was not required since the wife held a degree in M.A. Economics [CIT vs. Major B.K.Kaul (2004) 136 Taxman 411(All)].

INCOME FROM ASSETS TO SPOUSE [Sec. 64(1)(iv)]

Where an asset (other than house property) is transferred by an individual to his or her spouse directly or indirectly otherwise than for adequate consideration or in connection with an agreement to live apart any income from such asset will be deemed to be the income of transferor.

However, this section is not applicable in the following cases—

(a) if assets are transferred before marriage.

(b) if assets are transferred for adequate consideration.

(c) if assets are transferred in connection with an agreement to live apart.

(d) if on the date of accrual of income, the transferee is not spouse of the transferor.

(e) if property is transferred by the Karta of HUF, gifting co-parcenary property to his wife.

(f) the property is acquired by the spouse out of the pin money (i.e., an allowance given to the wife by her husband for her dress and usual household expenses).

INCOME FROM ASSETS TRANSFERRED TO SON'S WIFE OR MINOR CHILD [Sec. 64(1)(vi)]

If an individual directly or indirectly transfers the assets after 1.6.73 without adequate consideration to son's wife or son's minor child (including son's minor step child or son's minor adopted child), income arising from such assets will be included in the total income of the transferor from the Assessment Year 1976-77 onwards.

INCOME FROM ASSETS TRANSFERRED TO A PERSON FOR THE BENEFIT OF SPOUSE OR MINOR CHILD [Sec. 64(1)(vii)]

Where an asset is transferred by individual, directly or indirectly, without adequate consideration to a person or persons for the immediate or deferred benefits of his or her spouse or minor child, income arising from the transferred assets will be included in the total income of the transferor to the extent of such benefit. If no income is accrued out of the property transferred by an individual, then nothing will be included in the income of the individual.

INCOME FROM ASSET TRANSFERRED TO A PERSON FOR THE BENEFIT OF SON'S WIFE [Sec. 64 (1)(viii)]

Where an asset is transferred by an individual, directly or indirectly, or after 1.6.73 without adequate consideration to a person or an Association of Persons for the immediate or deferred benefits of son's wife, income arising directly or indirectly from transferred asset will be included in the total income of the transferor to the extent of such benefit with effect from the Assessment Year 1985-86.

INCOME OF MINOR CHILD [Sec. 64(1A)]

In computing the total income of any individual, there shall be included all such income as arises or accrues to his minor child. However, income of the following types will not be included in the total income of the individual where income arises or accrues to the minor child on account of any—

(a) manual work done by him; or

(b) activity involving application of his skill, talent or specialised knowledge and experience.

Person in whose hands to be clubbed :

(i) 1st year : that parent whose income is higher. Subsequent years : the same parent – unless the AO is satisfied that it should be clubbed with the other parent.

(ii) Where marriage does not subsist, in the hands of the custodian parent.

However, a deduction — Upto ₹1,500 per minor child [Sec. 10(32)] shall be allowed against such income which is clubbed in the hands of the parent.

Where the minor child attains majority during the previous year, then the income till date he remained minor in that previous year shall be clubbed in the hands of the parent.

For the purpose of clubbing of minor's income, it is necessary that the amount to be clubbed must satisfy that it is income. Although, amongst the items included as income in section 2(24), agricultural income has not been specified but section 2(24) starts with the words 'income includes' which makes it clear that the definition of income in section 2(24) is not exhaustive. Hence, the fact that agricultural income has not been specified as one of items in section 2(24) does not mean that agricultural income is not included in the word income wherever the word 'income' has been used in the Act. Section 10 makes it clear that agricultural income is income but by express provision therein agricultural income has been excluded from total income of the assessee for the purpose of levy of income-tax.

Section 2 of the relevant Finance Act clearly provides that net agricultural income shall be taken into account in the manner provided therein for the purpose of determining the rate of income tax applicable to the income of the assessee. In view of this, agricultural income of the minor child of an assessee has to be taken into consideration for the purpose of determining that rate of tax that is applicable to his income *[Suresh Chand Talera vs. Union of India (2006) 282 ITR 341 (MP.)]*

CONVERSION OF SELF-ACQUIRED PROPERTY INTO JOINT FAMILY AND SUBSEQUENT PARTITION [Sec. 64(2)]

Where a member of a HUF has converted his self-acquired property into joint family property after 21.12.1969, income arising from the converted property will be dealt with as follows :-

(i) For the Assessment Year 1976-77 onwards, the entire income from the converted property is taxable as the income of the transferor.

(ii) If the converted property is subsequently partitioned amongst the members of the family, the income derived from such converted property, as is receivable by the spouse and minor child of the transferor will be taxable in his hands.

INCOME FROM THE ACCRETION TO ASSETS

In the above mentioned cases the income arising to the transferee from the property transferred, is taxable in the hands of the transferor. However, income arising to the transferee from the accretion of such property or from the accumulated income of such property is not includible in the total income of the transferor. Thus, if Mr. A transfers ₹ 60,000 to his wife without any adequate consideration and Mrs. A deposits the money in a bank, the interest received from the bank on such deposits is taxable in the hands of Mr. A. If, however, Mrs. A purchases shares in a company from the accumulated interest, the dividend received by Mrs. A, will be taxable in her hands and will not be clubbed with the income of Mr. A.

As per Explanation 3 to section 64, if the assets transferred directly or indirectly by an individual to his spouse or son's wife (i.e. 'the transferee') are invested by the transferee.

In any business (such investment being not in the nature of contribution of capital as a partner in a firm or, as the case may be, for being admitted to the benefits of the partnership in a firm), that part of the income arising out of the business to the transferee in any previous year, which bears the same proportion to the income of the transferee from the business as the value of the assets aforesaid as on the first day of the previous year bears to the total investment in the business by the transferee as on the said day shall be included in total income of the individual in that previous year.

Amount to be included in the total income can be calculated as under:-

Amount invested by transferee out of assets transferred = [(Income from Business x without adequate consideration as on the first day of the previous year) / Total investment by transferee as on the first day of the previous year]

CLUBBING OF NEGATIVE INCOME [EXPLANATION TO Sec. 64]

The income of a specified person is liable to be included in the total income of the individual in the circumstances mentioned earlier. For the purposes of including income of the specified person in the income of the individual, the word "income" includes a loss.

RECOVERY OF TAX U/S. 60 TO 64 [Sec. 65]

As per incomes belonging to Sec.s 60 to 64 to other persons are included in the total income of the assessee in such cases, by virtue of sec. 65, the actual recipient of income is liable, on the service of notice of demand, to pay the tax assessed in respect of income included in the income of other person (where the Income Tax Officer so desires).

ILLUSTRATIONS ON CLUBBING OF INCOME

Illustration 1.

Mrs.G holds 7% equity shares in B Ltd., where her married sister, Mrs. N also holds 14% equity shares. Mr.G is employed with B Ltd., without holding technical professional qualification. The particulars of their income for the Previous Year 2015-2016 are given as follows:

		Income of Mr G ₹	Income of Mrs G ₹
(i)	Gross Salary from B Ltd.	1,02,000	—
(ii)	Dividend from B Ltd.	—	6,000
(iii)	Income from House Property	90,000	—

Solution :

Computation of Total Income of Mr. G & Mrs. G for the A.Y. 2016-2017

Particulars	**Mr. G ₹**	**Mrs. G ₹**
Gross Salary	—	1,02,000
Taxable Salary to be included in the total income of Mrs G [Sec. 64(1)(ii)]		
Add: Income from House Property	90,000	—
Add: Income from Other Sources : Dividends to Mrs G, but exempt under Sec. 10(34)	—	Nil
Total Income	90,000	1,02,000

Note:

1. In the instant case, Mrs. G along with his sister, holds substantial interest in B Ltd. and Mr. G does not hold professional qualification. Accordingly, remuneration of Mr.G has been included in the total income of Mrs. G.
2. If the requisite conditions of clubbing are satisfied, clubbing provision will apply even if their application results into lower incidence of tax.

Illustration 2.

Mrs. C, a law graduate, is legal advisor of L Ltd. She gets salary of ₹ 1,80,000. Mr. C is holding 20% shares in L Ltd. His income from business, during the Previous Year 2015-2016 is ₹ 4,00,000. Compute their Total Income.

Solution :

Computation of Total Income of Mr. C & Mrs. C for the A.Y. 2016-2017

Particulars	**Mr. C ₹**	**Mrs. C ₹**
1. Gross salary	—	1,80,000
2. Business profits	4,00,000	—
Total Income	4,00,000	1,80,000

Note: Since Mrs. C holds professional qualification, salary income is assessable in her hands.

Illustration 3.

Mr. B holds 5% shares in A Ltd., where his brother and nephew hold 11% and 6% shares, respectively. Mrs. B gets commission of ₹ 1,00,000 from A Ltd. for canvassing orders. She holds no technical/professional qualification. Mr. B earns income of ₹ 5,00,000 from sugar business.

Compute their Total Income for the Assessment Year 2016-17.

Solution :

Computation of Total Income for the AY 2016-17

Particulars of income	**Mr. B (₹)**	**Mrs. B (₹)**
Income from sugar business	5,00,000	—
Commission for canvassing orders from A Ltd.	—	1,00,000
Total Income	5,00,000	1,00,000

Note: In the instant case, Mr. B holds 5% and his brother holds only 11% shares in A Ltd. The total of their shareholding is less than 20%. They have no substantial interest.

Therefore, commission income is assessable as income of Mrs. B.

Illustration 4.

The shareholding of Mr. K and Mrs. K in S Ltd, is given as follows:

(i)	Shareholding of K	7%
(ii)	Shareholding of Mrs. K	9%
(iii)	Shareholding of M, brother of K	8%
(iv)	Shareholding of F, father of Mrs. K	5%

Mr. K and Mrs. K are employed with S Ltd. None of them hold technical qualification. Mr. K gets salary @ ₹ 10,000 p.m and Mrs. K gets @ ₹ 12,000 p.m.

Income from Other Sources:	₹
Mr. K	80,000
Mrs. K	1,00,000

Compute total income for the Assessment Year 2016-2017

Solution :

Computation of Total Income for the AY 2016-17

Particulars	**Mr. K (₹)**	**Mrs. K ₹ (₹)**
1. Gross Salary	1,20,000	1,44,000
Salary income of Mr. K to be included in the total income of Mrs. K as her Income from Other Sources is greater and both of them have substantial interest along with their relative in S Ltd.		1,20,000
2. Income from Other Sources	80,000	1,00,000
Total Income	**80,000**	**3,64,000**

Illustration 5.

Mr. A gifts ₹ 4,00,000 to Mrs. A on 1st February 2016. Mrs. A starts crockery business and invests ₹ 1,00,000 from her account also. She earns profit of ₹ 60,000 during the period ended 31st March 2016. How would you tax the business profits?

Solution:

Proportionate profits, in proportion to the gifted amount from the spouse on the first day of the Previous Year bears to the total investment in the business on the first day of the Previous Year, will be taxable in the income of the transferor spouse.

As Mrs. A has started the new business, the first Previous Year will begin on the date of setting up and will end on 31st March, immediately following. Thus, the first Previous Year will consist a period of 2 months from 1st February 2016 to 31st March, 2016. Therefore, proportionate profit of ₹ 48,000, computed as below, will be included in the income of Mr. A:

$$\frac{4,00,000}{5,00,000} \times 60,000 = 48,000$$

Illustration 6.

Mr. A gifts ₹ 3,00,000 to Mrs. A on 1st February 2016. Mrs. A invests the same in the existing crockery business where she has already invested ₹ 5,00,000. Mrs. A earns ₹ 3,00,000 from the business during the year 2015-2016 ended on 31st March, 2016. How would you assess the profits?

Solution :

The Previous Year of the existing business is April to March. On the first day of the Previous Year (i.e. 1 April 2015), total investment has come from Mrs. A account. As the proportion of the gifted amount from spouse on 1 April 2015 to the total investment in business on the same day is **NIL**, the whole of the profits of ₹ 3,00,000 for the year 2015-2016 will be included in the total income of Mrs A.

From the Previous Year 2016-2017, 60% [i.e. 3,00,000/5,00,000 × 100] of the business profits will be included in the total income of Mr. A.

Illustration 7.

Mrs. Z is the owner of the business units A and B. A unit has been started with capital contribution from Mr. Z and B unit has been started out of capital contribution from Mrs. Z. The particulars of their income for the Previous Year 2015-2016 are as follows:

	Particulars	Mrs. Z	Mr. Z
(i)	Income from A unit	—	(–) 6,00,000
(ii)	Income from B unit	4,00,000	—
(iii)	Income from House Property	—	2,50,000

How would you assess them for the Assessment Year 2016-2017?

Solution :

(a) Mrs. Z is assessable on the profits from B unit. She cannot set-off the loss from A unit against the profits of B unit. Thus, she would be assessed on ₹ 4,00,000.

(b) The loss from A unit will be included in the total income of Mr Z in view of Sec. 64(1)(iv). "Income" includes "loss" also. Mr Z is entitled to set-off business loss of A's unit against Income from House Property. Thus, loss of ₹ 3,50,000 would be carried forward but could be set-off only against business profits.

Illustration 8.

Mr. Goutam, out of his own funds, had taken a FDR for ₹1,00,000 bearing interest @10% p.a. payable half-yearly in the name of his wife Latika. The interest earned for the year 2015-2016 of ₹ 10,000, was invested by Mrs. Latika in the business of packed spices which resulted in a net profit of ₹55,000 for the year ended 31st March, 2016. How shall the interest on FDR and income from business be taxed for the Assessment Year 2016-2017?

Solution:

Where an individual transfers an asset (excluding house property), directly or indirectly to his/her spouse, otherwise than for adequate consideration, or in connection with an agreement to live apart, income from such asset is included in the total income of such individual [Sec. 64(1)(iv)].

Accordingly, interest on FDR, accruing to wife, is included in the total income of her husband. However, business profits cannot be clubbed with total income of husband. Clubbing applies only to the income from assets transferred without adequate consideration. It does not apply to the income from accretion of the transferred assets. Hence, business profit is taxable as the income of wife.

Illustration 9. Sawant is a fashion designer having lucrative business. His wife is a model. Sawant pays her a monthly salary of ₹ 20,000. The Assessing Officer, while admitting that the salary is an admissible deduction, in computing the total income of Sawant, had applied the provisions of Sec. 64(1) and had clubbed the income (salary) of his wife in Sawant's hands.

Discuss the correctness of the action of the Assessing Officer.

Solution:

Where an individual has got substantial interest in a concern and his spouse derives any income from such concern by way of salary, commission, fees or by any other mode, such income is clubbed with the total income of such individual [Sec. 64(1)(ii)].

However, clubbing provision does not apply if the earning spouse holds technical or professional qualification and the income is solely attributable to the application of such knowledge and experience.

Salary earned by wife as model from the concern where her husband holds substantial interest is assessable as her income.

Illustration 10. Discuss whether the loss could be set-off in the following case:

Smt. Vatika carried on business with the gifted funds of her husband Mr. Dabbu. For the Previous Year ending 31.3.2016, Vatika incurred loss of ₹ 5 lakh which Dabbu wants to set-off from his taxable income.

Solution:

Funds for business were gifted by husband to wife. Accordingly, income from business should be clubbed with the income of husband [Sec. 64(1)(iv)].

"Income" includes "loss" also. Hence, husband is entitled to set-off the business loss of wife against his taxable income.

Illustration 11. Is Section 64(1)(vi) applicable, if one individual gifts assets to wife and children of his brother who similarly gifts to the wife and children of the former individual?

Solution: A mutual agreement between the two brothers is inferable, so that it could be treated as indirect transfer as one's own wife and children as decided by the Supreme Court in CIT vs. C.M.Kothari (1963) 49 ITR 107 (SC).

Illustration 12. An assessee in terms of a divorce decree was bound to maintain his minor child. He transfers money to a bank for this purpose. Is clubbing u/s 64 possible?

Solution: From the Assessment Year 1993-94, clubbing of the minor's income in the hands of the parent with the higher income is mandatory. Earlier, what could be clubbed in such parent's hands u/s 64 was only the income from an asset transferred by the parent. Where such transfer to a trust for the benefit of a minor child was consequent on the terms of a divorce decree, income from such transfer could not be treated as transfer by the parent to the child, so as to be covered by section 64 [CIT vs. Behram B. Dubash (2005) 279 ITR 377 (Bom.)]. The reasoning was that the trust was created as a result of legal obligation imposed by the court, so that it could not be treated as transfer within the meaning of section 64, which has to be understood as a voluntary one by the parent to his/her child. But this decision will have no application after provision for automatic aggregation.

Study Note - 14

SET OFF OR CARRY FORWARD AND SET OFF OF LOSSES

This Study Note includes

14.1 INTRODUCTION

If income is one side of the coin, loss is the other side. When a person earns income, he pays tax. However, when he sustains loss, law affords him to have benefit in the form of reducing the said loss from income earned during the subsequent years. Thus, tax liability is reduced at a later date, if loss is sustained. Certain provisions govern the process of carry forward and set off of loss.

This will be discussed on :

1. Set off of Loss in the Same Year
2. Carry forward and Set off of Loss in Subsequent Years
   (i) Basic Conditions for carry forward of loss.
   (ii) Conditions applicable to each Head of Income

As stated in Section 14 of the Act computation of total income is made under certain heads viz. (i) Salaries (ii) Income from House Property (iii) Profits and Gains of Business or Profession (iv) Capital Gains and (v) Income from Other Sources.

In case computation results in to a positive figure, it is "Income." Likewise, if the computation results into a negative figure, it is 'Loss". Therefore, there cannot be loss from the head 'Salary'. Loss can occur from all the remaining heads.

14.2 SET OFF OF LOSS IN THE SAME YEAR

For the purpose of computing total income and charging tax thereon, income from various sources is classified under the following heads :

A. Salaries
B. House Property
C. Profits and Gains of Business or Profession
D. Capital Gains
E. Other Sources

These five heads of income are mutually exclusive. If any income falls under one head, it cannot be considered under any other head. Income under each head has to be computed as per provisions under that head. Then, subject to provisions of Set off of Losses (Sec. 70 to Sec. 80) between the heads of income, the income under various heads has to be added to arrive at a Gross Total Income. From this Gross Total Income, deductions under Chapter VIA are to be allowed to arrive at the total income.

In this part, the provisions relating to set off, carry forward and set off of losses are categorised as under:

Set off of losses within the same head [Section 70]

Where the net result for any Assessment Year in respect of any source falling under any head of income is a loss, the assessee shall be entitled to have the amount of such loss set off against his income from any other source under the same head of income for the Assessment Year.

(1) Where the result of the computation made for any Assessment Year under sections 48 to 55 in respect of any short-term capital asset is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived at under a similar computation made for the Assessment Year in respect of any other capital asset.

(2) Where the result of the computation made for any Assessment Year under sections 48 to 55 in respect of any capital asset (other than a short-term capital asset) is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived at under a similar computation made for the Assessment Year in respect of any other capital asset not being a short-term capital asset.

(3) Where result of the computation made for the Assessment Year in respect of speculative business is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived under a similar computation made for the Assessment Year in respect of speculative business only.

(4) Where result of the computation made for the Assessment Year in respect of a specified business as per Section 35AD is a loss, the assessee shall be entitled to have the amount of such loss set off against the income, if any, as arrived under a similar computation made for the Assessment Year in respect of other specified business covered by Section 35AD.

(5) Where any loss made in the business of owning and maintaining race horses, the assessee shall not be entitled to have the amount of such loss set off against any income except income from the business of owning and maintaining race horses.

Set off of losses among different head of income [Section 71]

Where the net result of the computation under any head of income in respect of any Assessment Year is a loss, the assessee shall be entitled to have such amount of loss set off against his income assessable for that Assessment Year under any other head of income.

Exceptions to provisions of Sections 70 and 71 are as follows:

(a) **Loss from Speculation Business**: "Speculation transaction" means a transaction in which a contract for the purchase or sale of any commodity including stocks and shares is periodically or ultimately settled otherwise than by actual delivery or transfer of the commodity or scripts [Sec. 43(5)]. Loss from speculative transaction, if it is in the nature of business, can be set off only against income of another speculative business.

(b) **Loss under the head Long Term Capital Gains:** Long Term Capital Loss arising from transfer of long-term capital assets will be allowed to be set off only against Long Term Capital Gains.

Note:

1. Loss can be set off against deemed income.
2. Inter head adjustment is made only when the net income computed under a head is a loss.
3. The scheme of inter source and inter head adjustment is mandatory.
4. Indexed Long-term Capital Loss can be set off against Long-term Capital Gain without indexation [Vipul A Shah *vs.* Asst CIT(2011) 63DTR 272 (Mum)(Tri), Keshav S. Phansalkar *vs.* ITO(2009) 126 TTJ 892 (Mum): (2010) 3 ITR (Trib) 236 (Mum)]

(c) **Loss from owning and maintaining race horses:** Loss from owing and maintaining race horses can be set off only against income of that activity.

(d) **Loss from lottery, card games, races, etc:** No expenditure or allowance is allowed from wining from lotteries, crossword puzzles, card games etc. similarly, no loss from any lottery, card games, races, etc. is allowed to be set off from the income of such sources. [Sec. 58(4)]

(e) **Loss from exempt Income:** Loss incurred by an assessee from a source, income from which is exempt cannot be set off against income from a taxable source.

(f) **Loss from business specified in Section 35AD**: Any loss arising from specified business u/s 35AD, cannot be set off against any other income.

(g) **Loss from business**: Loss from business and profession including unabsorbed depreciation cannot be set off against Income from Salary.

10.3 CARRY FORWARD AND SET OFF OF LOSS IN SUBSEQUENT YEARS

Basic conditions for carry forward of loss

Section 80: loss returns

In order to carry forward loss under section 72, 73, 74 and 74A, return of income to be submitted within the due date as prescribed in Section 139(1). No loss which has not been determined in pursuance of a return filed within the date in accordance with the provisions of Section 139(3) shall be carried forward under the provisions of section.

The condition for filing of return in accordance with the provisions of Sec. 139(3) shall not apply to loss from House Property carried forward u/s. 71B and unabsorbed depreciation u/s. 32(2).

Brought forward loss of earlier Assessment Year in accordance with Sec.s 72, 73, 74, 74A can be set off against the income of that Assessment Year and can be carried forward further, even if the return is not filed within the due date specified in Section 139(1) of the Act.

CBDT has issued Circular vide No. 8 of 2001 dated 16.5.2001 clarifying that the power has been delegated to Commissioner to condone delay in filing return and carry forward losses in cases where the claim for loss does not exceed ₹ 10,000 for each Assessment Year and to Chief Commissioner/ Director General upto ₹ 1 lakh and beyond such limit CBDT will exercise the power.

Conditions applicable to each head

Sec. 71B: Carry forward and set off of loss from House Property

Where for any Assessment Year the net result of computation under the head "Income from House Property" is a loss to the assessee and such loss cannot be or is not wholly set off against income from any other head of income in accordance with the provisions of Section 71 so much of the loss as has not been so set-off or where he has no income under any other head, the whole loss shall, subject to the other provisions of this Chapter, be carried forward to the following Assessment Year and—

(i) be set off against the income from House Property assessable for that Assessment Year; and

(ii) the loss, if any, which has not been set off wholly, the amount of loss not so set off, shall be carried forward to the following Assessment Year, not being more than eight Assessment Years immediately succeeding the Assessment Year for which the loss was first computed.

Sec 72A: Carry forward and set off of accumulated loss in Scheme of Amalgamation or Demerger or Business Re- organization.

Where there has been an amalgamation of -

(a) a company owning an industrial undertaking or a ship or a hotel with another company; or

(b) a banking company referred to in Clause (c) of Section 5 of the Banking Regulation Act, 1949 (10 of 1949) with a specified bank; or

(c) one or more public sector company or companies engaged in the business of operation of aircraft with one or more public sector company or companies engaged in similar business.

Accumulated loss and the unabsorbed depreciation of such company shall be deemed to be the loss of such amalgamated company for the Previous Year in which the Scheme of Amalgamation was brought into force if the following conditions are satisfied:

1. The amalgamating company should have been engaged in the business for three years or more.
2. The amalgamating company should have continuously held at least three-fourths of the book value of fixed assets for at least two years prior to the date of amalgamation.
3. The amalgamated company will hold continuously for a period of five years at least three-fourths of the book value of the fixed assets of the amalgamated company acquired on amalgamation.
4. The amalgamated company will continue the business of the amalgamated company for a period of at least 5 years.
5. The amalgamated company, which has acquired an industrial undertaking of the amalgamated company by way of amalgamation, shall achieve the level of production of at least 50% of the installed capacity of the amalgamated industrial undertaking before the end of four years from the date of amalgamation and continue to maintain the minimum level of production till the end of five years from the date of amalgamation [this condition may be relaxed by Central Government on an application made by the amalgamated company].
6. The amalgamated company shall furnish a certificate in Form 62, duly verified by an accountant, to the Assessing Officer.

If any of the aforesaid conditions are not fulfilled, then the amount of brought forward business loss or unabsorbed depreciation so set off in any Previous Year in the hands of the Amalgamated Company will be deemed to be the income chargeable to tax, the hands of that Amalgamated Company, for the year in which such conditions are not fulfilled.

In case of Demerger, the amount of set off of the accumulated loss and unabsorbed depreciation, if any, allowable to the assessee being a resulting company shall be –

(i) the accumulated loss or unabsorbed depreciation of the demerged company if the whole of the amount of such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company; or

(ii) The amount which bears the same proportion to the accumulated loss or unabsorbed depreciation of the demerged company as the assets of the undertakings transferred to the resulting company bears to the assets of the demerged company if such accumulated loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company.

Unabsorbed loss can be carried forward for the unexpired period of out of total 8 years. Conditions specified in Section 72A are applicable to amalgamation only and not to demerger. However, the Central Government may, for the purposes of this section, by notification in the Official Gazette, specify such other conditions as it considers necessary to ensure that the demerger is for genuine business purposes.

In case of Business Re-organisation, set off of the accumulated loss and unabsorbed depreciation, if any, allowable to the assessee being the successor company for a period of 8 years commencing from the Previous Year of such business re-organisation.

Sec 72AA: Provision relating to carry forward and set off of accumulated loss and unabsorbed depreciation allowance in a scheme of amalgamation of banking company in certain cases

Notwithstanding anything contained in Section 72(2)(1B)(i) to (iii) where there has been an amalgamation of a banking company with any other banking institution under a scheme sanctioned and brought into force by the Central Government under Sec 45(7)of Banking Regulation Act , 1949 the accumulated loss and the unabsorbed depreciation of such banking company shall be deemed to be the loss or, as the case may be, allowance for depreciation of such banking institution for the Previous Year in which the scheme of amalgamation was brought into force and other provision of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly. In this case conditions u/s 2(1B) or 72A may or may not be satisfied.

For the purposes of this section :

(i) "Accumulated loss" means so much of the loss of the amalgamating banking company, under the head "Profits and Gains from Business" (not being a loss sustained in a speculation business) which such amalgamating banking company, would have been entitled to carry forward and set off under the provision of Section 72 if the amalgamation had not taken place;

(ii) "Banking company" shall have the same meaning as assigned to it in Sub-section (15) of Section 45(15) of the Banking Regulation Act, 1949.

(iii) "Banking institution" shall have the same meaning as assigned to it in Sub-section (15) of Section 45(15) of the Banking Regulation Act, 1949.

(iv) "Unabsorbed depreciation" means so much of the allowance for depreciation of the amalgamating banking company which remains to be allowed and which would have been allowed to such banking company if amalgamation had not taken place.

Reverse Merger

One may see that Sec. 72A is an exception of the general rule that the benefit of carry forward of loss and unabsorbed depreciation allowance is available to the same person who incurred the loss or suffered depreciation. However, one may also find that Sec. 72D is not available to him as the entity in which the loss is incurred does not qualify as an industrial undertaking or that some of the conditions of Sec. 72D are onerous to fulfil. Therefore, to get over these problems, the concept of reverse merger gained momentum. Under a normal merger, it is a sick industrial undertaking that is wound up and merged with a healthy undertaking. Under a reverse merger, a healthy company is merged with the sick company that has losses and unabsorbed depreciation allowances carried forward. Thus, the profits of the healthy company after amalgamation will be available for set off to the losses and unabsorbed depreciation allowances. The sick company that incurred the losses and suffered depreciation allowance will be the same person as the person who will carry them forward and adjust against the profits. Thus, Sec. 72D will not apply and the purpose of set off of losses and unabsorbed depreciation allowances will still be achieved. Based on facts in given cases the route merger of reverse merger will suit some companies.

Sec. 72AB: Provisions relating to carry forward and set off of accumulated loss and unabsorbed depreciation allowance in Business Re-organisation of Co-operative Banks

(1) The assessee, being a successor co-operative bank, shall, in a case where the amalgamationhas taken place during the Previous Year, be allowed to set off the accumulated loss and the unabsorbed depreciation, if any, of the predecessor co-operative bank as if the amalgamation had not taken place, and all the other provisions of this Act relating to set off and carry forward of loss and allowance for depreciation shall apply accordingly.

(2) The provisions of this section shall apply if—

(a) the predecessor co-operative bank—

(i) has been engaged in the business of banking for three or more years; and

(ii) has held at least three-fourths of the book value of fixed assets as on the date of the business re-organisation, continuously for two years prior to the date of business re-organisation;

(b) the successor co-operative bank—

(i) holds at least three-fourths of the book value of fixed assets of the predecessor co-operative bank acquired through business re-organisation, continuously for a minimum period of five years immediately succeeding the date of business re-organisation;

(ii) continues the business of the predecessor co-operative bank for a minimum period of five years from the date of business re-organisation; and

(iii) fulfils such other conditions as may be prescribed to ensure the revival of the business of the predecessor co-operative bank or to ensure that the business re-organisation is for genuine business purpose.

(3) The amount of set-off of the accumulated loss and unabsorbed depreciation, if any, allowable to the assessee being a resulting co-operative bank shall be,—

(i) the accumulated loss or unabsorbed depreciation of the demerged co-operative bank if the whole of the amount of such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting co-operative bank; or

(ii) the amount which bears the same proportion to the accumulated loss or unabsorbed depreciation of the demerged co-operative bank as the assets of the undertaking transferred to the resulting co-operative bank bears to the assets of the demerged co-operative bank if such accumulated loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting co-operative bank.

(4) The Central Government may, for the purposes of this section, by notification in the Official Gazette, specify such other conditions as it considers necessary, other than those prescribed under Sub-clause (*iii*) of Clause (*b*) of Sub-section (2), to ensure that the business re-organisation is for genuine business purposes.

(5) The period commencing from the beginning of the Previous Year and ending on the date immediately preceding the date of business re-organisation, and the period commencing from the date of such business re-organisation and ending with the Previous Year shall be deemed to be two different Previous Years for the purposes of set off and carry forward of loss and allowance for depreciation.

(6) In a case where the conditions specified in Sub-section (2) or notified under Sub-section (4) are not complied with, the set off of accumulated loss or unabsorbed depreciation allowed in any Previous Year to the successor co-operative bank shall be deemed to be the income of the successor co-operative bank chargeable to tax for the year in which the conditions are not complied with.

Section 73A: Set off of losses of the specified business (w.e.f A.Y. 2010-11)

With reference to newly inserted Section 35AD (w.e.f A.Y. 2010-11), any loss computed in respect of the specified business shall not be set off except against profits and gains, if any, of any other specified business. To the extent the loss is unabsorbed the same will be carried forward for set off against profits and gains from any specified business in the following Assessment Year and so on.

Section	**Losses**
71B	Brought forward loss from House Property
32(2)	Brought forward unabsorbed depreciation
72	Carried forward and set-off of business losses other than speculative business.
73	Losses in speculation business.
73A	Brought forward loss from Specified Business u/s 35AD
74	Losses under the head Capital Gains.
74A	Losses from owning and maintaining race horses.

Sec.	Nature of loss	Details of set off	Conditions / Exceptions
32(2)	Brought forward unabsorbed depreciation	Set off against any head of income	Unabsorbed depreciation loss can be carried forward for any number of years until it is fully set off.
71B	Brought forward loss from House Property	Set off only against income from House Property	Carry forward and set off is permissible for 8 Assessment Years immediately succeeding the Assessment Year for which such loss was computed
72	Brought forward unabsorbed business loss other than Speculation Loss	Set off only against income under the head Profits and Gains of Business or Profession.	1. Carry forward and set off is permissible for 8 Assessment Years immediately succeeding the Assessment Year for which the loss was computed. 2. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined and communicated u/s 157.
73	Brought forward unabsorbed Speculation Business Loss	Set off only against income under Speculation Business	1. Carry forward and set off is permissible for 4 Assessment Years immediately succeeding the Assessment Year for which the loss was computed. 2. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined and communicated u/s 157.
73A	Brought forward unabsorbed loss from Specified Business u/s 35AD	Set off only against income from any other Specified Business only	Carry forward for any number of years until it is fully set off
74	Brought forward unabsorbed loss under the head Capital Gains	Set off only against income under the head Capital Gain	1. Carry forward and set off is permissible for 8 Assessment Years immediately succeeding the Assessment Year for which the loss was computed. 2. STCL can be set off against any Capital Gain. However, LTCL can be set off only against LTCG. 3. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined and communicated u/s 157.
74A	Brought forward unabsorbed loss from activity of owning and maintaining race horses	Set off only against income from owning and maintaining race horses	1. Carry forward and set off is permissible for 4 Assessment Years immediately succeeding the Assessment Year for which the loss was computed. 2. Loss can be carried forward only if the return is filed u/s 139(1) and it is determined and communicated u/s 157.

Special provisions

Section 78(1) :

Where a change has occurred in the constitution of the firm, the firm shall not be entitled to carry forward and set off so much of the loss proportionate to the share of a retired or deceased partner remaining unabsorbed. This restriction shall not apply to unabsorbed depreciation.

Change in constitution of the firm for the purpose of this section takes place –

If one or more of the partners cease to be partners due to retirement or death of anyone or more partners, in such circumstances that one or more of the persons who were partners of the firm before the change, continue as partner or partners after the change (provided the firm is not dissolved on the death of any of its partners).

This section does not cover change in constitution of the firm due to change in the profit sharing ratio or admission of new partners.

Section 78(2) :

Section 78(2) provides that where any person carrying on business or profession has been succeeded in such capacity by another person otherwise than by inheritance, nothing, in relating to set-off and carry forward of loss, shall entitle any person other than the person incurring the loss to have it carried forward and set off against his income. In other words, the brought forward business losses can be set off only by the same assessee. The assessee, who has suffered the loss and in whose hands the loss has been assessed, is the person who can carry forward the loss and set-off the same against his business income of the subsequent year. The following are the exceptions:

(a) **Inheritance:** Where a business carried on by one person, is acquired by another person through inheritance. For example, A is carrying on a business and there are losses to the extent of ₹3,00,000 which can be carried forward and set-off against the income of the subsequent years. A dies and his son R inherits his business. The losses incurred by A can be set-off by his son R against the income from a business activity carried on by R. However such loss can be carried forward by the son for the balance number of years for which the father could have carried forward the loss. However, the unabsorbed depreciation cannot be carried forward by the legal heir as inheritance is not covered u/s 32(2).

    Where there is a succession by inheritance, the legal heirs (assessable as BOI) are entitled to set off the business loss of the predecessor. Such carry forward and set off is possible even if the legal heirs constitute themselves as a partnership firm. In such a case, the firm can carry forward and set-off the business loss of the predecessor.

    Where the legal heirs of the deceased proprietor enters into partnership and carries on the same business in the same premise under the same trade name, it was held that such loss of sole proprietary firm was allowed to be carried forward by the firm of the legal heirs who have succeeded to the business of the deceased [CIT vs. Madhu Kant M. Mehta (2001) 247 ITR 805 (SC.)]

(b) **Amalgamation:** Business losses and unabsorbed depreciation of an amalgamating company can be set-off against the income of the amalgamated company if the amalgamation is within the meaning of section 72A/72AA of the Income Tax Act. If the amalgamation is not in the nature specified in section 72A/72AA, the business loss and unabsorbed depreciation of the amalgamating company cannot be carried forward by the amalgamating company. Similarly, business losses and unabsorbed depreciation of an amalgamating co-operative bank can be set off against the income of successor co-operative bank i.e. the amalgamated co-operative bank, if the amalgamation is within the meaning of section 72AB.

(c) **Succession of proprietary concern or a firm by a company:** Where there has been reorganization of business whereby a proprietary concern or a firm is succeeded by a company and certain conditions mentioned in section 47(xiii) or (xiv) are fulfilled, the accumulated business loss and the unabsorbed depreciation of the predecessor firm/proprietary concern shall be deemed to be the loss or allowance for depreciation of the successor company for the previous year in which business reorganization was effected and carry forward provisions shall be applicable to the successor company.

(d) **Conversion of private company or unlisted company into Limited Liability Partnership:** Where there has been reorganization of business whereby a private company or unlisted public company is succeeded by a Limited Liability Partnership fulfilling the conditions laid down in the proviso to clause (xiiib) of section 47, then, notwithstanding anything contained in any other provision of this Act, the accumulated loss and the unabsorbed depreciation of the predecessor company, shall be deemed to be the loss or allowance for depreciation of the successor deemed to be the loss or allowance for depreciation of the Limited Liability Partnership for the purpose of the previous year in which business reorganization was effected and other provisions of this Act relating to set-off and carry forward of loss and allowance for depreciation shall apply accordingly.

(e) **Demerger:** Loss of the demerged company can be carried forward by the resulting company subject to the fulfillment of certain conditions, which the Central Government may for this purpose notifiy, to ensure that the demerger is for genuine business purposes.

In the following cases, business loss/ unabsorbed depreciation will not be allowed to be carried forward:

(1) Loss/unabsorbed depreciation of HUF cannot be carried forward by the members of HUF on the partition of HUF.

(2) Loss/unabsorbed depreciation of a firm succeeded by another firm cannot be carried forward as the assessee has changed.

(3) Loss/unabsorbed depreciation of sole proprietary concern taken over by the firm cannot be carried forward by the firm even if sole proprietor also becomes the partner of such firm.

(4) Loss/unabsorbed depreciation of a partnership firm taken over by one of the partner cannot be carried forward in the hands of such partner.

Where any person carrying on any Business or Profession has been succeeded in such capacity by another person otherwise than by inheritance, then the successor cannot have the loss of predecessor carried forward and set off against his income.

Section 79 :

Losses (other than unabsorbed depreciation) in case of closely held company:

In case of a company in which public are not substantially interested (defined in Sec. 2(18) of the Act), the unabsorbed business loss relating to any Assessment Year can be carried forward and set off against the income in a subsequent Assessment Year only if the shares of the company carrying not less than 51% of the voting power were beneficially held by the same persons both on the last day of the Previous Year(s) in which the loss claimed to be set off and on the last day of the Previous Year in which loss was incurred.

Exceptions:

The provisions stated supra shall not apply if

(a) the change in the voting power takes place due to the following reasons :

(i) the death of a shareholder; or

(ii) transfer of shares by way of gift to any relative of the shareholder making such gift.

(b) W.e.f. AY 2000-01, this section shall not apply to any change in the shareholding of an Indian company which is subsidiary of a foreign company arising as a result of amalgamation or demerger of a foreign company subject to the condition that 51% of the shareholders of the amalgamating or demerged foreign company continue to remain the shareholders of the amalgamated or the resulting foreign company.

Notes : Unabsorbed business losses can be carried forward and set off against profits from any business from A.Y. 2000-01. There is no need to continue the same business in which the loss was incurred.

For example:

FY	Shareholders and their holding of shares with voting power as at close of each year		Amount of business profit/loss	
2013-2014	Ali	11%	Profit	2,00,000
	Bony	19%		
	Cady	30%		
	Dany	40%		
2014-2015	Ali	5%	Loss	1,00,000
	Bony	29%		
	Cady	30%		
	Dany	36%		
2015-2016	Adi	5%	Profit	4,00,000
	Sony	19%		
	Rani	26%		
	Dany	50%		

In this case, the loss of financial year 2014-15 will not be set off against the profit of financial year 2015-16, since the persons, Bony and Cady, or Bony and Dany or Cady and Dany who hold between them as a pair 51% shares as at the end of financial year 2014-15 do not hold 51% shares at the end of financial year 2015-16.

Case Laws:

(1) Section 79 applies to all losses, including losses under the head capital gains. However, overriding provisions of section 79 do not affect the set off of unabsorbed depreciation which is governed by section 32(2) [CIT vs. Concord Industries Ltd (1979) 119 ITR 458 (Mad)].

(2) In section 79, the phrase "beneficially held" should be understood as a registered holder and the expression 'holder of share' denotes, in so far as the company is concerned, only a person who, as a shareholder, has his/her name entered on the register of members. Furthermore, a shareholder has been equated with only the registered shareholder and not the beneficial shareholder [Howrah Trading Co. Ltd vs. CIT (1959) 36 ITR 215 (SC)].

(3) The words "unconditionally" and "beneficially" indicate that the voting power arising from the holding of those shares should be free and not within the control of some other shareholder and registered holder should not be a nominee of another. The Court has also pointed out in Shree Chang Deo Sugar Mills Ltd vs. CIT (1961) 41 ITR 667 (SC) that by "unconditional" and "beneficial" holding it means that the shares are held by the holders for their own benefit only and without any control of another [Raghuvanshi Mills Ltd vs. CIT (1961) 41 ITR 613 (SC)].

(4) For the applicability of section 79, one has to see that 51% of the voting power, and not 51% of shares, is beneficially held during the year under reference by the persons who held such voting right during the year in which loss as incurred. Therefore, the Tribunal held that the board of directors of wholly owned subsidiary can be considered to be effectively controlled by its parent company and therefore, the parent company would be beneficial owner of its wholly-owned subsidiaries and step-down subsidiaries u/s 79 of the Income Tax Act,1961 [Amco Power Systems Ltd vs. ITO (2008) 123 TTJ 238 (Bang)].

(5) In view of the overriding provisions of Article 24(4) of the India-Germany Tax Treaty, disability on account of carried forward and set-off of accumulated losses due to change in shareholding pattern u/s 79 of the Act cannot be extended to Indian subsidiaries of German parent companies as long as the German parent companies are listed on a German Stock Exchange recognized under their domestic laws [Dalmier Chrysler India Pvt. Ltd vs. DCIT (2009) 29 SOT 202 (Pune)]

Order of Priority in carry forward and set-off of losses

Depreciation can be carried forward and set off against the profits from any business in the succeeding Assessment Year upto A.Y. 2001-02. The business in which the loss was incurred need not be continued in that year.

The effect of depreciation and business loss should be given in the following order:

- Current year's Depreciation
- Unabsorbed Business loss
- Unabsorbed Depreciation

A return of loss is required to be furnished for determining the carry forward of such losses, by the due date prescribed for different assesses under section 139(1) of the Act. (Sec. 80).

ILLUSTRATIONS ON SET-OFF AND CARRY FORWARD OF LOSSES

Illustration 1.

Following are the particulars of the income of Mr. Srikant for the Previous Year 2015-2016

Particulars	₹
1. Income from House Property	
(a) Property R	(+) 12,000
(b) Property J	(-) 20,000
2. Profits and Gains from Business:	
(A) Non-speculation:	
(i) Business X	40,000
(ii) Business Y	(-) 50,000
(B) Speculation:	
(i) Silver	40,000
(ii) Bullion	(-) 10,000
3. Capital Gains:	
(i) Long-term Capital Gains	(+) 30,000
(ii) Short-term Loss	(-) 10,000
4. Income from Other Sources:	
(i) Card games-loss	(-)10,000
(ii) From the activity of owing and maintaining race horses:	
(a) Loss at Mumbai	(-) 50,000
(b) Profit at Kolkata	(+) 40,000
(iii) Dividend from Indian companies	10,000
(iv) Income by letting out plant and machinery	1,11,000
The following losses have been carried forward:	
(i) Long-term Capital Loss from the Assessment Year 2010-2011	18,000
(ii) Loss from silver speculation from the Assessment Year 2012-2013 and which was discontinued in the Assessment Year 2013-2014	25,000

Compute the Gross Total Income for the Assessment Year 2016-2017.

Solution :

Computation of Gross Total Income for the Assessment Year 2016-2017

	Particulars	₹	₹
1.	Income from House Property (12,000 - 20,000)		(-) 8,000
2.	Profits from speculation:		
	(i) Profit from Silver Business	40,000	
	Less: Current year loss from bullion	(-) 10,000	
		30,000	
	Less: Carried forward silver speculative loss	(-) 25,000	
	Surplus from Speculation Business	5,000	
	(ii) Add: Business profit from X business	40,000	
	(iii) Less: Business loss from Y business	(-) 50,000	(-) 5,000
3.	Capital Gains:		
	Long-term Capital Gains	30,000	
	Less : Short-term Capital Loss	(-) 10,000	20,000
	Long-term Capital Gain	20,000	
4.	Income from Other Sources:		
	(i) Income by letting out plant and machinery		
	(ii) Card game-loss		1,11,000
	Neither it can be set-off nor it can be carried forward	(-) 10,000	
	(iii) Profit from race horses at Kolkata	(+)40,000	
	Less : Loss from race horses at Mumbai	(-) 50,000	
	Less : to be carried forward for next four Assessment Year	(-) 10,000	
	(iv) Dividend from Indian companies: Exempt under Sec. 10(34)		Nil
	Aggregated income after setting-off current year losses from house property, profit and business against income from other sources:		1,18,000
	Less : Carried forward Long-term Capital Loss, from the Assessment Year 2010-2011 to be set-off against Long-term Capital Gains		18,000
	Gross Total Income or total income as there is no deduction available from GTI		1,00,000

Unabsorbed business loss may be set-off against the income of any other head except 'salaries' and 'winnings from lottery, card games, crossword puzzle, betting on race horses', etc.

Illustration 2.

Mr. Dey furnishes the following particulars of his income for the Previous Year 2015-2016:

Particulars	₹
Unit "A": Business loss	(-) 4,00,000
Unabsorbed depreciation	(-) 2,00,000
Unit "B": Business profit	10,00,000
Income from House Property	2,00,000
Apart from the above mentioned, the following are unabsorbed	
Carried forward losses and allowance:	
Unit "C" business was discontinued on 31-12-2009:	
1. Business loss	(-) 3,00,000
2. Unabsorbed depreciation	(-) 2,00,000
These are occurred during the Previous Year 2009-2010	
Unit "D" business was discontinued on 1-3-2011:	
1. Business loss	(-) 3,00,000
2. Unabsorbed depreciation	(-) 1,00,000
These are occurred during the Previous Year 2010-2011	

Compute his total income for the Assessment Year 2016-17.

Solution :

Computation of Total Income for the AY 2016-2017

Particulars	₹	₹
Income from House Property		2,00,000
Business - Profession		
Profit of B Business	(+) 10,00,000	
Less: Business loss of A Business	(-) 4,00,000	
Depreciation of A Business	(-) 2,00,000	
	(+) 4,00,000	4,00,000
Aggregated Income		6,00,000
Less: Carried forward business loss:		
(i) Loss of C Business to be set-off against business profits	(-) 3,00,000	
(ii) Loss of D Business	(-) 3,00,000	(-) 6,00,000
Total Income		Nil

Note : Where business loss and depreciation both are being carried forward, business loss has got priority, over depreciation. Unabsorbed depreciation is carried forward without time-limit.

Illustration 3.

XYZ & Co., a partnership firm, submits the following particulars of its income and carry forward losses for the Previous Year 2015-2016:

Particulars	Betting on race horses made lawfully (₹)	Betting on race horses made illegally (₹)
1. Gross prize on race horses	15,00,000	5,00,000
2. Expenses incurred:		
(i) Horses purchased during the year	6,00,000	75,000
(ii) Medical expenses	1,00,000	20,000
(iii) Animal trainer fees	50,000	15,000
(iv) Fodder expenses	2,60,000	50,000
(v) Stable-rent/insurance	1,20,000	36,000
(vi) Depreciation in the value of horses	4,60,000	1,50,000
(vii) Staff salaries	1,00,000	40,000
3. Loses brought forward from the Assessment Year 2012-2013	6,00,000	2,00,000

Solution :

Computation of Total Income for the Assessment Year 2016-17

Particulars	Betting on race horses made lawfully (₹)	Betting on race horses made illegally (₹)
Gross prize	15,00,000	5,00,000
Less: Expenses incurred :		
(i) Horses purchased—not allowed	—	—
(ii) Medical expenses	(-) 1,00,000	(-) 20,000
(iii) Animal trainer fees	(-) 50,000	(-) 15,000
(iv) Fodder expense	(-) 2,60,000	(-) 50,000
(v) Stable rent/insurance	(-) 1,20,000	(-) 36,000
(vi) Staff salaries	(-) 1,00,000	(-) 40,000
(vii) Depreciation in the value of horses—not allowed	—	—
	8,70,000	**3,39,000**
Less: Brought forward loss	6,00,000	Nil
Total Income of the firm = ₹ 6,09,000	**2,70,000**	**3,39,000**

Note:

"Horse race" means a horse race upon which wagering or betting may be lawfully made [Explanation (b) to Sec. 74A]. Thus, where wagering or betting is not lawfully made on race horses, any loss incurred on such betting can neither be set off nor carried forward. Hence, the carried forward loss of ₹ 2,00,000 cannot be set-off.

Illustration 4.

Mr. N discloses the following incomes for the Previous Year 2015-2016 :

House Property	Business or Profession		Capital Gains		Income from Other Sources
₹	Speculation ₹	Non-speculation ₹	STCG ₹	LTCG ₹	
A 50,000	P 3,00,000	X 5,00,000	C 6,00,000	F 7,00,000	Family pension 95,000
B (-) 40,000	S (-)2,00,000	Y (-) 3,00,000	D (-) 3,00,000	E (-)5,00,000	Loss from (-) 50,000 letting out from machinery/plant

Determine income under head of income for the A. Y. 2016-2017

Solution :

Aggregation of income under each head of income: A. Y. 2016-2017

House Property	Business or Profession		Capital Gains		Income from Other Sources
₹	Speculation ₹	Non-speculation ₹	STCG ₹	LTCG ₹	₹
A 50,000	P 3,00,000	X 5,00,000	C 6,00,000	F 7,00,000	Family pension 95,000
B (-)40,000	S (-)2,00,000	Y (-)3,00,000	D (-)3,00,000	E (-)5,00,000	Loss from (-)50,000 letting out machinery/ plant
10,000	1,00,000	2,00,000	3,00,000	2,00,000	45,000

Illustration 5.

A discloses the following incomes from business or profession for the Previous Year 2015-2016:

		₹
(i)	Profit froxm X business	6,00,000
(ii)	Loss from Y business	(-) 2,00,000
(iii)	Loss from profession Z	(-) 2,50,000
(iv)	Profit from speculation business – M	2,00,000
(v)	Loss from speculation business – N	(-) 3,00,000

Determine the Income from Business or Profession for the Assessment Year 2016-2017.

Solution :

Income from Business or Profession for the AY 2016-2017

Particulars	₹
(i) X	6,00,000
(ii) Y	(-) 2,00,000
(iii) Z	(-) 2,50,000
Total Income from Non Speculation Business and Profession	1,50,000
Income from Speculation Business	
(i) M	2,00,000
(ii) N	(-)3 ,00,000
Loss from Speculation Business	(-) 1,00,000

Speculation loss cannot be set-off against the income from business profit, though both of them fall under the same head of income.

Thus, taxable business profits for the Assessment Year 2016-2017 is ₹ 1,50,000. The speculation loss will be carried forward for future set-off for 4 Assessment Years, immediately succeeding the Assessment Year for which it was first computed [Sec. 73(4)].

The time-limit of 4 years is applicable from the Assessment Year 2017-2018 and subsequent year.

Illustration 6.

D has earned income of ₹ 5,60,000 from speculation business during the PY 2015-2016. However, he has suffered losses in business and profession ₹ 3,20,000 and ₹ 1,70,000, respectively during the same period. Determine his income from business profession for the Assessment Year 2016-2017.

Solution :

Income from Business and Profession for the AY 2016-2017 :

Particulars	₹
Profits from Speculation Business	5,60,000
Less. (i) Loss from Non Speculation Business	(-) 3,20,000
(ii) Loss from Profession	(-) 1,70,000
Income from Business and Profession	70,000

Illustration 7.

Mr. Samir submits the following information for the A.Y. 2016-17.

Particulars	₹
Taxable Income from Salary	1,64,000
Income from House property :	
House 1 Income	37,000
House 2 loss	(53,000)
Textile Business (discontinued on 10.10.2015)	(20,000)
Brought forward loss of textile business - A.Y. 2012-13	(80,000)
Chemical Business (discontinued on 15.3.2015)	
– b/f loss of Previous Year 2012-13	(25,000)
– unabsorbed depreciation of Previous Year 2012-13	(15,000)
– Bad debts earlier deducted recovered in July ’2015	40,000
Leather Business	62,000
Interest on securities held as stock in trade	10,000

Determine the Gross Total Income for the Assessment Year 2016-17 and also compute the amount of loss that can be carried forward to the subsequent years.

Solution :

Computation of Gross Total Income A.Y. 2016-17

Particulars		₹	₹
I. Income from Salary			1,64,000
II. Income from House property :			
House 1 Income		37,000	
House 2 Loss		(53,000)	(16,000)
III. Profits and Gains of Business or Profession :			
(i) Textile business loss		(20,000)	
(iii) Chemical business – Bad debts recovered taxable u/s 41(4)	40,000		
Less : (i) Set off of brought forward loss of P.Y. 2012-13 u/s. 72	(25,000)	15,000	
		(5,000)	
(iii) Leather Business Income	62,000		
(iv) Interest on securities held as stock-in-trade	10,000	72,000	
		67,000	
Less: B/f business loss ₹ 80,000 restricted to		67,000	Nil
Gross Total Income			**1,48,000**

Note :

1. The unabsorbed loss of ₹ 13,000 (80,000-67,000) of Textile business can be carried forward to A.Y. 2017-18 for set-off u/s. 72, even though the business is discontinued.
2. The unabsorbed depreciation of ₹ 15,000 is eligible for set-off against any income other than salary income. Since, Gross Total Income contains the balance of Income from Salary only, unabsorbed depreciation cannot be adjusted, and hence, carried forward for adjustment in the subsequent years.

Illustration 8.

An assessee has filed a belated return showing a business loss. What is the remedy available to him for carry forward and set off of the said loss? OR,

AG Ltd. filed its return of loss for the Assessment Year 2016-2017 on 10.01.2017 beyond the time prescribed u/s 139(3) declaring a total loss of ₹ 12,00,000. It approaches you for your advice regarding the course of action to be taken to secure the benefit of carry forward of the business loss for set off against future profits. Advise the company suitably.

Solution :

A. **CBDT's Powers:** CBDT has the powers to condone the delay in filing return in cases having claim of carry forward of losses. **[Associated Electro Ceramics vs. CBDT 201 ITR 501 (Kar.)]**

B. **Monetary limits** prescribed for the condonation of delay are as under – **[Cir. No. 8/2001 dt. 16.5.2001]**

Refund claimed	**Authority empowered to condone**
Upto ₹ 10,000	Assessing Officer with the prior approval of the CIT
₹ 10,001 - ₹ 1,00,000	Assessing Officer with the prior approval of the CCIT / DGIT
₹ 1,00,001 and above	Central Board of Direct Taxes

C. **Analysis and conclusion:** Here, since the loss of AG Ltd. is ₹ 12,00,000, the authority empowered to condone the delay is CBDT. Hence, AG Ltd. has to file a condonation petition to the CBDT to carry forward the business loss.

Illustration 9.

Will Long Term Capital Loss from transfer of equity shares which have been sold through recognized stock exchange on which securities transaction has been paid be allowed to the set-off from any other Long Term Capital Gain?

Solution:

Loss incurred by an assessee from a source, income from which is exempt, cannot be set-off against income from a taxable source [CIT vs. Thyagarajan (S.S.) (1981) 129 ITR 115 (Mad.)]

Since, Long Term Capital Gain from the transfer of equity shares which have been sold through recognized stock exchange on which securities transaction has been paid is exempt u/s 10(38), therefore Long Term Capital Loss from such transfer shall not be allowed to be set-off.

Illustration 10.

Can business loss be set-off against income from undisclosed sources?

Solution:

The Madras High Court in the case of CIT vs. Chensing Ventures (2007) 291 ITR 258 (Mad) held that once the loss is determined, the same should be set-off against the income determined under any other head of income. The loss can therefore be set-off even against income from undisclosed sources.

Illustration 11.

The business of Sia Ltd, an industrial undertaking was discontinued on 25th September, 2012 due to fire and the company had incurred the following business losses:

(i) Loss for Assessment Year 2013-14 ₹4,00,000

(ii) Brought forward business loss of Assessment Years 2009-10 to 2012-13 ₹6,00,000

The above business is re-established on 25th December, 2015. What will be the treatment of the losses if the profit of assessment year 2016-17 is ₹5,00,000?

Solution:

Since the business is re-established within three years from the end of the previous year in which it was discontinued due to fire, the loss of ₹10,00,000 can be set off against ₹5,00,000 i.e. the income of the year in which it was re-established. The balance loss of ₹5,00,000 can be carried forward for seven succeeding Assessment Years.

Illustration 12.

A, B & C are three partners of firm sharing profit and loss equally. B retires from the firm on 30.9.2015. From the following information furnished to you for the financial year ended 31st March, 2016, compute loss and depreciation which the firm shall be allowed to carry forward.

	₹
Current Year business loss before allowing current year depreciation	3,00,000
Current year depreciation	2,10,000
Brought forward business loss of assessment year 2015-16	1,20,000
Brought forward unabsorbed depreciation of assessment year 2015-16	90,000

Solution:

	₹
Proportionate share of loss of partner 'B' in the current year (3,00,000 x 1/3 x 6/12)	50,000
Proportionate share of brought forward business loss (1,20,000 x 1/3 x 6/12)	20,000
Loss not allowed to be carried forward in the hands of firm	70,000

Loss and depreciation allowed to be carried in the hands of firm

	₹
Business loss of assessment year 2016-17 before depreciation	3,00,000
Less: Share of loss of 'B' the retiring partner of assessment year 2016-17	50,000
Business loss allowed to be carried forward (A)	2,50,000
Brought forward business loss of assessment year 2015-16	1,20,000
Less: Share of loss of 'B' the retiring partner	20,000
Business loss of assessment year 2015-16 allowed to be carried forward (B)	1,00,000
Total unabsorbed depreciation to be carried forward by firm (A+B)	3,50,000

Depreciation allowed to be carried forward

	₹
Current Year Depreciation	2,10,000
Add : Brought forward unabsorbed depreciation of assessment year 2015-16	90,000
Total unabsorbed depreciation to be carried forward by firm	3,00,000

Illustration 13.

A, B, & C are the partners of a firm sharing profits and losses in the ratio 2:2:1 respectively. The firm has brought forward business loss of ₹2,00,000 and unabsorbed depreciation of ₹1,80,000.

During the previous year 2015-16, B retired from the firm w.e.f. 1st July, 2015. Compute the business loss which will not be allowed to be carried forward in the hands of firm if –

(a) The firm has earned business income of ₹3,00,000 during the previous year 2015-16.

(b) The firm has incurred business loss of ₹3,00,000 during the previous year 2015-16.

Solution:

(a) Where the firm earned business income of ₹3,00,000

Share of loss of partner B in the brought forward business loss = ₹2,00,000 x 2/5 = ₹80,000

Share of profit of partner B in the business income of the previous year 2015-16 i.e. for 3 months = ₹3,00,000 x 2/5 x 3/12 = ₹30,000

Hence, loss which cannot be carried forward in the hands of the firm = ₹80,000 - ₹30,000 = ₹50,000.

Business loss which can be carried forward and set-off brought forward loss = ₹2,00,000 – ₹50,000 (share of loss of partner B) = ₹1,50,000

Hence, in the previous year 2015-16, the firm shall be allowed to set-off of brought forward loss of ₹1,50,000 (instead of ₹2,00,000) from the current business income of ₹3,00,000.

However, entire unabsorbed depreciation of ₹1,80,000 can be set off from the balance income of ₹1,50,000 (= ₹3,00,000 – ₹1,50,000).

(b) The firm has incurred business loss of ₹3,00,000 during the previous year 2015-16.

Share of loss of partner B in the brought forward loss = (₹2,00,000 x 2/5) = ₹80,000.

Share of loss of partner B in the current year business loss for 3 months = ₹3,00,000 x 2/5 x 3/12 = ₹30,000.

Aggregate loss which cannot be carried forward ₹1,10,000 (₹80,000 + ₹30,000).

Loss which can be carried forward to subsequent assessment year = (₹2,00,000 + ₹3,00,000)-₹1,10,000 = ₹5,00,000 - ₹1,10,000 = ₹3,90,000.

However, entire unabsorbed depreciation of ₹1,80,000 shall be allowed to be carried forward.

Study Note - 15

DEDUCTION IN COMPUTING TOTAL INCOME

This Study Note includes

11.1 INTRODUCTION

In order to further the Government Policy of attracting investment and activity in the desired direction and to provide stimulus to growth or to meet social objectives, concession in the form of 'deduction' from Taxable Income is allowed. Chapter VI-A of the Income-tax Act, 1961 contains such deduction provisions.

With the advent of new philosophy of giving direct assistance to the desired goal and avoiding indirect route of tax concessions, the numbers of deductions are being omitted. This is also with a view to avoid complexity of tax law.

In computing Total Income of an assessee deductions under sections 80CCC to 80U are permissible from "Gross Total Income". [Section 80A (1)]

Deduction not to be allowed unless return furnished [Sec. 80AC]

Where in computing the Total Income of an assessee of the Previous Year relevant to the Assessment Year commencing on the 1st day of April, 2006 or any subsequent Assessment Year, any deduction is admissible under Section 80-IA or Section 80-IAB or Section 80-IB or Section 80-IC or Section 80-ID or Section 80-IE, no such deduction shall be allowed to him unless he furnishes a return of his income for such Assessment Year on or before the due date specified under sub-section (1) of section 139.

"Gross Total Income" means the aggregate of income computed under each head as per provisions of the Act, after giving effect to the provisions for clubbing of incomes (Sections 60 to 64) and set off of losses and but before making any deductions under this chapter. [Section 80B(5)]

The deductions under Chapter VIA are not available from the following incomes though these are included in the "Gross Total Income":

(i) Long Term Capital Gains;

(ii) Winnings from lotteries, cross word puzzles etc.;

(iii) Incomes referred to in Sections 115A to AD, 115BBA and 115D.

The aggregate amount of deductions under Chapter VIA [Sections 80CCC to 80U] shall not exceed the "Gross Total Income" of the assessee. [Section 80A (2)]

11.2 DEDUCTIONS FROM GROSS TOTAL INCOME

Deductions under Chapter VIA

I	II	III
In respect of expenditure or investments made by assessee [Sec 80C to Sec 80 GGA]	In respect of certain income [Section 80HH to 80 RRB]	Other Deductions [Section 80U]

DEDUCTION IN RESPECT OF LIP, CONTRIBUTIONS TO PF, ETC [SEC. 80C]:

1	Eligible Assessee	Individual and HUF
2	Condition	Investment or application of funds during the Previous Year
3	Maximum Deduction	₹ 1,50,000 in a Previous Year
4	Special Provisions	Withdrawal of deductions for certain premature exit from certain investments or application of funds

Rate of deduction [Section 80C(1)]

This deduction shall be admissible only to an assessee, being an Individual or a Hindu Undivided Family. The amount of deduction shall be actual amount paid or deposited during the Previous Year in prescribed saving schemes [to be calculated] as qualifying amount for deduction u/s 80C or ₹ 1,50,000 whichever is less.

Qualifying Amount For Deduction u/s 80C

Any sums paid or deposited in the previous year by the assessee:

(i) to effect or to keep in force an insurance on the life of persons specified in sub-section (4);

Note: Insurance premium on the life of an insured / premium payer, spouse and any children is allowable as deduction within the overall limit of ₹ 1,50,000. However, if the premium payable for any year is more than 20% of the actual sum assured, the excess amount does not qualify for any deduction.

With effect from the Assessment Year 2013-14, if the premium payable for any year is more than 10% of the actual sum assured, the excess amount does not qualify for any deduction.

According to Finance Act, 2013, if the policy, issued on or after 01.04.2013, is for insurance on life of any person, who is —

(a) a person with disability or a person with severe disability as referred in Section 80U, or

(b) suffering from discase or aliment as specified in the rules made u/s 80DDB,

the premium payable for any year should not be in excess of 15% of the actual sum assured.

The revised / amended provision is as follows :

1. The above provisions shall be applicable in case of policies issued on or after 1st April 2012.

2. In respect of the old policies, the earlier provision of 20% ceiling shall be applicable

3. Actual sum assured in relation to any life insurance policy shall mean the minimum amount assured under that policy on the happening of the insured event at any time during the term of the policy, not taking into account-

   (a) the value of any premiums agreed to be returned, or

   (b) any benefit by way of bonus or otherwise over and above the sum actually assured, which is to be or may be received under the policy by any person.

(ii) to effect or to keep in force a contract for a deferred annuity, not being an annuity plan referred to in Clause (*xii*), on the life of persons specified in sub-section (4)

Provided that such contract does not contain a provision for the exercise by the insured of an option to receive a cash payment in lieu of the payment of the annuity;

(iii) by way of deduction from the salary payable by or on behalf of the Government to any individual being a sum deducted in accordance with the conditions of his service, for the purpose of securing him a deferred annuity or making provision for his spouse or children, in so far as the sum so deducted does not exceed one-fifth of the salary;

(iv) as a contribution by an individual to any provident fund to which the Provident Funds Act, 1925 applies;

(v) as a contribution to any provident fund set up by the Central Government and notified by it in this behalf in the Official Gazette, where such contribution is to an account standing in the name of any person specified in sub-Section (4);

(vi) as a contribution by an employee to a recognised provident fund;

(vii) as a contribution by an employee to an approved superannuation fund;

(viii) as subscription, in the name of any person specified in sub-section (4), to any such security of the Central Government or any such deposit scheme as that Government may, by notification in the Official Gazette, specify in this behalf;

Tax benefits under section 80C for the girl child under the Sukanya Samriddhi Account Scheme [Section 80C] [W.r.e.f. A.Y. 2015-16]

The Act has formulized the above benefits envisaged in the Sukanya Samriddhi Account scheme by making the following amendments in the Income Tax Act:

(1) **Deduction under section 80C:** As per section 80C(2), subscription made to Sukanya Samriddhi Account scheme by the individual in the name of any of the following persons referred to in section 80C(4)(ba) shall be eligible for deduction under section 80C:

   (i) individual, or

   (ii) any girl child of that individual, or

   (iii) any girl child for whom such person is the legal guardian, if the scheme so specifies.

(2) Withdrawal from the Sukanya Samriddhi Account shall be exempt under section 10(11A).

(3) The interest accruing on deposits in such account will be exempt from income tax.

The Scheme has been notified under section 80C(2)(viii) vide Notification number 9/2015 S.O.210(E), F. No. 178/3/2015-ITA-I dated 21.01.2015.

(ix) as subscription to any such savings certificate as defined in clause (c) of Section 2 of the Government Savings Certificates Act, 1959 (46 of 1959), as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(x) as a contribution, in the name of any person specified in sub-section (4), for participation in the Unit-linked Insurance Plan, 1971 (hereafter in this Section referred to as the Unit-linked Insurance Plan) specified in Schedule II of the Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2002 (58 of 2002);

(xi) as a contribution in the name of any person specified in sub-section (4) for participation in any such unit-linked insurance plan of the LIC Mutual Fund *referred to in* clause (*23D*) of Section 10, as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(xii) to effect or to keep in force a contract for such annuity plan of the Life Insurance Corporation or any other insurer as the Central Government may, by notification in the Official Gazette, specify;

(xiii) as subscription to any units of any Mutual Fund referred to in clause (*23D*) of Section 10 or from the Administrator or the specified company under any plan formulated in accordance with such scheme as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(xiv) as a contribution by an individual to any pension fund set up by any Mutual Fund referred to in clause (*23D*) of Section 10 or by the Administrator or the specified company, as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(xv) as subscription to any such deposit scheme of, or as a contribution to any such pension fund set up by, the National Housing Bank established under Section 3 of the National Housing Bank Act, 1987 (53 of 1987) (hereafter in this Section referred to as the National Housing Bank), as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(xvi) as subscription to any such deposit scheme of—

(a) a public sector company which is engaged in providing long-term finance for construction or purchase of houses in India for residential purposes; or

(b) any authority constituted in India by or under any law enacted either for the purpose of dealing with and satisfying the need for housing accommodation or for the purpose of planning, development or improvement of cities, towns and villages, or for both, as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(xvii) as tuition fees (excluding any payment towards any development fees or donation or payment of similar nature), whether at the time of admission or thereafter,—

(a) to any university, college, school or other educational institution situated within India;

(b) for the purpose of full-time education of any of the persons specified in sub-section (4);

(xviii) for the purposes of purchase or construction of a residential house property the income from which is chargeable to tax under the head "Income from House Property" (or which would, if it had not been used for the assessee's own residence, have been chargeable to tax under that head), where such payments are made towards or by way of—

(a) any installment or part payment of the amount due under any self-financing or other scheme of any development authority, housing board or other authority engaged in the construction and sale of house property on ownership basis; or

(b) any installment or part payment of the amount due to any company or co-operative society of which the assessee is a shareholder or member towards the cost of the house property allotted to him; or

(c) repayment of the amount borrowed by the assessee from—

(1) the Central Government or any State Government, or

(2) any bank, including a co-operative bank, or

(3) the Life Insurance Corporation, or

(4) the National Housing Bank, or

(5) any public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes which is eligible for deduction under clause (*viii*) of sub-section (1) of Section 36, or

(6) any company in which the public are substantially interested or any co-operative society, where such company or co-operative society is engaged in the business of financing the construction of houses, or

(7) the assessee's employer where such employer is an authority or a board or a corporation or any other body established or constituted under a Central or State Act, or

(8) the assessee's employer where such employer is a public company or a public sector company or a university established by law or a college affiliated to such university or a local authority or a co-operative society; or

(d) stamp duty, registration fee and other expenses for the purpose of transfer of such house property to the assessee, but shall not include any payment towards or by way of—

(A) the admission fee, cost of share and initial deposit which a shareholder of a company or a member of a co-operative society has to pay for becoming such shareholder or member; or

(B) the cost of any addition or alteration to, or renovation or repair of, the house property which is carried out after the issue of the completion certificate in respect of the house property by the authority competent to issue such certificate or after the house property or any part thereof has either been occupied by the assessee or any other person on his behalf or been let out; or

(C) any expenditure in respect of which deduction is allowable under the provisions of Section 24;

(xix) as subscription to equity shares or debentures forming part of any eligible issue of capital approved by the Board on an application made by a public company or as subscription to any eligible issue of capital by any public financial institution in the prescribed form;

Explanation — For the purposes of this clause,—

(i) "eligible issue of capital" means an issue made by a public company formed and registered in India or a public financial institution and the entire proceeds of the issue are utilised wholly and exclusively for the purposes of any business referred to in sub-Section (4) of Section 80-IA;

(ii) "public company" shall have the same meaning assigned to it in Section 3 of the Companies Act, 1956 (Corresponding Section 2 (20), 2(67), 2(68), & 2(71) of Companies Act, 2013);

(iii) "public financial institution" shall have the same meaning assigned to it in Section 4A of the Companies Act, 1956(Corresponding Section 2(72) of Companies Act, 2013);

(xx) as subscription to any units of any mutual fund referred to in clause (*23D*) of Section 10 and approved by the Board on an application made by such mutual fund in the prescribed form;

(xxi) *as term deposit—*

(a) for a fixed period of not less than five years with a scheduled bank; and

(b) which is in accordance with a scheme framed and notified, by the Central Government, in the Official Gazette for the purposes of this clause.

(xxii) as subscription to such bonds issued by the National Bank for Agriculture and Rural Development, as the Central Government may, by notification in the Official Gazette, specify in this behalf;

(xxiii) deposit in an account under the Senior Citizens Savings Scheme Rules,2004;

(xxiv) deposit in an account under the Post Office Time Deposit Rules,1981 for a period of five years;

Taxability of Amount Received

1. In following cases the assessee shall have to pay tax on any amount received on:

   (i) Termination of his contract of insurance referred to at point (i) above by notice to that effect or where the contract ceases to be in force by reason of failure to pay any premium, by not reviving contract of insurance :

      (a) in case of any single premium policy, within two years after the date of commencement of insurance; or

      (b) in any other case, before premiums have been paid for two years; or

   (ii) Termination of his participation in any unit-linked insurance plan referred to above in point (x) and (xi) by notice to that effect or where he ceases to participate by reason of failure to pay any contribution, by not reviving his participation, before contributions in respect of such participation have been paid for five years; or

   (iii) Transfer of the house property before the expiry of five years from the end of financial years in which possession of such property is obtained by him, or receives back, whether by way of refund or otherwise, any sum specified in that clause, then :

      (a) no deduction shall be allowed to the assessee under 80C(1) with reference to any of the sums referred to in point (i), (x), (xi) and (xviii), paid in such Previous Year; and

      (b) the aggregate amount of the deductions of income so allowed in respect of the Previous Year or years shall be deemed to be the income of the assessee of such Previous Year and shall be liable to tax in the Assessment Year relevant to such Previous Year.

DEDUCTION IN RESPECT OF CONTRIBUTION TO PENSION FUND OF LIC OR ANY OTHER PENSION FUND [SEC. 80CCC]

1	Eligible Assessee	Individual
2	Condition	Investment or application of funds during the Previous Year
3	Maximum Deduction	₹ 1,50,000 in a Previous Year
4	Special Provisions	Withdrawal of deductions for certain premature exit from certain investments or application of funds

Deduction of a maximum amount of ₹ 1,50,000 is allowed to an individual assessee for the amount paid or deposited by the assessee during Previous Year to effect or keep in force a contract for annuity plan of LIC or any other insurer for receiving pension from the fund referred to in Sec. 10(23AAB). The whole of the amount received by an assessee or his nominee shall be taxable in the year in which the amount is so received. It may be mentioned that where deduction is claimed in respect of any amount paid or deposited, under this Section, no rebate u/s. 88 shall be allowed with reference to the same amount. However, any payment in commutation of pension received from the fund referred to in Section 10(23AAB) is exempt u/s.10(10A)(iii).

Where any amount paid or deposited by the assessee has been taken into account for the purposes of this Section :

(a) a rebate with reference to such amount shall not be allowed under Sec. 88 for any Assessment Year ending before the 1st day of April, 2006;

(b) a deduction with reference to such amount shall not be allowed under Section 80C for any Assessment Year beginning on or after the 1st day of April, 2006.

IN RESPECT OF CONTRIBUTION TO PENSION SCHEME OF CENTRAL GOVERNMENT [SEC. 80CCD]

1	Eligible Assessee	Individual
2	Condition	Investment or application of funds during the Previous Year
3	Maximum Deduction	Up to 10% of his salary or gross total Income subject to maximum of ₹ 1,50,000 u/s 80CCD(i)
4	Special Provisions	Withdrawal of deductions for certain premature exit from certain investments or application of funds

Following sub-section (1B) shall be inserted after sub-section (1A) [as so omitted w.e.f. 1-4-2016] of section 80CCD by the Finance Act, 2015, w.e.f. 1-4-2016 :

(1B) An assessee referred to in sub-section (1), shall be allowed a deduction in computation of his total income, whether or not any deduction is allowed under sub-section (1) to the extent of

(a) of the whole of the amount paid or deposited in the previous year in his account under a pension scheme notified or as may be notified by the Central Government,

(b) ₹ 50,000

Whichever is less.

Provided that no deduction under this sub-section shall be allowed in respect of the amount on which a deduction has been claimed and allowed under sub-section (1).

Where any amount paid or deposited by the assessee has been allowed as a deduction under sub-Section (1) or sub-Section (1B).

(a) No rebate with reference to such amount shall be allowed under Section 88 for any Assessment Year ending before the 1st day of April, 2006;

(b) No deduction with reference to such amount shall be allowed under Section 80C for any Assessment Year beginning on or after the 1st day of April, 2006.

Tax benefits for New Pension System - extended also to "any employee or self-employed", and tax treatment of savings under this system as "exempt-exempt-taxed" [Section 10(44), 115-0,197A and 80CCD W.r.e.f. A.Y. 2009-10]

New Pension System has been extended to employee as well as self- employed Individual .

Further, in the case of an employee of Central Government or of any other employer, the deduction of employees' contribution shall be limited to 10% of his salary. Whereas in the case self-employed persons, it shall be limited to 10% of his Gross Total Income in the Previous Year.

For the purposes of the said Section the assessee shall be deemed not to have received any amount in the Previous Year if such amount is used for purchasing an annuity plan in the same Previous Year.

RESTRICTION ON THE OVERALL LIMIT OF DEDUCTION [SEC. 80CCE]

The aggregate amount of deductions under Sec. 80C, Sec. 80CCC and Sec. 80CCD shall not, in any case, exceed ₹1,50,000.

DEDUCTION IN RESPECT OF SUBSCRIPTION TO LONG-TERM INFRASTRUCTURE BONDS [SEC. 80CCF]

1	Eligible Assessee	Individual and HUF
2	Condition	Subscription paid or deposited in notified long-term infrastructure bonds
3	Maximum Deduction	₹ 20,000.

However, this Section is discontinued from the Assessment Year 2013-14

DEDUCTION IN RESPECT OF INVESTMENT MADE UNDER AN EQUITY SAVINGS SCHEME [SEC. 80CCG] [W.E.F. A.Y. 2013-14]

1	Eligible Assessee	Individual who is resident in India has, in a Previous Year, acquired listed equity shares or invested in listed units of an equity oriented fund in accordance with a scheme, as may be notified by the Central Government in this behalf
2	Conditions	(i) The Gross Total Income of the assessee for the relevant Assessment Year *should not exceed* ₹ 12,00,000 (ii) The assessee is a *new retail investor* as may be specified under the scheme notified in this behalf; (iii) The investment is made in such listed equity shares or Listed units of equity oriented fund as may be specified under the notified scheme; (iv) The investment is locked-in for a period of three years from the date of acquisition in accordance with the notified scheme; and (v) Such other condition as may be prescribed.
3	Maximum Deduction	The assessee shall be allowed a deduction, in the computation of his Total Income of the Assessment Year relevant to such Previous Year to the extent of - (a) 50% of the amount invested in such equity shares (b) ₹ 25,000 Whichever is less.

If any amount of deduction is claimed by any assessee in any year, the assessee would not be allowed to any other deduction under this section.

If any assessee after claiming the deduction fails to satisfy any of the conditions, the deduction originally allowed, shall be deemed to be income of the assessee of that year in which the condition so violated.

DEDUCTION IN RESPECT OF MEDICAL INSURANCE PREMIUM [SEC.80D]

1	Eligible Assessee	Individual and HUF
2	Condition	Investment or application of funds during the Previous Year by any mode of payment other than cash
3	Maximum Deduction	Up to ₹ 25,000. If they medical insurance premium is paid for senior citizen, then maximum deduction is up to ₹ 30,000

Essential conditions for claiming deduction under this section: Deduction is permissible, under this section, only to an individual or HUF.

Where the assessee is an individual, the sum referred to in sub-section (1) shall be the aggregate of the following, namely:—

(a) the whole of the amount paid to effect or to keep in force an insurance on the health of the assessee or his family or any contribution made to the Central Government Health Scheme or such other scheme as may be notified by the Central Government in this behalf or any payment made on account of preventive health check-up of the assessee or his family as does not exceed in the aggregate ₹ 25,000; **and**

(b) the whole of the amount paid to effect or to keep in force an insurance on the health of the parent or parents of the assessee or any payment made on account of preventive health check-up of the parent or parents of the assessee as does not exceed in the aggregate ₹25,000.

However, where the amounts referred to in clauses (a) and (b) above are paid on account of preventive health check-up, the deduction for such amount shall be allowed to the extent it does not exceed in the aggregate ₹ 5,000.

Following clauses (c) and (d) shall be inserted after clause (b) of sub-section (2) of section 80D by the Finance Act, 2015, w.e.f. 1-4-2016.

Deduction on account of medical expenditure incurred (instead of sum paid to effect any insurance of the health) to be allowed in case of very senior citizen;

(c) the whole of the amount paid on account of medical expenditure incurred on the health of the assessee or any member of his family as does not exceed in the aggregate ₹ 30,000; **and**

(d) the whole of the amount paid on account of medical expenditure incurred on the health of any parent of the assessee, as does not exceed in the aggregate ₹ 30,000:

Provided that the amount referred to in clause (c) or clause (d) is paid in respect of a very senior citizen and no amount has been paid to effect or to keep in force an insurance on the health of such person.

Provided further that the aggregate of the sum specified under clause (a) and clause (c) or the aggregate of the sum specified under clause (b) and clause (d) shall not ₹ 30,000.

Explanation.—For the purposes of clause (a), "family" means the spouse and dependant children of the assessee.

Where the amounts referred to in clauses (a) and (b) of sub-section (2) are paid on account of preventive health check-up, the deduction for such amounts shall be allowed to the extent it does not exceed in the aggregate five thousand rupees.

For the purposes of deduction under sub-section (1), the payment shall be made by—

(i) any mode, including cash, in respect of any sum paid on account of preventive health check-up;

(ii) any mode other than cash in all other cases not falling under clause (i).

Following sub-section (3) shall be substituted for the existing sub-section (3) of section 80D by the Finance Act, 2015, w.e.f. 1-4-2016 :

Where the assessee is a Hindu undivided family, the sum referred to in sub-section (1), shall be the aggregate of the following, namely:—

(a) whole of the amount paid to effect or to keep in force an insurance on the health of any member of that Hindu undivided family as does not exceed in the aggregate ₹ 25,000; and

(b) the whole of the amount paid on account of medical expenditure incurred on the health of any member of the Hindu undivided family as does not exceed in the aggregate ₹30,000.

Provided that the amount referred to in clause (b) is paid in respect of a very senior citizen and no amount has been paid to effect or to keep in force an insurance on the health of such person.

Provided further that the aggregate of the sum specified under clause (a) and clause (b) shall not exceed ₹ 30,000.

Additional deduction of ₹ 5,000: Where the sum specified in the above para of quantum of deduction is paid to effect or keep in force an insurance on the health of any person specified therein, and who is a senior citizen, an additional deduction of ₹ 5,000 shall be allowed.

DEDUCTION IN RESPECT OF MEDICAL TREATMENT OF HANDICAPPED DEPENDENT [SEC. 80DD]

Section 80DD of the Income Tax Act provides for a deduction to an individual or HUF, who is a resident in India, in respect of the following:

(a) Expenditure for the medical treatment (including nursing), training and rehabilitation of a dependant, being a person with disability; and

(b) Amount paid to LIC or other insurance in respect of a scheme for the maintenance of a disabled dependant.

1	Eligible Assessee	Individual and HUF
2	Condition	Expenditure for medical treatment during the Previous Year
3	Maximum Deduction	₹75,000, but where dependent is a person with severe disability, maximum deduction is ₹ 1,25,000.

If the handicapped dependent predeceases the individual or the member of HUF in whose name money has been deposited or paid, an amount equal to the amount paid or deposited under the scheme shall be deemed to be the income of the assessee of the Previous Year in which sum amount is received by the assessee and chargeable to tax in that Previous Year.

For the purpose of this Section dependent means a person who is not dependent for the suspect or main term on any person other than the assessee.

DEDUCTION IN RESPECT OF MEDICAL TREATMENT, ETC. [SEC. 80DDB]

1	Eligible Assessee	Individual and HUF
2	Condition	The amount should be actually paid for the medical treatment of specified disease
3	Maximum Deduction	Actual or ₹ 40,000 whichever is less but if the amount paid is for senior citizen (aged 60 years or more) then the ceiling limit is ₹ 60,000 and if the person for whom such expenditure is incurred happens to be a very senior citizen, the maximum deduction shall be allowed for a sum of ₹ 80,000.
4	Special Provisions	The assessee is required to furnish with the return of income, a certificate is prescribed Form No. 10-I

Deduction is allowed to a resident individual or Hindu Undivided Family in respect of expenditure actually incurred during the P.Y., for the medical treatment of specified disease or ailment as specified in the Rules 11DD for himself or a dependent relative or a member of an HUF.

Conditions :

(i) The assessee has to furnish a certificate in Form 10 – I from any doctor registered with Indian Medical Association with postgraduate qualifications.

(ii) "Dependent" means a person who is dependent for his support or maintenance on the assessee and on no other person.

A deduction of ₹ 40,000 is allowed as reduced by the amount received, if any, from an insurer or reimbursed by an employer for the medical treatment of such person.

Specified diseases and ailments under Section 80DDB and Rule 11DD –

(i) Neurological Diseases i.e.

- (a) Dementia;
- (b) Dystonia Musculorum Deformans
- (c) Motor Neuron Disease;
- (d) Atanxia;
- (e) Chorea;
- (f) Hemiballismus
- (g) Aphasia
- (h) Parkinsons Desease

(ii) Cancer

(iii) AIDS

(iv) Chronic Renal Failure

(v) Hemophilia

(vi) Thalassalmia

Note: Age for Senior Citizen ≥ 60 year and age for very Senior Citizen ≥ 80 years.

DEDUCTION IN RESPECT OF INTEREST ON LOAN TAKEN FOR HIGHER EDUCATION [SEC. 80E]

1	Eligible Assessee	Individual
2	Condition	The amount is paid by the assessee out of his income as interest on loan taken for higher education.
3	Maximum Deduction	100% of the interest paid on loan taken without any monetary ceiling limit.
4	Special Provisions	The assessee can claim the amount of interest in the initial Assessment Year & carry forward up to 7 Assessment Years.

In computing the Total Income of an assessee, being an individual, there shall be deducted, in accordance with and subject to the provisions of this Section, any amount paid by him in the Previous Year, out of his income chargeable to tax, by way of interest on loan taken by him from any financial institution or any approved charitable institution for the purpose of his higher education or his relative [Section 80E(1)]

The deduction specified above shall be allowed in computing the Total Income in respect of the initial Assessment Year and seven Assessment Years immediately succeeding the initial Assessment Year or until the interest referred above is paid by the assessee in full, whichever is earlier [80E(2)]

Meaning of "relative" enlarged: The Act has enlarged the definition of "relative" given in clause (e) of sub-Section (3). As per the new definition "relative", in relation to an individual, means the spouse and children of that individual or the student for whom the individual is the legal guardian.

DEDUCTION IN RESPECT OF INTEREST ON LOAN FOR RESIDENTIAL HOUSE PROPERTY [SEC. 80EE]

1	Eligible Assessee	Individual
2	Condition	• Assessee has taken a loan from a financial institution during Financial Year 2013-14, for acquiring residential house property. • Amount of loan does not exceed ₹ 25 lakhs. • Value of house property does not exceed ₹ 40 lakhs. • Assessee does not own any residential house property on the date of sanction of loan
3	Maximum Amount of deduction	Interest payable for the previous year shall be deductible for the Assessment Year 2014-15 subject to a maximum of ₹ 1 lakh
4	Special Provision	If interest payable during the previous year 2013-14 is less than ₹ 1 lakh, the balance amount shall be allowed as deduction in the Assessment Year 2015-16.

From the Assessment Year 2014-15, any individual, not owning any residential house property on the date of sanction of loan, has taken loan for acquiring residential house property during the Financial Year 2013-14, is eligible for deduction u/s 80EE for the amount of interest paid on the loan upto a maximum of ₹ 1 lakh. If, however, interest payable is less than ₹ 1 lakh, the balance amount shall be allowed as deduction in Assessment Year 2015-16.

Conditions :

(i) The amount of loan sanctioned for acquisition of the residential house propertly does not exceed ₹25 lakh.

(ii) The value of residential house property does not exceed ₹ 40 lakh.

The interest allowed u/s 80EE can not be deductible under any other provision of the Act for the same or any other assessment year.

DEDUCTION IN RESPECT OF DONATIONS TO CERTAIN FUNDS, CHARITABLE INSTITUTIONS, ETC. [SEC. 80G]

Deduction under this Section is available to all assessees.

Conditions for claiming deduction:-

(i) The donation should be of a sum of money and not in kind.

(ii) The donation should be to specified funds/institutions.

(iii) Amount paid by any mode of payment other than cash and if paid in cash the amount should not exceed ₹ 10,000.

	Eligible Donation	Qualifying Deduction	Permissible Amount
1.	PM's National Relief Fund;	From item Nos. 1 to 23 there is no maximum limit (i.e. 100% of the amount will qualify for deduction)	Quantum of deduction for item Nos. 1 to 18, 20, 24, 30, 31, 32 & 33 = 100% of the qualifying amount. For other items, quantum of deductions = 50% of the qualifying amount.
2.	PM's Armenia Earthquake Relief Fund;		
3.	The Africa (Public Contributions India) Fund;		
4.	The National Foundation for Communal Harmony		
5.	A university or any educational institution of national eminence as may be approved;		
6.	The National Illness Assistance Fund;		
7.	Any Zila Saksharta Samiti for improvement of primary education in villages and towns and for literacy activities;		
8.	National Blood Transfusion Council or to any State Blood Transfusion Council;		
9.	Any fund set up by the State Government for medical relief to the poor;		
10.	The Army Central Welfare Fund or the Indian Naval Benevolent Fund or the Airforce Central Welfare Fund established by the armed forces of the Union for the welfare of the past and present members of the such forces or their dependants;		
11.	The Chief Minister's Relief Fund or the Lieutenant Governor's Relief Fund in respect of any State or Union Territory, as the case may be;		
12.	The National Sports Fund to be set up by the Central Government;		

13. The National Cultural Fund set up by the Central Government; 14. The Fund for Technology Department and Application setup by the Central Government; 15. The National Defence Fund; 16. Any fund setup by the State Government of Gujarat exclusively for providing relief to the victims of earthquake in Gujarat; 17. Any sum paid during the period beginning with 26.1.2001 and ending on 30.9.2001 to any trust, institutions or fund recognised under Section 80G for providing relief to the victims of earthquake in Gujarat; 18. National Trust for Welfare of Persons with Autism, Cerebral Palsy, Mental Retardation and Multiple disabilities constituted under the relevant Act of 1999; 19. PM's Drought Relief Fund; 20. The National Children's Fund; 21. Jawaharlal Nehru Memorial Fund; 22. Indira Gandhi Memorial Trust; 23. Rajiv Gandhi Foundation;		
24. Contribution by a company as donations to the Indian Olympic Association or to any other Association notified by the Central Government u/s. 10(23); 25. Any approved fund or institution established for charitable purposes; 26. Government or local authority to be used for charitable purpose; 27. Any authority set up for providing housing accommodation or town planning; 28. Any corporation established by Government for promoting interest of schedules caste/ scheduled tribe/backward class; 29. Renovation of notified temple mosque, church, or gurudwara or any other notified place of national importance; 30. Government or local authority or approved institution/association for promotion of family planning;	From Sl. Nos. 24 to 30 qualifying amount shall be restricted to 10% of Adjusted Total Income (i.e. G.T.I. as reduced by deductions u/s. 80CCC to 80U other than 80G and other income on which no tax is payable and other incomes on which deductions under Chapter VIA are not allowed)	

31. The Swachh Bharat Kosh, set up by the Central Government, other than the sum spent by the assessee in pursuance of Corporate Social Responsibility under sub-section (5) of section 135 of the Companies Act, 2013 **[w.e.f. A.Y. 2015-16]**; or 32. The Clean Ganga Fund, set up by the Central Government, where such assessee is a resident and such sum is other than the sum spent by the assessee in pursuance of Corporate Social Responsibility under sub-section (5) of section 135 of the Companies Act, 2013 **[w.e.f. A.Y. 2015-16]**; or 33. The National Fund for Control of Drug Abuse constituted under section 7A of the Narcotic Drugs and Psychotropic Substances Act, 1985 **[w.e.f. A.Y. 2016-17]**.		

The requirements for approval of an institution or fund u/s 80G and rule 11AA are as under:

(1) The application for approval of any institution or fund of section 80G(5)(vi) shall be in Form No.10G and shall be made in triplicate.

(2) The application shall be accompanied by the following documents, namely:

(i) Copy of registration granted u/s 12A or copy of notification issued u/s 10(23) (omitted w.e.f. Assessment Year 2003-04) or 10(23C);

(ii) Notes on activities of institution or fund since its inception or during the last three years, whichever is less;

(iii) Copies of accounts of the institution or fund since its inception or during the last three years, whichever is less.

(3) The Commission may call for such further documents or information from the institution or fund or cause such inquiries to be made as he may deem necessary in order to satisfy himself about the genuineness of the activities of such institution or fund.

(4) Where the Commissioner is satisfied that all the conditions laid down in clauses (i) to (v) of Section 80G(5) are fulfilled by the Institution or fund, he shall record such satisfaction in writing and grant approval to the institution or fund specifying the assessment year or years for which the approval is valid.

(5) Where the Commissioner is satisfied that one or more of the conditions laid down in clauses (i) to (v) of Section 80G(5) are not fulfilled, he shall reject the application for approval, after recording the reasons for such rejection in writing.

Provided that no order of rejection of an application shall be passed without giving the institution or fund an opportunity of being heard.

(6) The time limit within which the Commissioner shall pass an order either granting the approval or rejecting the application shall not exceed six months from the date on which such application was made.

Provided that in computing the period of six months, any time taken by the applicant in not complying with the directions of the Commissioner under sub-rule (3) shall be excluded.

DEDUCTION IN RESPECT OF RENTS PAID [SEC. 80GG]

1	Eligible Assessee	Individual
2	Condition	The condition for deduction in respect of rents paid is given below.
3	Maximum Deduction	Amount of deduction is also given below.

The deduction in respect of rent paid is available to Individual with effect from Assessment Year 1998-99.

Conditions :

(i) The assessee is not being in receipt of any house rent allowance following under clause (13A) of Section 10 from his employer.

(ii) The expenditure incurred (for the purpose of his own residence) by way of rent for any furnished or unfurnished accommodation is in excess of 10% of his Total Income after allowing all deductions except deduction under this Section.

(iii) The assessee or his spouse or minor child or an HUF of which he is a member, does not own any accommodation at the place where he ordinarily resides or performs duties of his office or employment or carries on his business/profession.

(iv) If the assessee owns any accommodation at any place other than the place of employment or business and such accommodation is not in the occupation of the assessee and shall not be assessed in his hands as self occupied property.

Deduction *:* Least of the following :–

(i) Rent paid minus 10% of Adjusted Total Income

(ii) 25% of Adjusted Total Income

(iii) ₹ 2,000 p.m.

Adjusted Total Income : Gross Total Income as reduced by :

(a) Long Term Capital Gain, if any, included in the Gross Total Income

(b) Short Term Capital Gain under section 111A, if any, included in the Gross Total Income

(c) All deduction under Chapter VIA (Section 80CCC to 80U) other than the deduction under this Section.

(d) Any income referred to in Sections 115A to D included in the Gross Total Income.

DEDUCTION IN RESPECT OF CERTAIN DONATIONS FOR SCIENTIFIC RESEARCH OR RURAL DEVELOPMENT [SEC. 80GGA]

In computing the Total Income of an assessee whose Gross Total Income does not include income from "Profits and Gains of Business or Profession", deduction shall be allowed of an amount paid by him to—

(a) an approved scientific research association or University or College or other institution to be used for scientific research, research in social science or statistical research.

(b) an approved association or institution to be used for carrying out any approved programme or rural development,

(c) an approved institution or association which has the object of training of persons for implementing programmes of rural development [Sec. 35CCA]

(d) public sector company or local authority or an approved association or institution for carrying out any eligible project or scheme u/s 35AC.

(e) association/institution/fund which has the object of carrying out any programme of conservation of natural resources or afforestation [Sec. 35CCB]

(f) National Urban Poverty Eradication Fund (NUPEF).

Section 80GGA (2A) provides that no deduction shall be allowed under section 80GGA in respect of any sum exceeding ₹ 10,000 unless such sum is paid by any mode other than cash.

DEDUCTIONS BY COMPANIES TO POLITICAL PARTIES [SEC. 80GGB]

Allowable to : An Indian Company

Condition : Amount should be contributed by any mode other than cash.

Amount of Deduction : 100% of sum contributed during a Previous Year to any political party, registered u/s 29A of Representation of the People Act, 1951.

DONATIONS TO POLITICAL PARTIES [SEC. 80GGC]

Allowable to : Any person except local authority and an artificial juridical person wholly or partly funded by the Government.

Condition : Amount should be contributed by any mode other than cash.

Amount of Deduction : 100% of sum contributed during a Previous Year to any political party, registered u/s 29A of Representation of the People Act, 1951.

Contributions to an Electoral Trust also eligible for deduction under Section 80GGB and 80GGC

DEDUCTIONS IN RESPECT OF PROFITS & GAINS FROM INDUSTRIAL UNDERTAKINGS OR ENTERPRISES ENGAGED IN INFRASTRUCTURE DEVELOPMENT [SEC. 80IA]

The deduction under this Section is applicable to all assessees whose Gross Total Income includes any profits and gains derived from any business of an industrial undertaking or an enterprise as below :

Sl. No.	Classification of Industries	Period of commencement	Deduction
(i)	Any enterprise carrying on the business of developing or maintaining and operating or developing, maintaining and operation any infrastructure facility	On or after 1.4.1995	100% for 10 consecutive Assessment Years.
(ii)	Any undertaking providing telecommunication services whether basic or cellular including radio paging, domestic satellite service or network of trunking and electronic data interchange services.	From 1.4.95 to 31.3.2005	100% for first 5 years & 30% for the next 5 years.
(iii)	Any undertaking which develops or develops and operates or maintains and operates an industrial park notified by the Central Government.	From 1.4.97 to 31.3.2011	100% for 10 consecutive Assessment Years.
(iv)	An Industrial undertaking set up in any part of India for the generation or generation and distribution of power.	From 1.4.93 to 31.3.2017	100% for 10 consecutive Assessment Years.
(v)	An industrial undertaking which starts transmission or distribution of power by laying a network of new transmission or distribution lines.	From 1.4.99 to 31.3.2017	100% for 10 consecutive Assessment Years.

(vi)	An industrial undertaking starts business of substantial renovation and modernisation of existing transmission / distribution lines in Power Sector.	From 1.4.2004 to 31.3.2017	100% for 10 consecutive Assessment Years.
(vii)	Undertaking established for reconstruction / revival of Power Generation Plant	Established before 30.11.2005 to 31.3.2011	100% for 10 consecutive Assessment Years.

The deduction under this Section is available at the option of the assessee for any 10 consecutive Assessment Years out of 15 years beginning from the year in which the undertaking or enterprise develops and begins to operate any infrastructure facility or starts providing telecommunication services or develops an industrial part or generates power or commences transmission or distribution of power. However, in case of an infrastructure facility being a high way project including housing or other activities being an integral part of a high way project, the assessee can claim deduction for any 10 consecutive Assessment Years out of 20 years beginning from the year of operation.

Other Conditions :

(i) For the purpose of completing deduction under this Section, the profits and gains of the eligible business shall be computed as if such eligible business were the only source of income during the relevant Previous Year.

(ii) Where housing or other activities are an integral part of the high way project and the profits and gains of which have been calculated in accordance of the provision of the Section, the profits have not been liable to tax if the following conditions are not fulfilled :–

(a) The profits have been transferred to a special reserve account

(b) The same is actually utilised for the high way project excluding housing and other activities before the expiry of 3 years following the year of transfer to the reserve account.

(c) The amount remaining unutilised shall be chargeable to tax as income of the year in which such transfer to reserve account took place.

(iii) Where the assessee is a person other than a company or a cooperative society, the deduction shall not be admissible unless the accounts of the industrial undertaking for the Previous Year relevant to the Assessment Year for which the deduction is claimed have been audited by an accountant and the report in Form No. 10CCB (Rule 18BBB) is furnished along with the return of income.

(iv) Where any goods or services held for purposes of the eligible business are transferred to any other business carried on by the assessee or vice versa and if the consideration for such transfer does not correspond to the market value of such goods of services as on the date of transfer, the profits and gains of the eligible business shall be computed as if the transfer had been made at the market value of such goods or services as on that date. However, if the computation of profits and gains presents any difficulty in the opinion of the Assessing Officer, he may compute such profits and gains on such reasonable basis as he may deem fit. Similarly, where due to close connection between the assessee and other person for any other reason it appears to the Assessing Officer that the profits of the eligible business is increased to more than the ordinary profit, the Assessing Officer shall compute the profit on a reasonable basis for allowing the deduction.

(v) If the profits and gains are allowed as deduction under this Section for any Assessment Year, no deduction under Sections 80HH to 80RRA to the extent of such profits and gains shall be allowed.

(vi) Where any undertaking of an Indian company which is entitled to the deduction under this Section is transferred before expiry of the period of deduction to another Indian company in a scheme of amalgamation or demerger, no deduction has been admissible to the amalgamating or demerged company for the Previous Year in which amalgamation or demerger expressed and the amalgamated or the resulting company shall be entitled to the deduction as if the amalgamation or demerger had not been taken place.

(vii) The Act has amended Section 80-IA(4) so as to enable an authority or a board or a corporation or any other body established or constituted under a Central or State Act which is not incorporated under the Companies Act, 2013 also to take advantage of the benefits provided under the said Section.

DEDUCTIONS IN RESPECT OF PROFITS AND GAINS BY AN UNDERTAKING OR ENTERPRISE ENGAGED IN DEVELOPMENT OF SPECIAL ECONOMIC ZONE [SEC. 80IAB]

(1) Where the Gross Total Income of an assessee, being a Developer, includes any profits and gains derived by an undertaking or an enterprise from any business of developing a Special Economic Zone, notified on or after the 1st day of April, 2005 under the Special Economic Zones Act, 2005, there shall, in accordance with and subject to the provisions of this Section, be allowed, in computing the Total Income of the assessee, a deduction of an amount equal to one hundred per cent of the profits and gains derived from such business for ten consecutive Assessment Years.

(2) The deduction specified in sub-section (1) may, at the option of the assessee, be claimed by him for any ten consecutive Assessment Years out of fifteen years beginning from the year in which a Special Economic Zone has been notified by the Central Government

Provided that where in computing the Total Income of any undertaking, being a Developer for any Assessment Year, its profits and gains had not been included by application of the provisions of sub-section (13) of Section 80-IA, the undertaking being the Developer shall be entitled to deduction referred to in this Section only for the unexpired period of ten consecutive Assessment Years and thereafter it shall be eligible for deduction from income as provided in sub-section (1) or sub-section (2), as the case may be

Provided further that in a case where an undertaking, being a Developer who develops a Special Economic Zone on or after the 1st day of April, 2005 and transfers the operation and maintenance of such Special Economic Zone to another Developer (hereafter in this Section referred to as the transferee Developer), the deduction under sub-section (1) shall be allowed to such transferee Developer for the remaining period in the ten consecutive Assessment Years as if the operation and maintenance were not so transferred to the transferee Developer.

(3) The provisions of sub-section (5) and sub-sections (7) to (12) of Section 80-IA shall apply to the Special Economic Zones for the purpose of allowing deductions under sub-section (1).

DEDUCTION IN RESPECT OF PROFITS AND GAINS FOR CERTAIN INDUSTRIAL UNDERTAKING OTHER THAN INFRASTRUCTURE DEVELOPMENT UNDERTAKINGS [SEC. 80IB]

The deduction is available to the following undertaking or enterprises etc.

Sl. No.	Undertaking	% of Profit deductible	Period of deduction
A.	Ship- brought into use between 1.4.91 & 31.3.95	30	For the first 10 years
B.	Hotel commenced between 1.4.97 and 31.3.2001 approved hotel in hilly are or rural area or a place of pilgrimage or in a notified area	50	For the first 10 years
C.	Any other approved hotel (Hotels in the cities of Calcutta, Chennai, Delhi and Mumbai are not eligible) commenced between 1.4.97 and 31.3.2001	30	For the first 10 years

D.

Sl. No.	Classification of Industries	Period of Commencement between	Deduction of profits dividend
1	Industrial undertaking located in an industrially backward state specified in the Eighth Schedule;	1.4.1993 and 31.3.2004 (1.4.1993 and 31.3.2012 for an industrial undertaking in the State of Jammu and Kashmir)	100% for initial 5 years. Thereafter 30% for 5 years in case of company otherwise 25%. For cooperative society deduction is 100% of initial 5 years and thereafter 25% of 7 years.
2	Industrial undertaking located in industrially backward district notified by the Central Government		
	-Category A	1.10.1994 and 31.3.2004	100% for 5 years and 30% for next 5 years in case of companies (25% for others). For cooperative society 25% for 7 years. after 100% for initial 5 years.
	-Category B	1.10.1994 and 31.3.2004	100% for 3 years and 30% for next 5 years in case of company (25% for others). For cooperative society 25% for 9 years after 100% for initial 3 years.
3	Any company engaged in scientific and industrial research and development.	Approved by the prescribed authority after business for 31.3.2000 but before 1.4.2007	100% of the profits derived from such business for 10 years starting from the initial Assessment year.
4	Undertaking which begins commercial production of mineral oil –		100% for the first 7 consecutive Assessment Years starting from the initial Assessment Years.
	a) in North Eastern Region.	Before 1.4.97	
	b) in other Regions	On or after 1.4.97	
	Undertaking which begins refining of mineral oil.	On or after 1.10.98 but before 1.4.2012	
	Undertaking which begins production of natural gas	On or after 1.4.2009	

Sl. No.	Classification of Industries	Period of Commencement between	Deduction of profits dividend
5	Undertaking engaged in developing and building housing projects approved by a local authority: profits derived from of the plot of land minimum 1 acre area and residential unit built up to 1000 sq. ft. where such residential units are in Delhi/Mumbai or within 25 kms. for the municipal limits of these cities and 1500 sq. ft. at any other place. The build-up area of the shops and other commercial establishments included in the housing project should not exceed 3% of the total build-up area of the housing project or 5,000 sq.ft., whichever is more. [see note]	1.10.98 and 31.3.2008 [In case where housing project has been approved by local authority during 2004-05, the construction should be completed within 4 years from the end of the financial year in which the project is approved and if the project is approved on or after 1st April, 2005, the construction should be completed within 5 years from the end of the financial year in which the project is approved]	100% of the profit derived from such business.
6	Industrial undertaking deriving profit from the business of setting up and operating a cold chain facility for agricultural produce.	1.4.1999 and 31.3.2004	100% for initial 5 years and thereafter 30% for 5 years in case of company (25% for others). For Co-operative Society after initial 5 years @100%, the next 7 years @ 25%
7	Undertaking engaged in integrated business of handling, storage and transportation of food grains.	On or after 1.4.2001	100% for initial 5 years. Thereafter 30% for 5 years for company (25% for others).
	Processing, preservation and packaging of meat and meat products or poultry/marine/dairy products	On or after 1.4.2009	
8	Finance Act, 2002, inserted Sec. 80IB(7A) and Sec. 80IB(7B) allowing deduction in case of any multiplex theatre and convention centers w.e.f. AY 2003-04 as under :		
	- Multiplex theatre other than located within the municipal jurisdiction of Chennai, Delhi, Mumbai or Kolkata.	1.4.2002 and ending 31.3.2005	50% of the profits of 5 consecutive years beginning from the initial Assessment Year.
	- Convention Centre	1.4.2002 and ending 31.3.2005	50% of the profits of 5 consecutive years beginning from the initial Assessment Year.
9	Operating and maintaining a hospital		100% of the profits derived from such business for 5 consecutive years beginning from the initial Assessment Year.
	-in rural area	From 1.10.2004 to 31.3.2008	
	-in anywhere in India other than excluded area (w.e.f. AY 2009-10)	From 1.4.2008 to 31.3.2013	

Note: The objective of the tax benefit for housing projects is to build housing stock for low and middle income households. This has been ensured by limiting the size of the residential unit. However, this is being circumvented by the developer by entering into agreement to sell multiple adjacent units to a single buyer. Accordingly, the Act has inserted new clauses viz. clause (e) and (f) to Section 80-IB(10) to provide that the undertaking which develops and builds the housing project shall not be allowed to allot more than one residential unit in the housing project to the same person, not being an individual, and where the person is an individual, no other residential unit in such housing project is allotted to any of the following person:—

(i) The individual or the spouse or minor children of such individual;

(ii) The Hindu Undivided Family in which such individual is the Karta;

(iii) Any person representing such individual, the spouse or minor children of such individual or the Hindu Undivided Family in which such individual is the Karta.

This amendment will take effect from 1-4-2010 and shall accordingly, apply in relation to Assessment Year 2010-11 and subsequent years.

Further, as per the Finance (No. 2) Act, 2009 the deduction will be available if the project is approved by the local authority before 31-3-2008 instead of 31-3-2007.

Where any goods held for the purposes of the eligible business are transferred to any other business carried on by the assessee, or where any goods held for the purposes of any other business are carried on by the assessee are transferred to the eligible business and, in either case, the consideration, if any, for such transfer as recorded in the accounts of the eligible business does not correspond to the market value of such goods as on the date of the transfer, then, for the purposes of the deduction under this section, the profits and gains of such eligible business shall be computed as if the transfer, in either case, had been made at the market value of such goods as on that date.

For the purposes of this sub-section w.e.f. A.Y. 2013-14, 'market value', in relation to any goods or services, means –

(i) The price that such goods or services would ordinarily fetch in the open market; or

(ii) The arm's length price as defined in clause (ii) of Section 92F, where the transfer of such goods or services is a specified domestic transaction referred to in section 92BA.

SPECIAL PROVISIONS IN RESPECT OF CERTAIN UNDERTAKINGS OR ENTERPRISES IN CERTAIN SPECIAL CATEGORY STATES [SEC. 80-IC]

(1) Where the Gross Total Income of an assessee includes any profits and gains derived by an undertaking or an enterprise from any business referred to in sub-section (2), there shall, in accordance with and subject to the provisions of this Section, be allowed, in computing the Total Income of the assessee, a deduction from such profits and gains, as specified in sub-section (3).

(2) This Section applies to any undertaking or enterprise,—

  (a) which has begun or begins to manufacture or produce any article or thing, not being any article or thing specified in the Thirteenth Schedule, or which manufactures or produces any article or thing, not being any article or thing specified in the Thirteenth Schedule and undertakes substantial expansion during the period beginning—

    (i) on the 23rd day of December, 2002 and ending before the 1st day of April, 2007 in any Export Processing Zone or Integrated Infrastructure Development Centre or Industrial Growth Centre or Industrial Estate or Industrial Park or Software Technology Park or Industrial Area or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the Central Government in this regard, in the State of Sikkim; or

    (ii) on the 7th day of January, 2003 and ending before the 1st day of April, 2012, in any Export Processing Zone or Integrated Infrastructure Development Centre or Industrial Growth Centre or Industrial Estate or Industrial Park or Software Technology Park or Industrial Area or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the Central Government in this regard, in the State of Himachal Pradesh or the State of Uttaranchal; or

    (iii) on the 24th day of December, 1997 and ending before the 1st day of April, 2007, in any Export Processing Zone or Integrated Infrastructure Development Centre or Industrial

Growth Centre or Industrial Estate or Industrial Park or Software Technology Park or Industrial Area or Theme Park, as notified by the Board in accordance with the scheme framed and notified by the Central Government in this regard, in any of the North-Eastern States;

(b) which has begun or begins to manufacture or produce any article or thing, specified in the Fourteenth Schedule or commences any operation specified in that Schedule, or which manufactures or produces any article or thing, specified in the Fourteenth Schedule or commences any operation specified in that Schedule and undertakes substantial expansion during the period beginning—

 (i) on the 23rd day of December, 2002 and ending before the 1st day of April, 2007, in the State of Sikkim; or

 (ii) on the 7th day of January, 2003 and ending before the 1st day of April, 2012, in the State of Himachal Pradesh or the State of Uttaranchal; or

 (iii) on the 24th day of December, 1997 and ending before the 1st day of April, 2007, in any of the North-Eastern States.

(3) The deduction referred to in sub-Section (1) shall be—

 (i) in the case of any undertaking or enterprise referred to in sub-clauses (i) and (iii) of clause (a) or sub-clauses (i) and (iii) of clause (b), of sub-section (2), one hundred per cent of such profits and gains for ten Assessment Years commencing with the initial Assessment Year;

 (ii) in the case of any undertaking or enterprise referred to in sub-clause (ii) of clause (a) or sub-clause (ii) of clause (b), of sub-section (2), one hundred per cent of such profits and gains for five Assessment Years commencing with the initial Assessment Year and thereafter, twenty-five per cent (or thirty per cent where the assessee is a company) of the profits and gains.

(4) This Section applies to any undertaking or enterprise which fulfils all the following conditions, namely:—

 (i) *it is not formed by splitting up, or the reconstruction, of a business already in existence*

 Provided that this condition shall not apply in respect of an undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as is referred to in Section 33B, in the circumstances and within the period specified in that Section;

 (ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

 Explanation : The provisions of *Explanations 1* and *2* to sub-Section (3) of Section 80-IA shall apply for the purposes of clause (*ii*) of this sub-section as they apply for the purposes of clause (*ii*) of that sub-section.

(5) Notwithstanding anything contained in any other provision of this Act, in computing the Total Income of the assessee, no deduction shall be allowed under any other Section contained in Chapter VIA or in Section 10A or Section 10B, in relation to the profits and gains of the undertaking or enterprise.

(6) Notwithstanding anything contained in this Act, no deduction shall be allowed to any undertaking or enterprise under this Section, where the total period of deduction inclusive of the period of deduction under this Section, or under the second proviso to sub-section (4) of Section 80-IB or under Section 10C, as the case may be, exceeds ten Assessment Years.

(7) The provisions contained in sub-section (5) and sub-sections (7) to (12) of Section 80-IA shall, so far as may be, apply to the eligible undertaking or enterprise under this Section.

(8) Deduction u/s 80-IC will not be allowed if the assessee does not furnish the Return of Income u/s 139(1).

(9) For the purposes of this Section,—

   (i) "Industrial Area" means such areas, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;

   (ii) "Industrial Estate" means such estates, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;

   (iii) "Industrial Growth Centre" means such centres, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;

   (iv) "Industrial Park" means such parks, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;

   (v) "Initial Assessment Year" means the Assessment Year relevant to the Previous Year in which the undertaking or the enterprise begins to manufacture or produce articles or things, or commences operation or completes substantial expansion;

   (vi) "Integrated Infrastructure Development Centre" means such centres, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government;

   (vii) "North-Eastern States" means the States of Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland and Tripura;

   (viii) "Software Technology Park" means any park set up in accordance with the Software Technology Park Scheme notified by the Government of India in the Ministry of Commerce and Industry;

   (ix) "Substantial Expansion" means increase in the investment in the plant and machinery by at least fifty per cent of the book value of plant and machinery (before taking depreciation in any year), as on the first day of the Previous Year in which the substantial expansion is undertaken;

   (x) "Theme Park" means such parks, which the Board, may, by notification in the Official Gazette, specify in accordance with the scheme framed and notified by the Central Government.

DEDUCTION IN RESPECT OF PROFITS AND GAINS FROM BUSINESS OF HOTELS AND CONVENTION CENTRES IN SPECIFIED AREA [SEC. 80ID]

(1) Where the Gross Total Income of an assessee includes any profits and gains derived by an undertaking from any business referred to in sub-section (2) (such business being hereinafter referred to as the eligible business), there shall, in accordance with and subject to the provisions of this Section, be allowed, in computing the Total Income of the assessee, a deduction of an amount equal to one hundred per cent of the profits and gains derived from such business for five consecutive Assessment Years beginning from the initial Assessment Year.

(2) This Section applies to any undertaking,—

   (i) engaged in the business of hotel located in the specified area, if such hotel is constructed and has started or starts functioning at any time during the period beginning on the 1st day of April, 2007 and ending on the 31st day of July, 2010; or

   (ii) engaged in the business of building, owning and operating a convention centre, located in the specified area, if such convention centre is constructed at any time during the period beginning on the 1st day of April, 2007 and ending on the 31st day of July, 2010; or

(iii) engaged in the business of hotel located in specified district having a World Heritage Site, if such hotel is constructed and has started or starts functioning at any time during the period beginning on the 1st day of April, 2008 and ending on 31st day of March, 2013.

(3) The deduction under sub-section (1) shall be available only if —

(i) the eligible business is not formed by the splitting up, or the reconstruction, of a business already in existence;

(ii) the eligible business is not formed by the transfer to a new business of a building previously used as a hotel or a convention centre, as the case may be;

(iii) the eligible business is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

(iv) the assessee furnishes along with the return of income, the report of an audit in such form and containing such particulars as may be prescribed, and duly signed and verified by an accountant, as defined in the Explanation to sub-section (2) of Section 288, certifying that the deduction has been correctly claimed.

(4) Notwithstanding anything contained in any other provision of this Act, in computing the Total Income of the assessee, no deduction shall be allowed under any other Section contained in Chapter VIA or Section 10AA, in relation to the profits and gains of the undertaking.

(5) The provisions contained in sub-section (5) and sub-sections (8) to (11) of Section 80-IA shall, so far as may be, apply to the eligible business under this Section.

(6) For the purposes of this Section, -

(i) "Convention Centre" means a building of a minimum 25,000 square metre covered plinth area with centralised air-conditioner comprising of at least 10 conventional halls to be used for the purpose of holding conference and seminars having other specified facilities and amenities.

(ii) "Hotel" means two-star, three-star or four-star category hotels as classified by the Central Government.

(iii) "Specified Area" means the National Capital Territory of Delhi and the district of Budh Nagar, Faridabad, Gurgaon, Gautam and Ghaziabad.

SPECIAL PROVISIONS IN RESPECT OF CERTAIN UNDERTAKINGS IN NORTH- EASTERN STATES [SEC. 80IE]

(1) Where the Gross Total Income of an assessee includes any profits and gains derived by an undertaking, to which this Section applies, from any business referred to in sub-section (2), there shall be allowed, in computing the Total Income of the assessee, a deduction of an amount equal to one hundred per cent of the profits and gains derived from such business for ten consecutive Assessment Years commencing with the initial Assessment Year.

(2) This Section applies to any undertaking which has, during the period beginning on the 1st day of April, 2007 and ending before the 1st day of April, 2017, begun or begins, in any of the North-Eastern States,—

(i) to manufacture or produce any eligible article or thing;

(ii) to undertake substantial expansion to manufacture or produce any eligible article or thing;

(iii) to carry on any eligible business.

(3) This Section applies to any undertaking which fulfils all the following conditions, namely:—

(i) it is not formed by splitting up, or the reconstruction, of a business already in existence

Provided that this condition shall not apply in respect of an undertaking which is formed as a result of the re-establishment, reconstruction or revival by the assessee of the business of any such undertaking as referred to in Section 33B, in the circumstances and within the period specified in the said Section;

(ii) it is not formed by the transfer to a new business of machinery or plant previously used for any purpose.

Explanation : The provisions of *Explanations 1* and 2 to sub-Section (3) of Section 80-IA shall apply for the purposes of clause (*ii*) of this sub-section as they apply for the purposes of clause (*ii*) of that sub-section.

(4) Notwithstanding anything contained in any other provision of this Act, in computing the Total Income of the assessee, no deduction shall be allowed under any other Section contained in Chapter VIA or in Section 10A or Section 10AA or Section 10B or Section 10BA, in relation to the profits and gains of the undertaking.

(5) Notwithstanding anything contained in this Act, no deduction shall be allowed to any undertaking under this Section, where the total period of deduction inclusive of the period of deduction under this Section, or under Section 80-IC or under the second proviso to sub-section (4) of Section 80-IB or under Section 10C, as the case may be, exceeds ten Assessment Years.

(6) Deduction u/s 80-IE will not allowed if the assessee does not furnish the Return of Income u/s 139(1)

(7) The provisions contained in sub-section (5) and sub-sections (7) to (12) of Section 80-IA shall, so far as may be, apply to the eligible undertaking under this Section.

(8) For the purposes of this Section, -

(i) "Substantial Expansion" means increase in the investment in the Plant and Machinery by at least 25% of the book value of Plant and Machinery as on the 1st day of the Previous Year in which substantial expansion is undertaken.

(ii) "Eligible Article or Thing" means the article or thing other than tobacco, manufactured tobacco substitute, plastic carry bag (Less than 20 Microns), and goods produced by petroleum oil or gas refineries.

(iii) "Eligible Business" includes –

- Hotel (Not Below 2 Star Category),
- Adventure & Leisure Sports including Ropeways,
- Nursing Homes (Minimum 25 Beds),
- Old-age Home,
- Information Technology related Training Centre,
- Manufacturing Information Technology related Hardware,
- Vocational Training Institute for Hotel Management, Food Craft, Entrepreneurship Development, Nursing & Para Medical, Civil Aviation & Fashion Design & Industrial Training.
- Bio-technology

DEDUCTION IN RESPECT OF PROFITS AND GAINS FROM BUSINESS OF COLLECTING AND PROCESSING OF BIO- DEGRADABLE WASTE. [SEC. 80JJA]

With effect from Assessment Year 1999-2000, where the Gross Total Income of an assessee include profits and gains derived from the business of collecting and processing or treatment of bio-degradable waste for generating power, or producing bio-fertilizers, bio-pesticides or other biological agents or for producing bio-gas or making pellets or briquettes for fuel or organic manure these shall be allowed in computing the Total Income of the assessee, a deduction of an amount equal to the whole of such profits and gains for a period of five consecutive Assessment Years beginning with the Assessment Year relevant to the Previous Year in which such business commences.

DEDUCTION IN RESPECT OF EMPLOYMENT OF NEW WORKMEN [SEC 80JJAA]

All assessee having manufacturing units is allowed for deduction provided the following conditions are satisfied :

(i) The Gross Total Income of the assessee includes profits and gains derived from the manufacture of goods in a factory.

(ii) The factory is not hived off or transferred from another existing undertaking or amalgamation with another industrial undertaking or as a result of any business re-organization.

(iii) The assessee employs new regular workmen in the Previous Year in such factory.

(iv) The assessee furnishes the report of a Chartered Accountant in Form No. 10DA [Rule 19AB]

Deduction is available for 3 Previous Years commencing from the Previous Year in which such employment is provided.

Amount of deduction

(i) **New industrial undertaking :** 30% of the wages paid to new regular workmen in excess of 50 regular workmen employed during the year.

(ii) **Existing undertaking :** 30% of the wages paid to new regular workmen provided these is at least 10% increase in number of regular workmen over the existing member of workmen employed in such undertaking, as on the last day of the preceding year.

Regular workmen

It does not include :–

(a) a casual workmen or

(b) a workmen employed through contract labour; or

(c) any other workman employed for a period of less than 300 days during the Previous Year.

For the purpose of this section, factory shall have the same meaning as assigned to it in clause (m) of Section 2 of the Factories Act, 1948.

DEDUCTIONS IN RESPECT OF CERTAIN INCOMES OF OFFSHORE BANKING UNITS AND INTERNATIONAL FINANCIAL SERVICES CENTRE [SEC. 80LA]

(1) Where the Gross Total Income of an assessee,—

(i) being a scheduled bank, or, any bank incorporated by or under the laws of a country outside India; and having an Offshore Banking Unit in a Special Economic Zone; or

(ii) being a Unit of an International Financial Services Centre, includes any income referred to in sub-section (2), there shall be allowed, in accordance with and subject to the provisions of this Section, a deduction from such income, of an amount equal to—

(a) one hundred per cent of such income for five consecutive Assessment Years beginning with the Assessment Year relevant to the Previous Year in which the permission, under clause (*a*) of sub-section (1) of Section 23 of the Banking Regulation Act, 1949 (10 of 1949) or permission or registration under the Securities and Exchange Board of India Act, 1992 (15 of 1992) or any other relevant law was obtained, and thereafter;

(b) fifty per cent of such income for next five Assessment Years.

(2) The income referred to in sub-section (1) shall be the income—

  (a) from an Offshore Banking Unit in a Special Economic Zone; or

  (b) from the business referred to in sub-section (1) of Section 6 of the Banking Regulation Act, 1949 (10 of 1949) with an undertaking located in a Special Economic Zone or any other undertaking which develops or develops and operates or develops, operates and maintains a Special Economic Zone; or

  (c) from any Unit of the International Financial Services Centre from its business for which it has been approved for setting up in such a centre in a Special Economic Zone.

(3) No deduction under this Section shall be allowed unless the assessee furnishes along with the return of income,—

  (i) the report, in the form specified by the Central Board of Direct Taxes under clause (*i*) of sub-Section (2) of Section 80LA, as it stood immediately before its substitution by this Section, of an accountant as defined in the *Explanation* to sub-section (2) of Section 288, certifying that the deduction has been correctly claimed in accordance with the provisions of this Section; and

  (ii) a copy of the permission obtained under clause (*a*) of sub-section (1) of Section 23 of the Banking Regulation Act, 1949 (10 of 1949).

  Explanation : For the purposes of this Section,—

    (a) "International Financial Services Centre" shall have the same meaning as assigned to it in clause (*q*) of Section 2 of the Special Economic Zones Act, 2005;

    (b) "Scheduled Bank" shall have the same meaning as assigned to it in clause (*e*) of Section 2 of the Reserve Bank of India Act, 1934 (2 of 1934);

    (c) "Special Economic Zone" shall have the same meaning as assigned to it in clause (*za*) of Section 2 of the Special Economic Zones Act, 2005;

    (d) "Unit" shall have the same meaning as assigned to it in clause (*zc*) of Section 2 of the Special Economic Zones Act, 2005.

DEDUCTION IN RESPECT OF CO-OPERATIVE SOCIETIES [SEC. 80P]

The following amounts are allowed as deduction under this Section –

(i) 100% of the profits attributable to any or more of the following activities in the case of a cooperative society engaged in –

  (a) carrying on business of banking or providing credit facilities to its members; or

  (b) a cottage industry; or

  (c) the marketing of the agricultural produce of its members; or

  (d) the purchase of agricultural implements, seeds, live stock or other articles intended for agriculture for the purpose of supplying them to its members; or

  (e) processing, without aid of power, of the agricultural produce of its members; or

  (f) the collective disposal of the labour of its members; or

  (g) fishing or allied activities; or

  (h) primary cooperative society engaged in supplying milk raised by its member to a Federal Milk Coop. Society or to the Government or a local authority or a Govt. Company or Corporation established under Central/State or Provincial Act. Similar benefit is also extended to a primary Cooperative Society engaged in supplying oilseeds, fruits and vegetables raised or grown by its members.

(ii) The whole of interest and dividend income derived by a Cooperative Society from its investments in any other Cooperative Society;

(iii) The whole of interest income from securities and property income in the case of a Cooperative Society other than housing society or an urban Consumer Society or a Society carrying on transport business where Gross Total Income does not exceed ₹ 20,000.

Urban Consumer Cooperative Society means a society for the benefit of consumers within the limits of Municipal Corporation, municipality, municipal committee, notified area committee, town area or cantonment.

(iv) The whole of the income from letting of godowns or warehouses for storage, processing or facilitating the marketing of commodities.

(v) In respect of other activities carried on either independently or in addition to above activities upto a sum of ₹ 50,000 (₹ 1,00,000 in case of Consumer Corporation Society) – U/s. 80P(2)(c).

Importance of Classification in registration:

Co-operative societies are classified under the respective State Co-operative Societies Acts as credit society, housing society, consumer co-operative society etc. This classification has apparently nothing to do with taxation as it is made for the purpose of regulating these institutions, which are under the purview and supervision of Registrars of Co-operative Societies. But, for income-tax purposes, there is a total immunity in respect of societies engaged in activities listed in section 80P(2)(a) and (b), while in respect of other co-operative societies deduction is partial.

A consumer co-operative society gets deduction of ₹1 lakh over and above the general exemption limit, while other co-operative societies get ₹50,000. Income by way of interest or dividend from any other co-operative society is totally exempt. So is the income of any co-operative society from letting of godowns or warehouses or storage or processing or facilitating marketing of commodities u/s 80P(2)(e). Section 80P also exempts total income upto ₹20,000 such exemption being confined to co-operative societies other than housing society or consumer society or societies engaged in transport business. This has now become meaningless with exemption limit for all co-operative societies having been raised. Co-operative societies are not deprived of the other deductions as for new industrial undertakings u/s 80-IA or for exports u/s 80-HHC or for that matter any other relief which is available for all persons. Section 80P(3) makes it clear that where deduction is available under other sections of Chapter VI-A, the exemption limit for co-operative societies will be applied after giving Chapter VI-A deductions to which it may be eligible.

DEDUCTION IN RESPECT OF ROYALTY OF AUTHORS [SEC. 80QQB]

Allowable to : Any resident individual, being an author/joint author, in respect of any income by way of lump sum consideration or otherwise as royalty or copyright fees for assignment or grant of any of his interests in the copyright of any book.

Amount of Deduction: 100% of the royalty income etc. subject to a maximum of ₹ 3,00,000.

In case of royalty or copyright fees, not in lump sum consideration, deduction shall be restricted to 15% of the value of books sold during the Previous Year.

Conditions:

(1) The assessee shall furnish a certificate in Form 10CCD.

(2) In case of income received from a source outside India, the assessee shall furnish a certificate in Form 10H.

DEDUCTION IN RESPECT OF ROYALTY ON PATENTS [SEC. 80RRB]

1	Eligible Assessee	Any resident individual
2	Condition	He must be registered under the Patents Act, 1970 on or after 1.4.2003, as the true and first inventor in respect of an invention, including a co-owner of the patent. The deduction is not available to assignees or mortgagees in respect of all or any rights of the patent
3	Maximum Cap	100% of such income subject to a maximum ₹ 3,00,000.
4	Special Provisions	(a) a certificate in Form 10CCE duly signed by the Controller under Patents Act. (b) a certificate in Form 10H, in case of income received from abroad, certifying that the deduction has been correctly claimed in accordance with this Section.

DEDUCTION IN RESPECT OF INTEREST ON DEPOSITS IN SAVINGS ACCOUNTS TO THE MAXIMUM EXTENT OF ₹ 10,000 [SECTION 80TTA] [W.E.F. A.Y. 2013-14]

Allowable to: an *individual or a Hindu Undivided Family*

Conditions: Where the Gross Total Income of an assessee, includes any income by way of interest on deposits (not being time deposits) in a saving account with-

(a) a banking company to which the Banking Regulation Act, 1949 applies (including any bank of banking institution referred to in Section 51 of that Act);

(b) a co-operative society engaged in carrying on the business of banking (including a co-operative land mortgage bank or a co-operative land development bank); or

(c) a Post Office as defined in clause (k) of Section 2 of the Indian Post Office Act, 1898.

Allowable Deduction: A deduction of such interest shall be allowed to the maximum extent of ₹ 10,000.

However, where the income referred to in this Section is derived from any deposit in a savings account held by, or on behalf of, a Firm, an Association of Persons or a Body of Individuals, no deduction shall be allowed under this Section in respect of such income in computing the Total Income of any partner of the firm or any member of the association or any individual of the body.

Exemption U/s. 10(15)(i) – Post Office Savings Bank Account exempt upto ₹ 3,500 (in an individual account) and ₹ 7,000 (in a joint Account) by virtue of notification number 32/ 2011

A consolidated study of Section 10(15)(i) and Section 80TTA provides (from Assessment Year 2013-14) as follows :

(i) Exemption upto ₹ 3,500 in a single account or / and ₹ 7,000/- in a joint account as deduction u/s. 10(15)(i)

(ii) Deduction upto ₹ 10,000 under Section 80TTA

DEDUCTION IN RESPECT OF TOTALLY BLIND OR MENTALLY RETARDED OR PHYSICALLY HANDICAPPED PERSON [SEC. 80U]

A resident individual suffering from permanent physical disability or total blindness or partial blindness or mental retardation reducing his capacity substantially for gainful employment is allowed a deduction of ₹ 75,000 or ₹ 1,25,000 in case of severe disability. The extent of blindness or other physical disability has to be certified by a Registered Medical Practitioner of the concerned discipline.

Such certificate has to be obtained from a physician, surgeon, etc. working in a Govt. Hospital. For the purpose of Sec. 80U of the Income Tax Act, 1961 any of the following disabilities shall be regarded as a permanent physical disability [Rule 11DD] e.g.–

(i) permanent physical disability of more than 50% in one limb; or

(ii) permanent physical disability of more than 60% in two or more limbs; or

(iii) permanent deafness with hearing impairment of 71 decibels and above; or

(iv) permanent and total loss of voice.

ILLUSTRATIONS ON DEDUCTIONS FROM GROSS TOTAL INCOME

Illustration 1 : Mr. N is employed at a gross salary of ₹ 8,00,000. He gets ₹ 15,000 interest on bank deposit. He has made the following investment/deposit during the year 2015-2016:

	₹
1. Life insurance premium:	
(i) Own life, insured for ₹ 80,000	15,000
(ii) Brother's life, dependent on him	5,000
(iii) Major son, not dependent on him	4,000
2. Contribution to unrecognised provident fund	60,000
3. Contribution to public provident fund	20,000
4. Contribution to ULIP	5,000
5. Repayment of loan to SBI to purchase a residential house: 50% repayment is towards interest.	1,20,000
He has paid education fees for his 3 children:	
A	12,000
B	9,000
C	6,000

Besides, interest of ₹ 1,632 on NSC-VIII, (purchased during the year 2009-2010) has been credited on them during the year 2015-2016.

Compute deduction u/s 80C for the Assessment Year 2016-2017.

Solution :

Computation of Deduction u/s 80C of Mr. N for the Assessment Year 2016-2017

Particulars	₹	₹
Deduction in respect of contribution to approved savings (Sec. 80C) :		
1. Life insurance premium(assumed issued before 1st April, 2012);		
(i) Own life	15,000	
(ii) Brother's life	—	
(iii) Major son	4,000	
2. Contribution to unrecognised provident fund	—	
3. Contribution to ULIP	5,000	
4. Contribution to public provident fund	20,000	
5. Repayment of housing loan to SBI	60,000	
6. Accrued interest on NSC- VIII issue	1,632	
7. Education fees for two children:		
A	12,000	
B	9,000	
	1,26,632	
Deduction available upto ₹ 1,50,000		**1,26,632**

Illustration 2 : Mr. Jamal resident in India, has paid ₹ 60,000 for medical expenses during the Previous Year 2015-2016 for his wife suffering from cancer. Mrs. Jamal is also resident in India and turns 60 years of age on 31st March 2016. The full treatment cost has been reimbursed by the General Insurance Corporation of India. Please determine if Mr. Jamal is entitled to any deduction under Sec. 80DDB and if the answer is yes, determine the quantum of deduction. Also, please work out the quantum of deduction in the following circumstances :

I. Mrs. Jamal turns 60 years of age on 1 April 2016 and the amount reimbursed by the insurer is ₹ 25,000. Payment of medical treatment was made out of exempted income.

II. Mr. Jamal turns 60 years of age on 1 April 2015 but Mrs. Jamal is 59 years, 11 months and 30 days as on 31 March 2016 and the insurer has not reimbursed any expenditure.

III. Mrs. Jamal is 61 years of age, a non-residential in India and the insurer has reimbursed ₹ 35,000

IV. Mr. Jamal, though having assessable income in India, is actually resident in Sri Lanka and is getting his wife treated in India for sake of better and more advanced medical facilities Mrs. Jamal is residential in India and the insurer has reimbursed ₹ 20,000.

V. The expenditure is incurred by the assessee on cancer treatment of his 25 year old grandson who is dependent on him and is resident in India. The insurer has not reimbursed the claim.

VI. Mr. Jamal is able to produce the receipt of the medical expenditure only to the extent of ₹ 10,000 as he misplaced other receipts and the certificate in Form 10-I regarding the treatment of his wife does not mention the total amount incurred by him during the Previous Year. The insurer has reimbursed only ₹ 5,000.

Solution :

Amount of deduction under Sec. 80DDB : PY 2015-2016 / AY 2016-2017

Particulars	Existing	I	II	III	IV	V	VI
Gross deduction u/s 80DDB in respect of specified ailment of dependant wife.	60,000	40,000	40,000	40,000	Nil	Nil	10,000
Less : Insurance claim received	60,000	25,000	Nil	35,000	20,000	Nil	5,000
Net deduction allowable u/s 80DDB	**Nil**	**15,000**	**40,000**	**5,000**	**Nil**	**Nil**	**5,000**

Working Notes :

1. In order to be a senior citizen, a person should be a resident in India and be 60 years of age at any time during the Previous Year, be it one the last day of the Previous Year or at any time during the Previous Year. Therefore, except when Mrs. Jamal turns 60 after the end of the Previous Year or when she is a non-resident in India, the gross amount of deduction will be ₹ 40,000.
2. The assessee individual must be resident in India in order to be eligible to the deduction.
3. A grandson is not covered by the definition of "dependant".
4. Form No. 10-I does not require the doctor to certify the amount incurred.

Illustration 3 : Mr. C, manager of L Ltd., has paid ₹ 38,000 during the Previous Year 2015-2016 by way of medical insurance under GIC approved medical policies. The details are given as below:

(i) For himself ₹ 6,000

(ii) For Mrs. C, a Canadian citizen, resident in Toronto and not dependent on him ₹ 5,000

(iii) For B, married son living with him and dependent on him ₹ 3,000

(iv) For D, minor son resident in Toronto and not dependent on him ₹ 3,000

(v) For Mrs. B, daughter-in-law, dependent on him ₹ 5,000

(vi) For E, a minor grandson dependent on him ₹ 3,000

(vii) For K, father, 67 years, resident and dependent on him ₹ 3,000

(viii) For M, mother, 66 years, resident in Toronto and dependent on him ₹ 6,000

(ix) For Grandfather, dependent on him, 95 years of age and resident in India ₹ 4,000.

C has earned gross salary of ₹ 2,50,000 during the year and also earns ₹ 95,000 as interest from 7% Capital Investment Bonds, purchased on 31 May 2005. Compute his eligible deduction u/s 80D for the Previous Year 2015-2016 assuming the following situations:

I. Premium is paid by cheque from his salary income.

II. Premium is paid in cash from his salary income. He holds a valid receipt for cash payment.

III. Premium is paid by cheque out of interest from 7% Capital Investment Bonds, acquired on 31-5-2005.

IV. Premium is paid in cash out of interest from 7% Capital Investment Bonds, acquired on 1-6-2005.

Solution :

Computation of Deduction for Medical Insurance Premium u/s 80D

Particulars of Medical Insurance premium paid	**I** ₹	**II** ₹	**III** ₹	**IV** ₹
For himself	6,000	Nil	Nil	Nil
For Mrs. C, a Canadian citizen, resident in Toronto and not dependent on him	5,000	Nil	Nil	Nil
For B, married son living with him and dependent on him	3,000	Nil	Nil	Nil
For D, minor son resident in Toronto and not dependent on him	Nil	Nil	Nil	Nil
For Mrs. B, daughter-in-law, dependent on him	Nil	Nil	Nil	Nil
For E a minor grandson, dependent on him	Nil	Nil	Nil	Nil
For K, father, 67 years, resident in India, a senior citizen and dependent on him	3,000	Nil	Nil	Nil
For M, mother, 66 years, resident in Toronto -not a senior citizen but dependent on him	6,000	Nil	Nil	Nil
For Grandfather, 95 years of age, dependent on him, resident in India, and senior citizen (not a parent, hence not eligible)	Nil	Nil	Nil	Nil
Eligible premium for Deduction u/s 80D	23,000	Nil	Nil	Nil

Working Notes :

1. Medical insurance premium on spouse's health is always eligible irrespective of whether the spouse is dependent on the assessee or not. The condition of dependency applies only in case of children and parents.

2. Medical premium on health of grandson, grandparents, daughter-in-law or son-in-law are not eligible for deduction u/s 80D.

3. Only the premium on health of dependent father will qualify for relaxation as a senior citizen. Since dependent mother is non-resident and, therefore, outside the purview of being a "senior citizen". However, the premium for health of mother will qualify for the normal limit irrespective of the residential status.

4. Any premium paid in cash or by cheque or out of exempted income does not quality for deduction u/s 80D.

Illustration 4 : Mr. Maity, a resident individual, furnishes the following particulars of his income/expenditure for the Previous Year 2015-2016 :

		₹
(i)	Gross Salary	3,00,000
(ii)	Income from House Property	1,70,000
(iii)	Share of profit from an AOP	25,000
(iv)	Long-term Capital Gain	50,000

He has paid medical insurance on his life, his wife and his dependent children. Total premium paid under GIC approved policies is ₹ 10,000 but a sum of ₹ 1,000 was paid in cash due to a prolonged bank clearing strike. He has spent ₹ 20,000 on the treatment of his brother, a dependant with disability. He has also deposited ₹ 25,000 with a specified company u/s 2(h) of Unit Trust of India (Transfer of Undertaking and Repeal) Act, 2003 for maintenance of his brother.

He has paid the following donations during the year:

Particulars of donations made during the year	₹
• Donation to P.M.'s National Relief Fund	10,000
• Donation to Jamia Milia University	5,000
• Donation to National Cultural Fund, set up by Central Government	5,000
• Donation to Delhi Municipal Corporation for Family Planning	12,000
• Donation to Birla Temple (notified):	
(i) for repair and renovation of the temple	2,000
(ii) for religious ceremonies, prasad, etc. for the benefit of devotees in general	5,000
• Donation to a temple managed by the Residents Welfare Association for its much needed repair and maintenance. The Association is a non-profit entity registered with the Registrar of Societies.	5,000
• Following donations to Pt. Pyare Lal Charitable Trust recognised by the Commissioner u/s 80G(5)(vi):	
(i) Donation in form of equity shares of blue chip companies: The shares were sold by the Trust at their market value of ₹ 75,000 and used wholly towards its charitable objectives. However, shares were transferred at cost,	25,000
(ii) Donation paid in cash,	5,000
(iii) Donation made by cheque,	7,000
(iv) 50 blankets costing ₹ 100 each.	5,000
• Donation made to Indian Olympic Association 80G(2)(c) paid by A/c payee cheque,	7,500
• Donation for developing low cost homes for slum-dwellers, paid	
(i) Delhi Development Authority,	3,000
(ii) Delhi Slum-dwellers Rehabilitation Society duly registered with the Registrar,	2,500
• The Rajiv Gandhi Foundation	6,000
• National Children's Fund	3,000

Mr. Maity borrowed a sum of ₹ 2,00,000 in 2004 @9% interest from Harsh Vardhan Charitable Trust (registered under Sec. 80G) to complete his B.Tech. degree from Nalanda University. In March 2016, he repaid a sum of ₹ 75,000 (including ₹ 20,000 interest) to the said trust.

Compute his Total Income for the Assessment Year 2016-2017.

Solution :

Computation of Total Income of Mr. Maity for the Assessment Year 2016-2017

Particulars	₹	₹
1. Income from Salary		3,00,000
2. Income from House Property		1,70,000
3. Share of profits from an AOP : Exempt (Sec. 86)		Nil
4. Long-term Capital Gains		50,000
Gross Total Income		**5,20,000**
5. Deduction from Gross Total Income :		
(i) Medical insurance premium (Sec. 80D)	9,000	
(ii) Expenditure on medical treatment and deposit for maintenance of a handicapped dependent relative (Sec. 80DD)	75,000	
(iii) Repayment of interest on loan for higher studies (Sec. 80E) (No deduction is allowed for repayment of principal amount of educational loan w.e.f. A.Y. 2008-2009)	20,000	
	1,04,000	
(iv) Charitable donations Sec. 80G – [See Note below]	44,000	**1,48,000**
Total Income		**3,72,000**

Working Note :

	₹	₹
Goss Total Income		5,20,000
Less : Aggregate of :		
(i) Share of profit in AOP entitled to rebate u/s 86.	Nil	
(ii) Any amount qualifying for deduction from GTI exempt for deduction for donation u/s 80G itself.	1,04,000	
(iii) Long-term Capital Gain	50,000	
(iv) Any to a NRI from dividend and interest etc. on foreign currency investment referred to u/s 115A, 115AB, 115AC, 115ACA, 115AD.	Nil	1,54,000
Adjusted Gross Total Income		**3,66,000**

Computation of Deduction for Donations u/s 80G

	₹	₹
A. Donations not subject to qualifying amount, eligible for deduction @ 100% of the amount donated :		
(i) Donation to P.M.'s National Relief Fund	10,000	
(ii) Donation to National Cultural Fund, set up by Central Government	5,000	
(iii) National Children's Fund	3,000	18,000
B. Donation not subject to qualifying amount, eligible for deduction @50% of the amount donated :		
The Rajiv Gandhi Foundation	6,000	
Only 50% of the amount of donation available as deduction	6,000	3,000
C. Donation subject to qualifying amount :		
(i) Donation to Delhi Municipal Corporation for Family Planning	12,000	
(ii) Donation made to Indian Olympic Association 80G (2)(C) (available only to a company assessee)	Nil	
(iii) Donation to Jamia Milia University	5,000	
(iv) Donation to Birla Temple (notified) for repair and renovation of the temple.	2,000	
(v) Monetary donation to Pt. Pyare Lal Charitable Trust recognized by the Commissioner u/s 80G (5) (vi).	12,000	
(vi) Donation to Delhi Development Authority	3,000	
Aggregate of donations subject to qualifying amount	**34,000**	
Qualifying amount :		
Lower of the following :		
(a) 10% of Adjusted Gross Total Income, i.e. ₹ 36,600, or		
(b) Aggregate of donations, ₹ 34,000		
Whichever is less, is qualifying amount = 34,000		
100% of ₹ 12,000 out of the QA of 34,000	12,000	
50% of the balance of the QA i.e. 50% of (34,000-12,000)	11,000	23,000
Total deduction for donations u/s 80G		44,000

1. Medical Insurance Premium paid in cash is not allowable as a deduction.
2. Donation to a notified temple is allowed only if it is towards its repairs or maintenance and not otherwise.
3. Only donations paid in monetary terms that is, either in cash or by cheque are eligible for deduction. Conversion of donations in kind into cash by the donee or mere possibility of their conversion is immaterial.
4. Temple managed by the Resident Welfare Association is not a notified temple.

Illustration 5 : Mr. Jamal, a resident assessee, runs a manufacturing business in Delhi. For the Previous Year 2015-2016, he disclosed his Taxable Income as below:

	₹
Business Profits	2,55,000
Long-term Capital Gains	25,000
Short-term Capital Gain	15,000

He has hired furnished accommodation for his own use and pays ₹ 4,000 p.m. He has paid donation amounting to ₹ 10,000 to National Defence Fund. He has deposited ₹ 50,000 under a scheme framed by the Life Insurance Corporation for maintenance of his dependant brother with a disability. The disability is certified by the medical authority. Compute his Total Income for the Assessment Year 2016-2017.

Solution :

Computation of Total Income of Mr Jamal — Assessment Year 2016-2017

Particulars	₹	₹
Income from Business (computed)		2,55,000
Long-term Capital Gain (computed)		25,000
Short-term Capital Gain (computed)		15,000
Gross Total Income		2,95,000
Deductions from Gross Total Income:		
(i) Deposit for maintenance of a dependent with disability [Sec. 80DD]	75,000	
(ii) Charitable donations to National Defence Fund [Sec. 80G]:		
Amount of Deduction @ 100% of ₹ 10,000	10,000	
	85,000	
(iii) Expenditure incurred on rent [Sec. 80GG] [W.N.1]	24,000	1,09,000
Total Income		1,86,000

Workings Note :

Particulars	₹	₹
Expenditure incurred on rent [Sec. 80GG]:		
• [Rent paid -10% of AGTI], i.e. 48,000 – 18,500 = 29,500, or		
• 25% of AGTI, i.e. 25% of 1,85,000 = 46,250, or		
• ₹ 2,000 p.m. = ₹ 24,000		
whichever is less, is to be deducted, i.e. ₹ 24,000		
Adjusted Gross Total Income for Sec. 80GG:		2,95,000
Gross Total Income		
Less: Aggregate of		
2. All permissible deduction from GTI except for deduction for u/s 80GG	85,000	
(ii) Any Long-term Capital Gain	25,000	1,10,000
Adjusted Gross Total Income [AGTI] for Sec. 80GG		**1,85,000**

Illustration 6 : M, resident in India, furnishes the following particulars of his receipts and outgoings during the Previous Year 2015-2016.

		₹
Receipts:		
(i)	Income from Salary	2,00,000
(ii)	Income from House Property	3,00,000
(iii)	Gross winning from crossword puzzle	3,50,000
Outgoing :		
(i)	Contribution to LIC annuity plan	15,000
(ii)	Medical insurance premium:	
	(a) For himself	4,000
	(b) His wife, not dependent	3,000
	(c) Mother, non-resident, 67 years, dependent	5,000
	(d) Nephew, wholly dependent with disability	3,000
	(e) Grandson, dependent	2,000
(iii)	Expenditure on medical treatment and maintenance of the nephew referred to	30,000
(iv)	Medical treatment for grandson, suffering from a disease specified under Income-tax Rules(v)	50,000
(v)	Donation to Gujarat Government for family planning	50,000
(vi)	Scholarship to a poor but meritorious student	20,000
(vii)	Contribution to approved scientific research association	30,000
(viii)	Contribution to Delhi Municipal Corporation for sewage scheme for slum-dwellers, approved by National Committee	50,000
(ix)	Donation to Political party paid during November 2015	20,000

Compute his Total Income for the Assessment Year 2016-2017. Make necessary assumptions and clarify them.

Solution :

Computation of Total Income for AY 2016-2017

Particulars		₹	₹
Income from Salary			2,00,000
Income from House Property			3,00,000
Gross winnings from crossword puzzle			3,50,000
Gross Total Income			**8,50,000**
Less: Deductions under Chapter VIA :			
Contribution to LIC annuity plan [Sec. 80CCC]		15,000	
Medical insurance premium [Sec, 80D]			
Self	4,000		
His wife	3,000		
Mother, 67 years old	5,000		
Nephew dependent with disability	Nil		
Grand son	Nil	12,000	
Maintenance and medical treatment of a dependent with disability [Sec. 80DD]		Nil	
Expenditure for medical treatment of grandson [Sec. 80DDB]		Nil	
Donations for scientific research or rural development [Sec. 80-GGA]			
(a) Donation to approved scientific research association		30,000	
(b) Contribution to MCD for slum-dwellers scheme, approved by National Committee		50,000	
Donations to political party [Sec. 80GGC w.e.f. 22.9.2004]		20,000	
Charitable donations [Sec. 80G]			
(a) Scholarship to a poor meritorious student		Nil	
(b) Gujarat government for family planning: 100% of qualifying amount			
1. Actual donation = 50,000, or			
2. 10% of specified GTI = 37,300			
8,50,000 – (3,50,000 + 15,000 + 12,000 + 30,000 + 50,000 + 20,000) = ₹ 3,73,000			
whichever is less, is QA 37,300= 100% of 37,300		37,300	1,64,300
Total Income			**6,85,700**

Illustration 7 : SK Industries, a diversified group, discloses profit from the following sources for the Previous Year 2015-2016 :

		(₹ in lakhs)
(i)	Profits from industrial undertaking located in backward district notified by Central Govt. (Catagory A), started in 2004-2005	6.00
(ii)	Profit from industrial undertaking 1999-2000, in Vidisha, a B-class industrially backward district.	10.00
(iii)	Profit from multiplex theatre, started in 2008-2009	
	(a) Delhi	4.00
	(b) Allahabad	2.00
(iv)	Profits from convention centre, started in 2010-2011	
	(a) Delhi	5.00
	(b) Allahabad	3.00

(v) Profits from Hill View, a hotel started in 2005-2006 at Manali in Himachal Pradesh. Hotel is approved by prescribed authority — 10.00

(vi) Profits from undertakings engaged in refining of mineral oil since 1st January 2008 in Uttar Pradesh, not listed in backward state in Eighth Schedule. — 10.00

Compute the Total Income for the Assessment Year 2016-2017.

Solution : **Computation of Total Income**

Assessee: S.K Industries **Previous Year-2015-16** **Assessment Year- 2016-17**

Particulars	**(₹ lakhs)**	**(₹ lakhs)**
(i) Profits from industrial undertaking located in backward district		6.00
(ii) Profits from undertaking located in industrially backward B-class district		10.00
(iii) Profits from multiplex theatre: (4 + 2)		6.00
(iv) Profits from convention centre: (5+3)		8.00
(v) Profits from Hill View Hotel		10.00
(vi) Profits from refining undertaking		10.00
Gross Total Income		**50.00**
Less : Deduction in respect of profits and gains from certain industrial undertaking, other than infrastructure undertakings (Sec. 80-IB) :		
1. Profits from industrial undertaking located in backward district [Sec. 80-IB] [No deduction is available]	Nil	
2. Profits from undertaking in B-class industrially backward district [Sec. 80-IB (4)] [No deduction is available]	Nil	
3. Profits from multiplex theatre [Sec. 80-IB(7A) 50% of ₹ 2 lakh (No deduction is available)	Nil	
4. Profits from convention centre [Sec. 80-IB(7B)] [No deduction is available]	Nil	
5. Profits from Hill View Hotel [Sec. 80-IB(7)] Allowed only for Indian company	Nil	
6. Profits from refining undertaking [Sec. 80-IB(9)]-100% of profits for 7 Assessment Years	10.00	**10.00**
Total Income		**40.00**

Illustration 8 : Mekon Ltd., an Indian company, starts an industrial undertaking on 1st April, 2015. During the Previous Year, it earns profits of ₹ 80 lakh before allowing any deduction for wages. Compute its Total Income for the Previous Year 2015-2016 taking into account the following employment schedules of workers:

Date of employment	**Number of workers**	**Status of workers**	**Rate of wages**
1-5-2015	90	Regular	3000 p.m.
1-6-2015	20	Regular	4000 p.m.
1-7-2015	10	Regular	4000 p.m.

Solution :

Computation of Total Income for the AY 2016-2017

Particulars	₹	₹
Profits before allowing deduction for wages		80,00,000
Less: Wages paid to workers [Sec. 37(1)] :		
(i) 90 × ₹ 3000 × 11	29,70,000	
(ii) 20 × ₹ 4000 × 10	8,00,000	
(iii) 10 × ₹ 4000 × 9	3,60,000	(-) 41,30,000
Business Profits and Gross Total Income		38,70,000
Less: Deduction in respect of employment of new regular workmen U/s Sec. 80 JJAA - 30% of earned wages in excess of 50 regular workmen:		
1.5.2015 – 40 regular worker [₹3,000 × 40×11× 30%] = 3,96,000		
1.6.2015 – 20 regular worker [₹4,000 × 20×10× 30%] = 2,40,000		
1.7.2015 – Nil, as employed for less than 300 days = Nil		(-) 6,36,000
Total Income		32,34,000

Illustration 9 : Mr. R has developed an improved economical model of a motor cycle and got it patented on 31-3-2015 under the Patent Act, 1970. He allowed Z Ltd. to use his patent rights and licenses has been granted to it under the Patent Act, 1970. He has received royalty of ₹ 8,00,000 during the Previous Year 2015-2016. However, the royalty in accordance with the terms and conditions of the license settled by the Controllers under the said Act is ₹ 2,80,000.

He has incurred ₹ 1,00,000 expenses in developing his invention and getting it patented.

Compute his Total Income for the Assessment Year 2016-2017 (i) if he is resident in India, (ii) non-resident India.

Solution : **Computation of Total Income for the Assessment Year 2016-2017**

Particulars	**(i)** ₹	**(ii)** ₹
Income from Other Sources	8,00,000	8,00,000
Less : Expenses	1,00,000	1,00,000
Gross Total Income (GTI)	7,00,000	7,00,000
Less: Deduction for respect of royalty on patent (Sec. 80-RRB)		
Least of the followings:		
(a) Income from royalty ₹ 8,00,000; or		
(b) Royalty under the terms of license settled by the		
Controller ₹ 2,80,000;		
(c) Maximum limit ₹ 3,00,000	2,80,000	Nil
Whichever is less, is to be deducted		
Total Income	**4,20,000**	**7,00,000**

Illustration 10 : Mr. J is suffering with 60% locomotor disability which is certified by medical authority. He is employed as Technical Supervisor with Airtel at a salary of ₹ 20,000 p.m.

	Particulars	₹
(i)	Income from Government securities	20,000
(ii)	Long-term Capital Loss	(-) 40,000
(iii)	Short-term Capital Gain (Sec. 111A)	1,00,000
(iv)	Insurance commission (gross)	1,00,000
(v)	Interest on Saving Fund A/c from Bank	10,000

He has incurred the following expenses:

(i)	Medical insurance paid by cheque for his father, resident in India and 70 years	18,000
(ii)	Deposit with LIC for maintenance of father, mainly dependant on him for support and maintenance and suffering from low-vision with a severe disability of 80%, as per certificate of the medical authority	1,00,000
(iii)	Rent paid for the year 2015-2016 for accommodation hired by him.	40,000

Compute his Total Income for the Assessment Year 2016-2017.

Solution :

Computation of Total Income for the Assessment Year 2016-2017

Particulars	₹	₹
1. Income from Salaries		2,40,000
2. Income from Capital Gains :		
(a) Short-term Capital Gains (Sec. 111A)		1,00,000
(b) Long-term Capital Loss to be carried forward		Nil
3. Income from Others Sources :		
(a) Interest from Government securities	20,000	
(b) Interest on Savings Fund A/c with Bank	10,000	
(c) Insurance commission	1,00,000	1,30,000
Gross Total Income		**4,70,000**
Less : Deductions under Chapter VIA:		
Medical insurance (Sec. 80D)	18,000	
Deduction in respect of maintenance including medical treatment of a dependant, a person with severe disability (Sec. 80DD)	1,25,000	
Deduction in respect of Interest on Savings Fund A/c (Sec. 80TTA)	10,000	
Deduction in case of a person with disability (Sec. 80U)	75,000	
Deduction u/s 80GG : (Least of the followings)		
(a) (i) Rent paid less 10% of Adjusted Gross Total Income 40,000-14,200 = 25,800,		
(b) (ii) 25% of 1,42,000 Adjusted Gross Total Income = 35,500,		
(iii) 2,000 p.m. × 12 = 24,000		
Whichever is less, is or be deducted	24,000	2,52,000
Total Income		**2,18,000**

Illustration 11 : Mr. Krishna is a lawyer of Allahabad High Court. He keeps his accounts on cash basis. His Receipts and Payments A/c for the year ended 31-03-2016 is given below :

Dr. Cr.

Receipts	₹	Payments	₹
Balance b/d	3,820	Purchase of Infrastructure Bonds	20,000
Legal fees	3,45,000	Subscription and membership	4,500
Special commission fees	5,500	Purchase of legal books	17,500
Salary from Law College as part time lecture	87,000	Rent	47,500
		Municipal Tax paid on H. P.	3,000
Exam. Remuneration	1,480	Car expenses	44,000
Interest on Bank Deposit	3,500	Office expenses	38,500
Sale proceeds of residential property	3,01,000	Electricity Exps.	4,000
Dividend from Co-operative society	1,000	Income Tax	8,000
Dividend received from the units of UTI	2,000	Gift to daughter	12,000
		Domestic expenses	85,000
Rent from house property	15,000	Donation to Institutions approved u/s 80G	12,000
		Car purchased	3,27,000
		Life Insurance premium	16,000
		Balance c/d	1,26,300
	7,65,300		7,65,300

Following information are available :

1. The Rent and Electric expenses are related to a house, of which half portion in used for self residence and remaining half portion in used for office.
2. Car is used only for professional purposes.
3. Outstanding legal fees ₹ 10,000.
4. Rent has been paid for 10 months only.
5. Car was purchase on 25-09-2015. Law books purchased are annual publications out of which books of ₹ 2,000 were purchasd on 6-4-2015 and balance on 31-10-2015.
6. The house was purchased in January 1988 for ₹ 45,000 and sold on 1-7-2015.
7. Rent of the property which has been sold was ₹ 5,000 p.m. The property was vacated by the tenant on 30-6-2015.

   Compute his Total Income for the Assessment Year 2016-17.

Solution :

Computation of Total Income of Mr. Sen for the Assessment Year 2016-17

Particulars		₹	₹
1. *Income from Salary*			
Salary as a part time lecturer		87,000	
Less: Deduction		Nil	87,000
2. *Income from House Property*			
Annual Rent		60,000	
Less: Vacancy Allowance		45,000	
Gross Annual Value (GAV)		15,000	
Less: Municipality Tax paid		3,000	
Net Annual Value (NAV)		12,000	
Less: Standard deduction @ 30% of NAV		3,600	8,400
3. *Income from Profession*			
Professional Earnings:			
(i) Legal fees		3,45,000	
(ii) Special commission		5,500	
		3,50,500	
Less: Allowable expenses			
(i) Subscription etc.	4,500		
(ii) 1/2 Rent (Office)	23,750		
(iii) Car expenses	44,000		
(iv) 1/2 electric charges	2,000		
(v) Office expenses	38,500		
(vi) Depreciation on car @ 15% on 3,27,000	49,050		
(vii) Depreciation on books :			
@ 100% on Annual Publication of ₹ 2,000 = 2,000			
@ 50% on Others of 15,500 = 7,750	9,750	1,71,550	1,78,950
4. *Capital Gains :*			
Sale consideration		3,01,000	
		3,24,300	
Less: Indexed cost of acquisition $45,000 \times \frac{1081}{150}$		(23,300)	
5. *Income from Other Sources* :		3,500	
Interest on bank deposit		1,480	
Examiner's fees		1,000	
Dividend from Co-operative Society		Exempt	5,980
Dividend from UTI			2,80,330
Gross Total Income			
Less : Deductions			
(i) 80C - LIP		16,000	
(ii) 80G - Donation @ 50% of ₹ 12,000		6,000	
(iii) 80CCF - Purchase of Infrastructure Bonds (discontinued)		Nil	
(iv) 80TTA – Interest on bank deposit (assumed savings deposit)		3,500	25,500
Total Income			2,54,830

Notes :

1. As the assessee follows the cash system of accounting, amount actually received and payment actually made on account of expenditure, during the year, shall be considered for computing the income. Therefore, any outstanding receipts will not be included in the Total Income. Similarly, rent not paid for two months will not be allowed as deduction.
2. The system of accounting does not affect the computation of Income from Salary, House Property and Capital Gains. Therefore, in this case, rent for three months, though not received (as it has not been shown in the Receipt and Payment Account) shall be taken into account in computing the income under the head House Property.
3. Car was purchased and put to use for more than 180 days. Therefore, full depreciation @15% has been claimed.
4. Law books worth ₹ 2,000 were purchased and put to use for more than 180 days and are, therefore, eligible for depreciation @100%. The balance books worth ₹ 15,500 were purchased on 31-10-2015; therefore, 50% of the normal depreciation will be allowed as the books were purchased and put to use for less than 180 days. The total depreciation shall, therefore, be ₹ 2,000 + 50% of ₹ 15,500 = ₹ 9,750.
5. Long term capital loss of ₹6,200 is carried forward for adjustment in subsequent A.Y.

Illustration 12 : Dr. Paul is running a Nursing Home with his wife Dr. (Mrs.) Paul as a partnership firm Paul & Co. On the basis of the following particulars, compute the Total Income of Dr. Paul and Dr. (Mrs.) Paul for the Assessment Year 2016-17.

(A)	Particulars of income of the Nursing Home	₹
(i)	Income as per Income and Expenditure Account	3,20,000
(ii)	Firm’s tax not provided in the account	48,000
(iii)	Dontation to Public Charitable Trust exempt u/s 80G debited in the A/c	35,000

(B) Particulars of Income of Dr. Paul :

(i) 40% of profit from Nursing Home as per books ₹ 1,28,000

(ii) Dr. Paul had purchased 500 shares of Laha (P) Ltd. at ₹ 110 each in May 1991. On 14-5-2015 Dr. Paul sold 300 shares at ₹ 400 per share. He invested ₹ 40,000 out of the net sale proceeds in Bonds of RECL in June, 2015. The balance of 200 shares were sold in December, 2015 at ₹ 380 per share.

(iii) Dr. Paul is a Director in Raha (P) Ltd. from which he received director’s fees amounting to ₹ 4,000.

(iv) Dr. Paul has obtained a loan of ₹ 50,000 from the said company for renovating the Nursing Home. The balance sheet of Raha (P) Ltd. for the Accounting year, *inter alia*, disclosed the following particulars.

(*a*)	General Reserve	40,000
(*b*)	Profit & Loss Account (Cr. Balance)	20,000
		60,000

(v) Share of income from property belonging to HUF of which Dr. Paul is the Karta amounts to ₹ 30,000.

(C)	Particulars of Income of Dr. (Mrs.) Paul :	₹
(i)	60% share of profit from Nursing Home as per books	1,92,000
(ii)	Income from dividend from UTI	18,000
(iii)	Income from house property (as computed under Income-tax Act)	48,000

(D) Particulars of Income of Master Pritam :

Pritam minor son of Dr. Paul and Dr. (Mrs.) Paul has been admitted to the benefits of partnership in Paul & Co. which is carrying on business as Chemists & Druggists. The said firm has two other partners Soham (brother of Dr. Paul) and Priya [sister of Dr. (Mrs.) Paul]. Pritam's share of profits is determined at ₹ 20,000.

Solution :

Computation of Total Income of Paul & Co. **A.Y : 2016-17**

	₹
Income as per Income and Expenditure Account	3,20,000
Add : Donation to public charitable trust	35,000
Gross Total Income	3,55,000
Donation to public charitable trust being restricted to 10% of Gross Total Income (3,55,000) i.e. 50% of ₹ 35,000	17,500
Total Income	3,37,500
Total tax *plus* education cess *plus* SHEC payable by the firm ₹ 1,04,288.	

Computation of Total Income of Dr. Paul **A.Y.: 2016-17**

Particulars	₹	₹
1. His income from the Nursing Home is not taxable. (as tax is already paid by the firm)		Nil
2. **Capital Gains**		
Sale proceeds : 300 shares of ₹ 400 each	1,20,000	
200 shares of ₹ 380 each	76,000	
	1,96,000	
Less : Indexed cost : $55,000 \times \frac{1081}{182}$	3,26,676	
Long term Capital Loss	(–) 1,30,676	
3. Income from other sources :		
(a) Director's fees	4,000	
(b) Deemed dividends u/s 2(22)(e) for having taken a loan from the company in which the assessee has substantial holding	50,000	54,000
Gross Total Income		54,000
Deduction under Chapter VI A		Nil
Total Income		54,000

Computation of Total Income of Dr. (Mrs.) Paul **A.Y.: 2016-17**

	₹
1. 60% share from Nursing Home is not taxable (as tax is already paid by the firm)	Nil
2. Income from house property (net).	48,000
3. Income from other sources — dividends from UTI	Exempt
Gross Total Income	48,000
Less : Deduction under Chapter VI A	Nil
Total Income	48,000

Notes :

1. Share of profit from the firm accruing to minor is not included in the Total Income of parent as share of profit to a partner is exempt.

2. Long-term Capital Loss cannot be set off against other income and therefore has to be carried forward.

Illustration 13 : From the following details compute the Total Income of Mr. X, a resident of Delhi, for the A.Y. 2016-17.

Particulars	₹
(a) Salary including Dearness Allowance	6,30,000
(b) Bonus	57,600
(c) Contribution to a Recognised Provident Fund	36,000
(d) Life Insurance Premium	57,000
(e) Rent paid by the Employer for flat provided to Mr. X	90,000
(f) Cost of Furniture provided by the employer at the aforesaid flat	80,000
(g) Rent recovered from Mr. X by employer	36,000
(h) Bills paid by the employer for gas, electricity and water provided free of cost at the above flat	18,000
(i) Mr. X was provided with Company's car (with driver) also for personal use, not possible to determine expenditure on personal use and all expenses were borne by the employer.	

Particulars	₹
Mr. X owns a house. The particulars are :	
Rent received (12 months)	72,000
Municipal valuation	48,000
Municipal taxes paid	12,000
Ground rent	2,000
Insurance charges	1,000
Collection charges	3,400
Interest on borrowing used for construction of house (constructed in June 2004)	48,000
Other Information :	
Dividend received from UTI	14,000
Deposits under National Saving Certificate	20,000

Solution :

Assessee : Mr. X **Previous Year : 2015-16** **Assessment Year : 2016-17**

Computation of Total Income

Particulars	₹	₹
Income under the head Salary		
Salary including Dearness Allowance		6,30,000
Bonus		57,600
Gross Salary before including value of perquisites		**6,87,600**
Value of Concessional Furnished Accommodation [Rule 3(1)]		
Least of Rent Paid by employer		
[₹ 90,000 or 15% of Salary ₹ 6,87,600]	90,000	
Add : 10% of Furniture Value		
[₹ 80,000 × 10%]	8,000	
Less : Rent recovered from Mr. X	(36,000)	62,000
Gas, Electricity and Water provided by the employer		18,000
Motor Car provided to the employee for use (assumed capacity upto 1.6 liitres) [(₹ 1,800 p.m. + ₹ 900 p.m. for chauffeur) × 12 Months)] as per Rule 3		32,400
Gross Income from Salary		**8,00,000**
Income from House Property :		
Gross Annual Value u/s 23(1) Higher of Municipal Value ₹ 48,000		
or Rent Received ₹ 72,000	72,000	
Less : Municipal Taxes paid	(12,000)	
Net Annual Value	**60,000**	
Less : Deduction		
Standard deduction @ 30% of Net Annual Value u/s 24(a)	(18,000)	
Interest on borrowed capital u/s 24(b)	(48,000)	**(6,000)**
Income from Other Sources :		
Income from UTI	14,000	
Exemption u/s 10(35)	(14,000)	Nil
GROSS TOTAL INCOME		**7,94,000**
Less : Deduction under Chapter VIA - Section 80C		
- Contribution to RPF	36,000	
- LIC Premium	57,000	
- Deposits in NSC	20,000	
	1,13,000	
Deduction u/s 80C restricted to ₹ 1,50,000 [Sec. 80CCE]		(1,13,000)
TOTAL INCOME (Rounded Off u/s 288A)		**6,81,000**

Illustration 14 : Mr. X, Finance Manager of K Ltd. Mumbai, furnishes the following particulars for the Previous Year 2015-2016.

		₹
(a)	Gross Salary (per month)	64,000
	[Tax deducted from Salary ₹ 1,09,000]	
(b)	Valuation of medical facility in a hospital maintained by the Company	7,000
(c)	Rent Free Accommodation owned by the Company	
(d)	Housing Loan of ₹ 6,00,000 at the interest rate of 5% p.a. (no repayment made during the year, to be repaid within 10 years)[Standard Rate of SBI is 10% p.a.]	
(e)	Gift made by the Company on the occassion of wedding anniversary of X	4,750
(f)	A wooden table and 4 Chairs were provided to X at his residence (Dining Table). This was purchased on 1.5.2012 for ₹ 60,000 and sold to X on 1.8.2015 for ₹ 30,000	
(g)	Personal purchases through Credit Card provided by the Company amounting to ₹ 20,000 was paid by the Company. No part of the amount was recovered from X.	
(h)	A Maruti Esteem Car which was purchased by the Company on 16.7.2011 for ₹ 5,50,000 was sold to the assessee on 14.8.2015 for ₹ 1,30,000.	
(i)	Other income received by the assessee during the Previous Year 2015-2016 are :	₹
	Interest on Fixed Deposits with a Company	5,000
	Income from specified mutual fund	3,000
	Interest on bank deposits of a minor married daughter	3,000
	Income from UTI received by his handicapped minor son	1,200
(j)	Contribution to LIC towards Premium u/s 80CCC	10,000
(k)	Deposit in PPF Account made during the year 2015 -2016	75,000
(l)	Bonds of ICICI (Tax Savings) eligible for tax deduction	25,000

Compute the Taxable Income of Mr. X and the tax liability for the A.Y. 2016-2017.

Solution :

Assessee : Mr. X **Previous Year : 2015-16** **Assessment Year : 2016-17**

Computation of Total Income

Particulars		₹	₹
Income from Salaries :			
Basic Salary (₹ 64,000 × 12)			7,68,000
Add : **Value of Perquisities :**			
1. Value of Medical Facility in hospital maintained by K Ltd.			
— Treatment in hospital maintained by Employer — Fully Exempt			Nil
2. Rent Free Accommodation owned by Company — Explanation 1 to Sec.17(2) 15% of salary = 15% of ₹ 7,68,000 (Population > 25 Lakhs)			1,15,200
3. Housing Loans at concessional rate – Rule 3(7)(i) = ₹ 6,00,000 × (10% – 5%)			30,000
4. Use of Furniture & Fittings upto 1.8.2015 - Rule 3(1)(vii) = 10% × ₹ 60,000 × 4/12			2,000
5. Transfer of Assets - Rule 3(7)(viii)			
— Dining Table as per WN 1 (a)		12,000	
Motor Car as per WN 1 (b)		95,280	
			1,07,280
6. Gifts made by the Company on the occasion of the Wedding Anniversary			Nil
7. Credit Card Purchases taxable as perquisite u/s 17(2)			20,000
Gross Income from Salary			**10,42,480**
Less : Deduction u/s 16			Nil
Net Income from Salaries			**10,42,480**
Income from Other Sources :			
Interest on Fixed Deposits with a Company		5,000	
Income from specified mutual fund	3,000		
Less : Exempt u/s 10(35)	(3,000)	Nil	
Interest on Bank Deposits of minor married daughter	3,000		
Less : Exempt u/s 10(32)	(1,500)	1,500	
Income received by handicapped minor son - not clubbed u/s 64(IA)		Nil	6,500
GROSS TOTAL INCOME			**10,48,980**
Less : **Deduction under Chapter VI-A**			
U/s 80CCC – Contribution towards Pension Fund		10,000	
U/s 80C – Contribution towards PPF		75,000	
– Bonds of ICICI (Tax Savings)		25,000	
		1,10,000	
TOTAL INCOME			1,10,000
TAX PAYABLE			**9,38,980**
Add : Education Cess @ 2%			**1,12,796**
Add : Secondary and Higher Education Cess @ 1%			2,256
Gross Tax Payable			1,128
Less : Tax Deducted at source			**1,16,180**
Net Tax Liability			1,09,000
			7,180

Working Notes :

1. **Valuation of Perquisites on transfer of Movable Assets :**

(a)	**Transfer of Assets : Dining Table**	(₹)
	Purchase Price	60,000
	Less : Depreciation till date of Sale	
	(₹ 60,000 × 3 × 10%)	(18,000)
	WDV as at date of transfer	42,000
	Less : Deduction for collection from Employee	(30,000)
	Value of Perquisite	**12,000**
(b)	**Motor Car**	₹
	Cost of Purchase (16.7.2011)	5,50,000
	Less : Depreciation @ 20% (16.7.2011 - 15.7.2012)	1,10,000
	16.7.2012 WDV	4,40,000
	Less : Depreciation for 16.7.2012 - 15.7.2013	88,000
	16.7.2013 WDV	3,52,000
	Less : Depreciation for 16.7.2013 - 15.7.2014	70,400
	16.7.2014 WDV	2,81,600
	Less : Depreciation for 16.7.2014 - 15.7.2015	56,320
	16.7.2015 WDV	2,25,280
	Less : Amount Recovered on Transfer	1,30,000
	Value of Perquisite	**95,280**

2. Gifts received from the employer on the occasion of the wedding anniversary
   (a) Taxable as perquisite u/s 17(2).
   (b) As per Rule 3(7)(vi), value of any gift or voucher or token (other than made in cash) or convertible ; in cash on ceremonial occasion or otherwise shall be taxable if the the aggregate value of Gift during the Previous Year is ₹ 5,000 or more. Since the value of gifts received is less than ₹ 5,000, it shall be exempt from tax.

3. As the total income of Mr. X is more than ₹ 5,00,000, rebate u/s 87A is not available.

Illustration 15 : M, an individual, retired from the services of a Company on 31.10.2015. He joined another employer on 1.11.2015 and was in service till end of March 2016, when he furnishes the following details and information —

1. Salary and Allowances for the period

From First Employer	₹ Per month
Basic Salary	30,000
Dearness Allowance	16,000
Conveyance Allowance	6,000
From Second Employer	₹ Per month
Basic Salary	35,000
Fixed Conveyance Allowance	8,000

2. While he was with the first employer, M contributed 10% of his basic salary to a Provident Fund Account with the Regional Provident Fund Commissioner. He did not become a member of the Provident Fund maintained by the second employer.

3. M was permitted by the second employer to encash 15 days leave he had accumulated during his service and received ₹ 12,500 from his employer.

4. M had constructed a residential house in Chennai in February 2011 for ₹ 30 Lakhs. Part of the costs of construction was met by borrowals of ₹ 20 lakhs from the Housing Development Corporation, at interest of 12.5% p.a. The loan was taken on June 2010. The loan outstanding at the beginning of the current year was ₹ 12,00,000. The rate of interest applicable for the current year was reduced to 9% p.a. due to reduction in rates. He had also borrowed from some relatives ₹ 4,00,000 on which interest at 15% p.a. was due. The property had been let-out soon after completion.

5. In the Assessment Year 2011-12, M was allowed a deduction of ₹ 50,000 for irrecoverable rents. The annual value decided by the Corporation of Channai for the property is ₹ 80,000. The property was let-out in the current year to a Company on a rent of ₹ 20,000 p.m. The half-yearly municipal taxes on the property were fixed by the Corporation of Channai only in August 2015 at ₹ 15,000 for every half year from 1.4.2012. M paid the taxes due in September 2015 upto the year ending 31.3.2015.

6. M also received from the previous tenant ₹ 40,000 (out of the dues of ₹ 50,000).

7. After retirement from the first employer, M received ₹ 4,50,000 from the Regional Provident Fund Commissioner, money was fully invested by him in the 15% Non-Redeemable Debentures issued by the Indian Oil Corporation interest on these had not come in by the end of March 2016.

8. M received interest of ₹ 60,000 on long-term fixed deposits with Banks, ₹ 2,500 as interest on Post Office Savings Bank Accounts and ₹ 20,000 as income from units.

9. M owns a car which is used for office purposes also and it is found that the entire conveyance allowance from his employer had been fully spent on travel for official purposes.

10. One of the policies of insurance taken by M had matured for payment and ₹ 8,00,000 received by him in June 2015 from the LIC was invested by him, in the name of his 16-year old son, in fixed deposits with companies. Interest received uplo 31.3.2016 on these deposits was ₹ 90,000. On one of the continuing policies of insurance, M paid a premium of ₹ 60,000 in the year.

Compute M's Total Income for the Assessment Year 2016-17.

Solution :

Assessee : Mr. M **Previous Year : 2015-16** **Assessment Year : 2016-17**

Computation of Total Income

		₹	₹	₹
Income under the head Salaries				
From First Employer				
Basic Pay	(₹ 30,000 × 7)		2,10,000	
Dearness Allowance	(₹ 16,000 × 7)		1,12,000	
Conveyance Allowance	(₹ 6000 × 7)	42,000		
Less: Exempt u/s 10(14)		(42,000)	Nil	3,22,000
Amount received from Regional Provident Fund Commissioner		4,50,000		
Less: Exempt u/s 10(12)		(4,50,000)	Nil	

From Second Employer			
Basic Salary (₹ 35,000 × 5)		1,75,000	
Conveyance Allowance (₹ 8,000 × 5)	40,000		
Less: Exempt u/s 10(14) (incurred for official performance of duties)	(40,000)	Nil	
Leave Encashment - Fully taxable while in service		12,500	1,87,500
Gross Income from Salary			**5,09,500**
Income from House Property :			
Gross Annual Value u/s. 23(1) — Higher of Municipal Value of ₹ 80,000 or Actual Rent of ₹ 2,40,000		2,40,000	
Less: Municipal Taxes paid during the year @ ₹ 15,000 for every half year from 1.4.2012 upto 31.3.2015		(90,000)	
(Current Year - Not Paid)			
Net Annual Value (NAV)		1,50,000	
Less: Deduction			
@ 30% of NAV u/s 24(a)		(45,000)	
Interest on Borrowed Capital u/s 24(b)			
Loan from Housing Development Corporation:			
Current Period Interest: ₹ 12,00,000 × 9%	1,08,000		
Prior Period Interest (Interest upto 31.3.2011)			
[(₹ 20,00,000 × 12.5%) +(4,00,000 × 15%)] × 10/12 × 1/5	51,667		
Loan from Relative - Current Period Interest			
(₹ 4,00,000 x 15%)	60,000	(2,19,667)	
Add: Unrealised Rent recovered (taxable in the year of recovery u/s 25AA]		40,000	**(74,667)**
Income from Other Sources			
Interest on Long-term Fixed Deposits with Bank		60,000	
Interest on Post Office Savings Bank A/c	2,500		
Less: Exempt u/s 10(15)	(2,500)	Nil	
Income from Units of UTI	20,000		
Less: Exempt u/s. 10(35)	(20,000)	Nil	
LIC Policy matured	8,00,000		
Less: Exempt u/s. 10(1D)	(8,00,000)	Nil	
Interest from Fixed Deposits with Companies in the name of minor son	90,000		
Less: Exemption u/s. 10(32)	(1,500)	88,500	**1,48,500**
Gross Total Income			**5,83,333**
Less: Deduction under Chapter VIA:			
u/s 80C – LIC Premium		(60,000)	
– RPF – 10% of ₹ 2,10,000		(21,000)	81,000
Total Income			**5,02,333**
Total Income (Rounded Off u/s 288A)			**5,02,330**

Assumptions :

1. It is presumed that Mr. M accounts for his interest income on receipt basis.
2. Assumed that there has been no repayment of Housing Loan Principal during the year ending 31.3.2010 for the purpose of calculation of prior period interest.
3. Recognised Provident Fund received on retirement shall not be taxable u/s 10 (assuming conditions are satisfied).
4. **Unrealised Rent recovered :** Since the assessee has been allowed a deduction of ₹ 50,000 from his house property income in ealier years in respect of Unrealised Rent, entire ₹ 40,000 recovered during current year becomes taxable.
5. **Deduction of Interest** u/s 24 shall be allowed even if the amount is borrowed from any person other than the Banks/Financial Institutions in respect of Let Out property.

Ilustration 16 : Mr. A, a Senior Citizen, has furnished the following particulars relating to his House Properties —

Particulars	**House I — ₹**	**House II — ₹**
Nature of Occupation	Self Occupied	Let-out
Municipal Valuation	60,000	1,20,000
Fair Rent	90,000	1,50,000
Standard Rent	75,000	1,40,000
Actual Rent per month	—	12,000
Municipal Taxes paid	6,000	12,000
Interest on Capital borrowed	90,000	80,000

Loan for both Houses were taken on 1.4.2009. House II remained vacant for 4 months.

Besides the above two house, A has inherited during the year 1989-90 an old house from his grandfather. Due to business commitments, he sold the house for a sum of ₹ 250 Lakhs during the year. The house was purchased in 1963 by his grandfather for a sum of ₹ 2 Lakhs. However, the Fair Market Value as on 1.4.1981 was ₹ 30 Lakhs. With the sale proceeds, A purchased a new house in March 2016 for a sum of ₹ 140 Lakhs and the balance was used in his business.

The other income particulars of Mr. A besides the above are as follows (AY 2016–2017) —

- Business Loss ₹ 12 Lakhs
- Income from Other Sources (Bank Interest) ₹ 1 Lakh
- Investments made during the year PF ₹ 70,000
- ICICI Infrastructure Bond Purchased ₹ 30,000

Compute Total Income of Mr. A and his Tax Liability for the Assessment Year 2016–2017.

Solution :

Assessee : Mr. A **Previous Year : 2015-16** **Assessment Year : 2016-17**

Computation of Total Income

Particulars		₹	₹
1. Income from House Property :			
(a) **House I :** Self Occupied — Annual Value u/s 23(2)	Nil		
Less : Deduction u/s 24(b) = Interest on Housing Loan			
taken on 1.4.2009 (Note 3)	90,000	(90,000)	
(b) **House II :** Let-out – (Note 6)		(21,200)	(1,11,200)
2. Profits and Gains of Business or Profession – Loss			(12,00,000)
3. Capital Gains — Sale of Residential House Property — Long Term Asset			
Sale Consideration		2,50,00,000	
Less : Expenses on Transfer		Nil	
Net Consideration		2,50,00,000	
Less : Indexed Cost of Acquisition — Fair Market Value as on 1.4.81 × CII of year of Sale /CII of year of first holding (₹ 30 Lakhs × $\frac{1081}{161}$)		2,01,42,857	
Long Term Capital Gain		48,57,143	
Less : Exemption u/s 54 — New House purchased		(1,40,00,000)	
			Nil
4. Income from Other Sources : Bank Interest			1,00,000
Gross Total Income (assuming this balance is out of Income from other sources only)			**(12,11,200)**
Less : Deduction under Chapter VI-A			
u/s 80C – Deposits in PPF		70,000	
u/s 80TTAA – Interest on Savings Bank Interest		10,000	
However, i.e. Deduction restricted upto the balance of Gross Total Income		80,000	
			Nil
Total Income			**(12,11,299)**

Notes :

1. Assumed that loss from House Property & Loss from Business are at first adjusted inter-head, against Long Term Capital Gains and then against Income from Other Sources since it is beneficial to the assessee.
2. Deduction under Chapter VIA cannot be done against LTCG.
3. It is assumed that the construction of the house was completed **within 3 years** from the end of the financial year in which the loan was taken.
4. Deduction in respect of Investment in Long Term Infrastructure Bond u/s 80CCF is discontinued.
5. It is assumed that Bank Interest represents Interest from Savings Bank Account.

6. **Annual Value of House Property II** is computed as under —

(i)	Municipal Value (MV)	1,20,000
(ii)	Fair Rental Value (FRV)	1,50,000
(iii)	Higher of MV + FRV	1,50,000
(iv)	Standard Rent	1,40,000
(v)	Reasonable Expected Rent (RER) [lower of (iii) + (iv)]	1,40,000
(vi)	Annual Rent @ ₹ 12,000 pm	1,44,000
(vii)	Unrealised Rent	Nil
(viii)	Actual Rent [(vi) – (vii)] [Higher than RER]	1,44,000
(ix)	Vacancy Allowance $\left[\frac{1,44,000}{12}\times 4\right]$	48,000
(x)	Gross Annual Value [(viii) – (ix)]	96,000
	Less : Municipal Tax paid	12,000
	Net Annual Value (NAV)	**84,000**
	Less : Standard deduction @ 30% of NAV u/s 24(a)	25,200
	Less : Interest on borrowed Capital u/s 24(b)	80,000
	Income for House II	**(21,200)**

Illustration 17 : Mr. Ashok a senior citizen, owns a property consisting of two blocks of identical size. The first block is used for business purposes. The other block has been let out from 1.4.2015 to his cousin for ₹ 20,000 p.m. The cost of construction of each block is ₹ 5 lacs (fully met from bank loan), rate of interest on bank loan is 10% p.a. The construction was completed on 31.3.2014. During the year ended 31.3.2015, he had to pay a penal interest of ₹ 2,000 in respect of each block on account of delayed payments to the bank for the borrowings. The normal interest paid by him in respect of each block was ₹ 42,000. Principal repayment for each block was ₹ 23,000. An identical block in the same neighbourhood fetches a rent of ₹ 25,000 per month. Municipal Tax paid in respect of each block was ₹ 12,000.

The income from business prior to adjustment towards depreciation on any asset is ₹ 2,20,000. He follows Mercantile System of Accounting. Depreciation on equipments used for business is ₹ 30,000.

On 23.2.2016, he sold shares of B Ltd., a listed share in BSE for ₹ 2,30,000. The share had been purchased 10 months back for ₹ 1,80,000. Security transaction tax paid may be taken as ₹ 220.

Brought forward business loss of a business discontinued on 12.1.2013 is ₹ 90,000. This loss has been determined in pursuance of a return of income filed in time and the current year is the seventh year.

The following payments were affected by him during the year :

1. LIP of ₹ 20,000 on his life and ₹ 12,000 for his son aged 22, engaged as a software engineer and drawing salary of ₹ 25,000 per month.
2. Mediclaim premium of ₹ 6,000 for himself & ₹ 5,000 for above son. The premiums were paid by cheque.

You are required to compute the Total Income for the Assessment Year 2016-17 and the tax payable. The various heads of income should be properly shown. Ignore the interest on bank loan for the period prior to 1.4.2015, as the bank had waived it.

Solution :

Computation of Total Income of Mr. Ashok for A.Y. 2016-17

Particulars		Amount (₹)	Amount (₹)
(1) **Income from House Property (Let out)**			
Gross Annual Value (being Fair rent)		3,00,000	
Less: Municipal Tax		12,000	
Net Annual Value (NAV)		2,88,000	
Less: Deduction:-			
u/s 24(a) Standard Deduction (30% of NAV)	86,400		
u/s 24(b) Interest on loan	42,000	(1,28,400)	1,59,600
(2) **Profits and Gains of Business or Profession**			
Net Profit before depreciation		2,20,000	
Less: Expenditure allowed but not debited in P & L Account			
Depreciation on equipment	30,000		
Depreciation on building i.e. 10% of ₹ 5,00,000	50,000	80,000	
Profits and Gains of Business or Profession of current year		1,40,000	
Less: Brought forward losses set off u/s 72		(90,000)	50,000
(3) **Capital Gains**			
Consideration for Transfer		2,30,000	
Less: Cost of acquisition		(1,80,000)	
Short Term Capital Gains			50,000
Gross Total Income			2,59,600
Less: Deduction u/s			
80C: LIC Premium paid	32,000		
Repayment of bank loan	23,000	55,000	
80D: Medical insurance premium		6,000	61,000
Total Income			**1,98,600**
Tax Payable			Nil

Notes :

1. Penal interest is not allowed u/s 24(b)
2. It has been assumed that interest, municipal tax on property used for business have already being charged while computing "Business Income Before Depreciation" i.e. ₹ 2,20,000.
3. STT is not allowed as expenditure on transfer.

Illustration 18: Thomas aged 56 years, took voluntary retirement from State Bank of India on 1st April, 2015 under the Voluntary Retirement Scheme (VRS) and received a sum of ₹ 25 lakh on account of VRS benefits. At the time of his retirement, Thomas was having 47 months of service left and had served the organisation for 18 years 11 months. His last drawn Basic Pay ₹ 60,000, D.A. @ 60% of B/Pay (80% of which forming part of salary). Later, he started a business of plying, hiring and leasing of goods carriages from 1st June, 2015 by acquiring 3 heavy vehicles for ₹ 12 lakh, 2 medium goods vehicle for ₹ 5 lakh and 3 light commercial vehicles for ₹ 6 lakh. Although, he did not maintain regular books of account for his business, the diary maintained by him revealed gross receipts of ₹ 3,12,000 for the financial year ended 31st March, 2016 and he incurred an expenditure of ₹ 1,68,500 on the business towards salaries of drivers, repairs, fuel, etc. Depreciation on vehicle is not included in the said expenditure.

During the financial year 2015-16, he received a sum of ₹ 3,00,000 on account of pension from bank and he contributed a sum of ₹ 65,000 to his PPF account maintained with the said bank in the same year. His PPF account was credited with interest of ₹ 35,000 during the financial year 2015-16. He also purchased long-term infrastructure bonds for ₹ 20,000; Repayment of educational loan interest for the year ₹ 50,000. He also paid medical insurance premium of ₹ 14,000.

Further, he had two residential properties, one is self occupied and other is let out. During the financial year 2015-16, Thomas was able to let out his property for 12 months on a monthly rent of ₹ 17,000. The total municipal taxes on the let out property was ₹ 18,000, 50% of which was paid by the tenant and 50% by him. The interest on loan taken for renovation of the self occupied property paid by him during the year was ₹ 34,000. The insurance premium on the house and actual repairs and collection charges paid are ₹ 1,600 and ₹ 18,000 respectively and the entire expenditure is borne by him. During the financial year 2015-16, he was able to recover the unrealized rent of ₹ 33,000 from old tenant who vacated the house during the August, 2012 after spending litigation expenses of ₹ 15,000. During the financial year 2015-16, Thomas suffered short term capital loss on account of sale of shares on various dates amounting to ₹ 8,50,000.

From the aforesaid information, you are required to compute the Total Income of Thomas for the A.Y. 2016-17 giving reasons in respect of each and every item and indicate the relief/rebate/deduction which he is entitled to claim.

Solution :

Assessee : Mr. Thomas **Previous Year : 2015-2016** **Assessment Year : 2016-2017**

Computation of Total Income

Particulars		₹	₹
(1) **Income from Salary**			
Pension Received			3,00,000
Voluntary Compensation			
Actual Amount Received		25,00,000	
Less : Exemption u/s 10(10C)			
Least of the following :			
(i) Actual Amount Received	25,00,000		
(ii) Maximum limit	5,00,000		
(iii) Higher of the following :			
(a) Last Drawn Salary × 3 × No. of Fully completed year of service = 88,800 × 3 × 18 = 47,95,200			
(b) Last Drawn Salary × Balance of number of months of service left = 88,800 × 47 = 41,73,600	47,95,200		
Last Drawn Salary = B/ Pay + D.A (forming part)		5,00,000	20,00,000
= ₹ [60,000 + 60% of 80% of 60,000]			
= ₹ [60,000 + 28,800]			
= ₹ 88,800			

Particulars		₹	₹
(2) **Income from House Property**			
(a) **Self occupied :**			
Annual Value	Nil		
(–) Interest on Loan u/s 24(b) ₹ 34,000			
– restricted upto ₹ 30,000	(30,000)	(30,000)	
(b) **Let-out House Property**			
Gross Annual Value			
(being the Rental Value) = 17,000 ×12	2,04,000		
Less : Municipal Tax Paid by the assessee during the year			
= 18,000 × 50%	9,000		
Net Annual Value (NAV)	**1,95,000**		
Less : Standard deduction @ 30% of NAV u/s 24(a)	58,500		
Less : Interest on loan u/s 24(b)	Nil	1,36,500	1,06,500
(3) **Income from Business or Profession**			
Presumptive Income u/s 44AE			
In the Business of plying, leasing or hiring trucks			
No. of goods Vehicles = 3 + 2 + 3 = 8			
Goods Vehicle (8 x 7500 x 10)			
			6,00,000
(5) **Income from Captal Gains**			(8,50,000)
Short Term Capital Loss			**21,56,500**
Gross Total Income			
Less : **Deductions under Chapter VIA**			
u/s 80C – Deposits in PPF	65,000		
u/s 80D – Medical Insurance Premium	14,000		
u/s 80E – Interest paid on Education loan	50,000		1,29,000
Total Income			**20,27,500**
Tax on Total Income of ₹ 20,27,500			4,33,250
(+) E/C @ 2%			8,665
(+) SHEC @ 1%			4,332
Tax Payable			4,46,247
Tax Payable (Rounded off u/s 288B)			4,46,250

Note: Deduction u/s 80CCF, in respect of investment made in Long Term Infrastructure Bond, is discontinued from the A.Y. 2014-15.

Illustration 19:

R borrowed a sum of ₹25,00,000 from the State Bank of India @ 12% p.a. on 1.5.2015 and purchased a house property for ₹36,00,000 on the same day. He does not own any residential house property on the date of taking the loan. He has been using the house property for his own residence since its acquisition.

(a) Compute the total income of R assuming he has salary income of ₹9,60,000 and he deposited ₹1,30,000 in PPF during the previous year 2015-16.

(b) What shall be the answer if the total interest on borrowed money is ₹2,40,000 instead of ₹2,75,000.

Solution:

Computation of total income of R for Assessment Year 2015-16

	₹	₹
Income from salary		9,60,000
Income from house properly		
Annual value	Nil	
Less: Deduction		
Interest limited to	2,00,000	(–) 2,00,000
Gross total income		7,60,000
Less: Deduction u/s 80C restricted to ₹1,50,000	1,50,000	
U/s 80EE	1,00,000	2,50,000
Total income		5,10,000

Working Note:

Total interest @ 12% on ₹25,00,000 for 11 months

₹25,00,000 × 12 x×11/100 x 12 = 2,75,000

(b) The deduction under section 80EE in this case shall be allowed to the extent of ₹900,000 and the balance ₹10,000 shall allowed in financial year 2016-17 (Assessment Year 2017-18).

Illustration 20.

A handicapped person in business has an income of ₹25 lakhs per annum. He claims the concession u/s 80U. The Assessing Officer declines to grant the same on the ground that his disability has not affected his opportunity to a gainful employment. Is he right?

Solution:

The Assessing Officer is not right, since eligibility for deduction u/s 80U depends upon the nature of permanent physical disability as prescribed under the rules. As long as he qualifies for the same under the rules and files a certificate to that effect from a medical practitioner with prescribed qualification, relief cannot be denied.

Illustration 21.

Whether photographers and TV news film cameraman can avail of the benefit u/s 80RR?

Solution:

Yes, as per Circular No.31 dated 25.10.1969, photographers and TV news film cameraman can be regarded as artists for the purpose of Sec. 80RR.

Illustration 22.

Is it necessary that the assessee to link his savings eligible for deduction u/s 80C with the current taxable income?

Solution:

As long as the assessee has taxable income and the eligible investments are made during the year, there can be no bar for deduction. Section 80C as presently worded would admit the deduction without any pre-qualification of such investments having to be made out of current income.

Illustration 23.

A book written by G was recommended as text book by the Annamalai Univesity for the first time for the academic year 1977-78. Whether G is entitled to special deduction u/s 80QQA?

Solution:

Yes. It is not necessary that the book should have been recommended for the first time during the relevant previous year. G would get special deduction even if the book has been recommended prior to the insertion of section 80QQA, vide Circular No.258 dated 14.6.1979.

Illustration 24.

What is the present position as regards availability of processing of living things?

Solution:

It was considered that relief for processing of living things will no longer be available after the decision of the Supreme Court in CIT vs. Venkateswara Hatcheries (P) Ltd (1999) 237 ITR 174 (SC), and in respect of hotel in CIT vs. Relish Foods (1999) 237 ITR 59 (SC) in respect of processing of shrimps. However, some hope is offered as regards processing for making them marketable treated it as an issue, which is left open by the Supreme Court in Indian Poultry vs. CIT (2001) 250 ITR 664 (SC). The Supreme Court did not deal with the issue only because the relevant material for decision had not been placed by the assessee before the Appellate Tribunal.

The Supreme Court, in CIT vs. Relish Foods(1999) 237 ITR 59 (SC), held that processing of marine products for export may not constitute industrial activity, and reiterated this view in CIT vs. Kala Cartoons P. Ltd. (2001) 252 ITR 658 (SC). But in both the decisions, it found an exception in CIT vs. Marwell Sea Foods (1987) 166 ITR 624 (Ker), on the ground that it was a case where detailed description of the processes was given and that such description spelt out manufacture as found by the Tribunal. It would, therefore, mean that where the assessee is able to show that various processes involved use of skilled labour, and sophisticated machinery, there is no reason why the deduction should not be available.

Illustration 25.

An assessee does not make a claim for relief u/s 80-IA, because it returned a loss. The Assessing officer has computed positive income by making certain disallowances but does not grant relief as no claim had been made. Is the Assessing Officer correct in his view?

Solution:

In CIT vs. Gujarat Agro Oil Enterprises (2000) 244 ITR 3 (Guj), the High Court pointed out that the deduction is permissible, though no specific claim had been made if the conditions therefore are satisfied. The Assessing Officer should, therefore, give an opportunity to the taxpayer to file such audit report.

Illustration 26.

Where a co-operative society is eligible for relief u/s 80-IA as well as u/s 80P, which relief will have precedence?

Solution:

Relief u/s 80-IA will be first given and balance will be reckoned for relief u/s 80P.

Illustration 27.

Should the past losses or unabsorbed depreciation in respect of the same activity in the past be set-off against current income eligible for deduction?

Solution:

The controversy based upon Cambay Electric Supply Industrial Co. Ltd. vs. CIT (1978) 113 ITR 84 (SC) continues to haunt the incentive provisions and concessions. Co-operative sector is no exception. The Supreme Court, in CIT vs. Kotagiri Industrial Co-operative Tea Factory Ltd. (1997) 224 ITR 604 (SC) has held that the definition of gross total income would taken into consideration the past losses or unabsorbed depreciation as well as has been decided even for the purposes of sections 80HHC, 80-I and 80-IB. Further, the more liberal language "attributable to" instead of "derived from" has been used for section 80P.

Past unabsorbed loss, it was held, would go to reduce the eligible profit for section 80P, since it is required to set-off against current income for the purposes of relief, in CIT vs. Ganganagar Sahkari Spinning Mills Ltd. (2004) 265 ITR 540 (Raj.) following Kotagiri Industrial Co-Operative Tea Factory's Case.

Illustration 28.

For purposes of relief u/s 80P(e) meant for co-operative societies engaged in letting of godowns and warehouses for storage, processing or facilitating marketing of commodities, is it possible to get relief for a co-operative society having income from cold storage?

Solution:

Cold storage, on a liberal interpretation, would be construed as godown and warehouse considering the purpose of marketing agricultural produce in a condition fit for marketing should merit a favourable interpretation.

Illustration 29.

Is commission earned by a co-operative society from public distribution of controlled commodities exempt?

Solution:

No. In Udaipur Shahakari Upbhokta Thok Bhandar Ltd. vs CIT (2009) 315 ITR 21 (SC), the society was storing goods given by the Government and supplying it to fair price shops. The Supreme Court held that the Commission earned was not from letting on hire of godowns and so was not entitled to exemption, the goods having stored in its own godown not for the purpose of storing, processing or facilitating the marketing of the commodities.

Illustration 30.

Is a co-operative society engaged in collective disposal of labour be entitled to relief u/s 80P(2)(a) when firms and associations are its members?

Solution:

No. In view of the retrospective amendment to clause (iii) of section 80P(2)(a) in 1988, it is not possible to treat firms and associations as members of the same status as individuals. The decision in CIT vs. Salem District Printers Service Industrial Co-operative Society Ltd. (2007) 290 ITR 371 (SC), following Kerala State Co-operative Marketing Federation Ltd. vs. CIT (1998) 231 ITR 814 (SC), is no longer good law.

Illustration 31.

Can interest on loans advanced to nominal members by a credit society be entitled to exemption?

Solution:

Yes, exemption is available in view of the decision of CIT vs. Punjab State Co-operative Bank Ltd. (2008) 300 ITR 24 (P&H), following CIT vs. Bangalore District Co-operative Central Bank Ltd. (1998) 233 ITR 282 (SC), and CIT vs. Karnataka State Co-operative Apex Bank (2001) 251 ITR 194 (SC).

Illustration 32.

Is concession given for cottage industries vulnerable because of some payment to outside agency for bleaching, dyeing, transport arrangement, etc.?

Solution:

No. Board's Circular No. 722 dt. 19.09.1995 points out that as long as cottage industry is carried on at the residence or at a common place provided by weavers' society without any outside labour, the use of outside agency for some activity does not lose the benefit for cottage industry.

Illustration 33.

Mr. Rabi is a person with sever disability. He submits you the following information:

	₹
Salary p.a.	48,000
Interest on Bank deposit	40,000
Long Term Capital Gains	2,15,000
Deposit in PPF during the year	10,000

You are required to compute the net tax payable for the Assessment Year 2016-17.

Solution:

Statement Showing Computation of Total Income

	₹	₹
Income from Salary		48,000
Income from Capital Gains:		
Long Term Capital Gains		2,15,000
Income from Other Sources:		
Interest on Bank deposit		40,000
Gross Total Income		3,03,000
Less: Deduction under Chapter VIA		
U/s 80C	10,000	
U/s 80U	1,25,000	
	1,35,000	
Chapter VIA deduction cannot be availed against LTCG so the deduction cannot exceed GTI exclusive of Long Term Capital Gain Hence deduction allowed		88,000
Total Income		2,15,000

Statement Showing Computation of Tax Payable

	₹
Tax on Long Term Capital Gains (2,15,000-2,00,000) × 20%	3,000
Less : Rebate u/s 87A	2,000
	1,000
Add: Education Cess & SHEC @3%	30
Tax (Rounded Off)	1,030

Study Note - 16

SETTLEMENT OF CASES

This Study Note includes

16.1 Settlement of Cases [Section 245A to 245L]
16.2 Advance Ruling

16.1 SETTLEMENT OF CASES [SECTION 245A TO 245L]

16.1.1 Meaning of Case [Section 245A(b)]

"Case" means any proceeding for assessment under this Act, of any person in respect of any assessment year or assessment years which may be pending before an Assessing Officer on the date on which an application under sub-section (1) of section 245C is made.

Explanation.—For the purposes of this clause—

(i) a proceeding for assessment or reassessment or recomputation under section 147 shall be deemed to have commenced—

   (a) from the date on which a notice under section 148 is issued for any assessment year;

   (b) from the date of issuance of the notice referred to in sub-clause (a), for any other assessment year or assessment years for which a notice under section 148 has not been issued, but such notice could have been issued on such date, if the return of income for the other assessment year or assessment years has been furnished under section 139 or in response to a notice under section 142;

(ii) a proceeding for making fresh assessment in pursuance of an order under section 254 or section 263 or section 264, setting aside or cancelling an assessment shall be deemed to have commenced from the date on which such order, setting aside or cancelling an assessment was passed;

(iii) a proceeding for assessment or reassessment for any of the assessment years, referred to in clause (b) of sub-section (1) of section 153A in case of a person referred to in section 153A or section 153C, shall be deemed to have commenced on the date of issue of notice initiating such proceeding and concluded on the date on which the assessment is made;

(iv) a proceeding for assessment for any assessment year, other than the proceedings of assessment or reassessment referred to in clause (i) or clause (iii) or clause (iiia), shall be deemed to have commenced from the date on which the return of income for that assessment year is furnished under section 139 or in response to a notice served under section 142 and concluded on the date on which the assessment is made; or on the expiry of two years from the end of relevant assessment year, in case where no assessment is made.

16.1.2 Income-tax Settlement Commission [Section 245B]

(1) The Central Government shall constitute a Commission to be called the Income-tax Settlement Commission for the settlement of cases under this Chapter.

(2) The Settlement Commission shall consist of a Chairman and as many Vice-Chairmen and other members as the Central Government thinks fit and shall function within the Department of the Central Government dealing with direct taxes.

(3) The Chairman Vice-Chairman and other members of the Settlement Commission shall be appointed by the Central Government from amongst persons of integrity and outstanding ability, having special knowledge of, and, experience in, problems relating to direct taxes and business accounts.

Provided that, where a member of the Board is appointed as the Chairman Vice-Chairman or as a member of the Settlement Commission, he shall cease to be a member of the Board.

16.1.3 Jurisdiction and Powers of Settlement Commission [**Section 245BA]**

(1) Subject to the other provisions of this Chapter, the jurisdiction, powers and authority of the Settlement Commission may be exercised by Benches thereof.

(2) Subject to the other provisions of this section, a Bench shall be presided over by the Chairman or a Vice-Chairman and shall consist of two other Members.

(3) The Bench for which the Chairman is the Presiding Officer shall be the principal Bench and the other Benches shall be known as additional Benches.

(4) Notwithstanding anything contained in sub-sections (1) and (2), the Chairman may authorize the Vice-Chairman or other Member appointed to one Bench to discharge also the functions of the Vice-Chairman or, as the case may be, other Member of another Bench.

(5) Notwithstanding anything contained in the foregoing provisions of this section, and subject to any rules that may be made in this behalf, when one of the persons constituting a Bench (whether such person be the Presiding Officer or other Member of the Bench) is unable to discharge his functions owing to absence, illness or any other cause or in the event of the occurrence of any vacancy either in the office of the Presiding Officer or in the office of one or the other Members of the Bench, the remaining two persons may function as the Bench and if the Presiding Officer of the Bench is not one of the remaining two persons, the senior among the remaining persons shall act as the Presiding Officer of the Bench.

Provided that if at any stage of the hearing of any such case or matter, it appears to the Presiding Officer that the case or matter is of such a nature that it ought to be heard of by a Bench consisting of three Members, the case or matter may be referred by the Presiding Officer of such Bench to the Chairman for transfer to such Bench as the Chairman may deem fit.

(5A) Notwithstanding anything contained in the foregoing provisions of this section, the Chairman may, for the disposal of any particular case, constitute a Special Bench consisting of more than three Members.

(6) Subject to the other provisions of this Chapter, the places at which the principal Bench and the additional Benches shall ordinarily sit shall be such as the Central Government may, by notification in the Official Gazette, specify and the Special Bench shall sit at a place to be fixed by the Chairman.

16.1.4 Vice-Chairman to act as Chairman or to discharge his functions in certain circumstances [Section 245BB]

(1) In the event of the occurrence of any vacancy in the office of the Chairman by reason of his death, resignation or otherwise, the Vice-Chairman or, as the case may be, such one of the Vice-Chairmen as the Central Government may, by notification in the Official Gazette, authorise in this behalf, shall act as the Chairman until the date on which a new Chairman, appointed in accordance with the provisions of this Chapter to fill such vacancy, enters upon his office.

(2) When the Chairman is unable to discharge his functions owing to absence, illness or any other cause, the Vice-Chairman or, as the case may be, such one of the Vice-Chairmen as the Central Government may, by notification in the Official Gazette, authorise in this behalf, shall discharge the functions of the Chairman until the date on which the Chairman resumes his duties.

16.1.5 Power of Chairman to transfer cases from one Bench to another [Section 245BC]

On the application of the assessee or the Chief Commissioner or Commissioner and after notice to them, and after hearing such of them as he may desire to be heard, or on his own motion without such notice, the Chairman may transfer any case pending before one Bench, for disposal, to another Bench.

16.1.6 Decision to be taken by majority [Section 245BD]

If the Members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority, if there is a majority, but if the Members are equally divided, they shall state the point or points on which they differ, and make a reference to the Chairman who shall either hear the point or points himself or refer the case for hearing on such point or points by one or more of the other Members of the Settlement Commission and such point or points shall be decided according to the opinion of the majority of the Members of the Settlement Commission who have heard the case, including those who first heard it.

16.1.7 Application for settlement of cases [Section 245C]

(1) An assessee may, at any stage of a case relating to him, make an application in such form and in such manner as may be prescribed, and containing a full and true disclosure of his income which has not been disclosed before the Assessing Officer, the manner in which such income has been derived, the additional amount of Income-tax payable on such income and such other particulars as may be prescribed, to the Settlement Commission to have the case settled and any such application shall be disposed of in the manner hereinafter provided :

Provided that no such application shall be made unless—

(i) the additional amount of Income-tax payable on the income disclosed in the application exceeds the amount given below

Different situations	Application can be filed only if the additional amount of Income-tax payable on the income disclosed in the application exceeds the amount of tax given below		
	Up to May 31 2010	From June 1, 2010 to May 31, 2011	With effect from June 1, 2011
Case 1 – When an application is filed before the Settlement Commission, in cases where proceedings for assessment or reassessment have been initiated as a result of requisition of books of account or other documents or any assets.	Settlement not possible	₹ 50 Lakhs	₹ 50 Lakhs
Case 2 – Where the applicant- a. is "related" to the person [referred to in Case 1 above] in whose case proceedings have been initiated as a result of search and who has filed an application; and b. is a person in whose case proceedings have also been initiated as a result of search	Settlement not possible	₹ 50 Lakhs	₹ 10 Lakhs
Case 3 – Where an application is filed in any other case	₹ 3 Lakhs	₹ 10 Lakhs	₹ 10 Lakhs

(ii) such tax and the interest thereon, which would have been paid under the provisions of this Act had the income disclosed in the application been declared in the return of income before the Assessing Officer on the date of application, has been paid on or before the date of making the application and the proof of such payment is attached with the application.

However, in the case of the following proceedings though pending for assessment before the Assessing Officer, the assessee shall not be allowed to make the application to the Settlement Commission:

(i) a proceeding for assessment or reassessment or recomputation under section 147.

These proceeding shall be deemed to have commenced from the date on which a notice under section 148 is issued;

(ii) a proceeding for making fresh assessment in pursuance of an order under section 254 or section 263 or section 264, setting aside or cancelling an assessment.

These proceedings shall be deemed to have commenced from the date on which the order under section 254 or section 263 or section 264, setting aside or cancelling an assessment was passed.

Thus, the proceeding for assessment or re-assessment under section 147 for fresh assessment in pursuance of order under section 254 or 263 or 264, though pending before the Assessing Officer, shall not be treated as any proceeding pending before the Assessing Officer and thus application for settlement cannot be made in such cases.

(1A) For the purposes of sub-section (1) of this section, the additional amount of Income-tax payable in respect of the income disclosed in an application made under sub-section (1) of this section shall be the amount calculated in accordance with the provisions of sub-sections (1B) to (1D).

(1B) Where the income disclosed in the application relates to only one Previous Year,—

(i) if the applicant has not furnished a return in respect of the total income of that year, then, tax shall be calculated on the income disclosed in the application as if such income were the total income;

(ii) if the applicant has furnished a return in respect of the total income of that year, tax shall be calculated on the aggregate of the total income returned and the income disclosed in the application as if such aggregate were the total income.

(1C) The additional amount of Income-tax payable in respect of the income disclosed in the application relating to the Previous Year referred to in sub-section (1B) shall be,—

(*a*) in a case referred to in clause (*i*) of that sub-section, the amount of tax calculated under that clause;

(*b*) in a case referred to in clause (*ii*) of that sub-section, the amount of tax calculated under that clause as reduced by the amount of tax calculated on the total income returned for that year;

(1D) Where the income disclosed in the application relates to more than one Previous Year, the additional amount of Income-tax payable in respect of the income disclosed for each of the years shall first be calculated in accordance with the provisions of sub-sections (1B) and (1C) and the aggregate of the amount so arrived at in respect of each of the years for which the application has been made under sub-section (1) shall be the additional amount of Income-tax payable in respect of the income disclosed in the application.

(2) Every application made under sub-section (1) shall be accompanied by a fee of ₹ 500

(3) An application made under sub-section (1) shall not be allowed to be withdrawn by the applicant.

(4) An assessee shall, on the date on which he makes an application under sub-section (1) to the Settlement Commission, also intimate the Assessing Officer in the prescribed manner of having made such application to the said Commission.

Case Law:

Application must disclose undisclosed income: The requirement is that there must be an income disclosed in a return furnished and undisclosed income disclosed to the Commission by a petition u/s 245C – *CIT* vs. *Damani Bros.* 259 ITR 475/126 Taxman 321

Additional tax shall be computed as follows :-

(i) Where the income disclosed in the application relates to only one Previous Year	• Tax on income disclosed in the application as if such income were the total income
(a) If the applicant has not furnished a return of income of that year (b) If the applicant has furnished a return in respect of total income of that year	• Tax on the aggregate of the total income returned and income disclosed in the application for settlement minus tax calculated on returned income
(ii) Where the income disclosed relates to more than one Previous Year	Aggregate of the amount of tax determined for each year according to rules mentioned.

16.1.8 Procedure for Receipt of Application [Section 245D]

(1) On receipt of an application under section 245C, the Settlement Commission shall, within seven days from the date of receipt of the application, issue a notice to the applicant requiring him to explain as to why the application made by him be allowed to be proceeded with, and on hearing the applicant, the Settlement Commission shall, within a period of fourteen days from the date of the application, by an order in writing, reject the application or allow the application to be proceeded with.

Provided that where no order has been passed within the aforesaid period by the Settlement Commission, the application shall be deemed to have been allowed to be proceeded with.

(2) A copy of every order under sub-section (1) shall be sent to the applicant and to the Commissioner.

(2A) Where an application was made under section 245C before the 1st day of June, 2007, but an order under the provisions of sub-section (1) of this section, as they stood immediately before their amendment by the Finance Act, 2007, has not been made before the 1st day of June, 2007, such application shall be deemed to have been allowed to be proceeded with if the additional tax on the income disclosed in such application and the interest thereon is paid on or before the 31st day of July, 2007.

Explanation— In respect of the applications referred to in this sub-section, the 31st day of July, 2007 shall be deemed to be the date of the order of rejection or allowing the application to be proceeded with under sub-section (1).

(2B) The Settlement Commission shall,—

(i) in respect of an application which is allowed to be proceeded with under sub-section (1), within thirty days from the date on which the application was made; or

(ii) in respect of an application referred to in sub-section (2A) which is deemed to have been allowed to be proceeded with under that sub-section, on or before the 7th day of August, 2007, call for a report from the Commissioner, and the Commissioner shall furnish the report within a period of thirty days of the receipt of communication from the Settlement Commission.

(2C) Where a report of the Commissioner called for under sub-section (2B) has been furnished within the period specified therein, the Settlement Commission may, on the basis of the report and within a period of fifteen days of the receipt of the report, by an order in writing, declare the application in question, after giving opportunity of being heard to the applicant, as invalid, and shall send the copy of such order to the applicant and the Commissioner;

(2D) Where an application was made under sub-section (1) of section 245C before the 1st day of June, 2007 and an order under the provisions of sub-section (1) of this section, as they stood immediately before their amendment by the Finance Act, 2007, allowing the application to have been proceeded with, has been passed before the 1st day of June, 2007, but an order under the provisions of sub-section (4), as they stood immediately before their amendment by the Finance Act, 2007, was not passed before the 1st day of June, 2007, such application shall not be allowed to be further proceeded with unless the additional tax on the income disclosed in such application and the interest thereon, is, notwithstanding any extension of time already granted by the Settlement Commission, paid on or before the 31st day of July, 2007.

(3) The Settlement Commission, in respect of—

(i) an application which has not been declared invalid under sub-section (2C); or

(ii) an application referred to in sub-section (2D) which has been allowed to be further proceeded with under that sub-section, may call for the records from the Commissioner and after examination of such records, if the Settlement Commission is of the opinion that any further enquiry or investigation in the matter is necessary, it may direct the Commissioner to make or cause to be made such further enquiry or investigation and furnish a report on the matters covered by the application and any other matter relating to the case, and the Commissioner shall furnish the report within a period of ninety days of the receipt of communication from the Settlement Commission;

(4) After examination of the records and the report of the Commissioner, if any, received under—

(i) sub-section (2B) or sub-section (3), or

(ii) the provisions of sub-section (1) as they stood immediately before their amendment by the Finance Act, 2007, and after giving an opportunity to the applicant and to the Commissioner to be heard, either in person or through a representative duly authorized in this behalf, and after examining such further evidence as may be placed before it or obtained by it, the Settlement Commission may, in accordance with the provisions of this Act, pass such order as it thinks fit on the matters covered by the application and any other matter relating to the case not covered by the application, but referred to in the report of the Commissioner.

(4A) The Settlement Commission shall pass an order under sub-section (4),—

(i) in respect of an application referred to in sub-section (2A) or sub-section (2D), on or before the 31st day of March, 2008;

(ii) in respect of an application made on or after the 1st day of June, 2007, but before the 1st day of June, 2010, within twelve months from the end of the month in which the application was made;

(iii) in respect of an application made on or after June 1, 2010, within eighteen months from the end of the month in which application was made;

(5) Subject to the provisions of section 245BA, the materials brought on record before the Settlement Commission shall be considered by the Members of the concerned Bench before passing any order under sub-section (4) and, in relation to the passing of such order, the provisions of section 245BD shall apply.

(6) Every order passed under sub-section (4) shall provide for the terms of settlement including any demand by way of tax, penalty or interest, the manner in which any sum due under the settlement shall be paid and all other matters to make the settlement effective and shall also provide that the settlement shall be void if it is subsequently found by the Settlement Commission that it has been obtained by fraud or misrepresentation of facts.

(6A) Where any tax payable in pursuance of an order under sub-section (4) is not paid by the assessee within thirty-five days of the receipt of a copy of the order by him, then, whether or not the Settlement Commission has extended the time for payment of such tax or has allowed payment thereof by instalments, the assessee shall be liable to pay simple interest at one & one-fourth percent per month (or part of month)on the amount remaining unpaid from the date of expiry of the period of thirty-five days aforesaid. Interest is payable even if the Settlement Commission has extended the time of payment.

(6B) The Settlement Commission may, with a view to rectifying any mistake apparent from the record, amend any order passed by it under sub-section (4)—

(a) at any time within a period of six months from the end of the month in which the order was passed; or

(b) at any time within the period of six months from the end of the month in which an application for rectification has been made by the Principal Commissioner or the Commissioner or the applicant, as the case may be.

Provided that no application for rectification shall be made by the Principal Commissioner or the Commissioner or the applicant after the expiry of six months from the end of the month in which an order under sub-section (4) is passed by the Settlement Commission.

Provided further that an amendment which has the effect of modifying the liability of the applicant shall not be made under this sub-section unless the Settlement Commission has given notice to the applicant and the Principal Commissioner or Commissioner of its intention to do so and has allowed the applicant and the Principal Commissioner or Commissioner an opportunity of being heard.

(7) Where a settlement becomes void as provided under sub-section (6), the proceedings with respect to the matters covered by the settlement shall be deemed to have been revived from the stage at which the application was allowed to be proceeded with by the Settlement Commission and the Income-tax Authority concerned, may, notwithstanding anything contained in any other provision of this Act, complete such proceedings at any time before the expiry of two years from the end of the financial year in which the settlement became void.

(8) For the removal of doubts, it is hereby declared that nothing contained in section 153 shall apply to any order passed under sub-section (4) or to any order of assessment, reassessment or re-computation required to be made by the Assessing Officer in pursuance of any directions contained in such order passed by the Settlement Commission and nothing contained in the proviso to sub-section (1) of section 186 shall apply to the cancellation of the registration of a firm required to be made in pursuance of any such directions as aforesaid.

Case laws:

(1) Effect of omission of sub-section (1A) of section 245D: Where the applications of the respondents were not proceeded with only because of the objection raised by the Commissioner under sub-section (1A), having regard to the fact that the said sub-section (1A) was removed from the statute book subsequent to 1991, there was no reason why the Settlement Commission could not have entertained fresh applications under section 245C and this would not be a case of review at all - *CIT* vs. *Bhaskar Picture Palace* 113 Taxman 109.

(2) Power to over-rule objections is procedural: Amendment of section 245D with effect from 1-4-1979 empowering Settlement Commission to overrule objections of Commissioner was procedural and an order passed by Commissioner under section 245D prior to aforesaid amendment without giving applicant an opportunity of hearing was a nullity being passed in violation of principles of natural justice and after amendment of section 245D with effect from 1-4-1979 assessee was entitled to be heard on objections of Commissioner *R.B. Shreeram Durga Prasad and Fatechand Nursing Das* vs. *Settlement Commission (IT & WT)* 176 ITR 169/43 Taxman 34.

16.1.9 Provisional Attachment to protect Revenue [Section 245DD]

If during the pendency of any proceedings the Commission is of the opinion that for the purpose of protecting the interests of the revenue, it is necessary to do so, it may attach provisionally for six months any property belonging to the applicant in the manner provided in the Second Schedule to the Act. Such attachment shall not extend in any case more than two years.

16.1.10 Reopening of completed proceedings [Section 245E]

If the Settlement Commission is of the opinion that for the proper disposal of the case pending before it, it is necessary or expedient to reopen any proceedings connected with the case but which has been completed by any Income-tax Authority before the application was made, it may, with the concurrence of the applicant reopen such proceedings and pass such orders thereon as it thinks fit. However, no proceeding shall be reopened by the Settlement Commission under this provision if the period between the end of the Assessment Year to which such a proceeding relates and the date of application for settlement u/s 245C exceed nine years.

Case Law:

Others/matters relating to jurisdiction of Settlement Commission: Failure on the part of the petitioner to deduct tax at source does not come within purview of section 245C(1). Section 245E contemplates reopening of completed proceedings not for benefit of assessee but in the interest of the revenue -*CIT* vs. *Paharpur Cooling Towers (P.) Ltd.* 85 Taxman 357.

16.1.11 Exclusive jurisdiction of the Settlement Commission over the admitted applications [Section 245F]

After an application made u/s 245C has been allowed to be proceeded with, the Settlement Commission will have exclusive jurisdiction over the case till an order u/s 245D(4) has been made. During this period the Settlement Commission will have all the powers vested in an Income-tax Authority under the Act. However, in the absence of any express direction to the contrary by the Settlement Commission nothing contained in Section 245F shall effect the operation of any other provisions of the Act requiring the applicant to pay tax on the basis of Self Assessment in relation to the matters before the Settlement Commission.

Case Law:

A final decision, however wrong, is still final and its binding force does not depend upon its correctness Capital Cables (India) (P.) Ltd. vs. Income-tax Settlement Commission 267 ITR 528/139 Taxman 332.

16.1.12 Inspection, etc. Reports [Section 245G]

No persons shall be entitled to inspect or obtain copies of any reports made by any Income-tax Authority to the Settlement Commission but the Settlement Commission may in its discretion, furnish copies thereof to any such person or an application made to in this behalf. However, for the purposes of enabling any person whose case is under consideration to rebut any evidence on record against him in any such report, the Commission shall furnish him a certified copy of any such report if the applicant makes an application in this behalf. The copies will be supplied to the applicant on payment of the prescribed fee.

16.1.13 Immunity from Prosecution and Penalty [Section 245H]

If the Settlement Commission is satisfied that any person who made the application for settlement has cooperated with the Settlement Commission in the proceedings before it and has made a full and true disclosure of his income and the manner in which such income has been derived subject to such conditions as it may think fit to impose for the reasons to be recorded in writing, it may grant immunity from prosecution under the Income-tax Act or under the Indian Penal Code or under any other Central Act as also the imposition of any penalty under the Income-tax Act with respect to the case covered by the settlement. However, w.e.f. 1.6.2007 no such immunity shall be granted by the Settlement Commission in cases where the proceedings for prosecution for any such offence have been instituted before the date of receipt of the application under Section 245C. An immunity granted by the Settlement Commission shall stand withdrawn if the applicant fails to pay the sum specified in the order of settlement within the time specified in such order or within such further time as may be allowed by the Settlement Commission or fails to comply with any other condition subject to which the immunity was granted. The immunity may also be withdrawn if the Settlement Commission is satisfied that the applicant has, in the course of proceedings, concealed any particular material to the settlement or had given false evidence. Once the immunity granted is withdrawn, the assessee may be tried for offence with respect to which the immunity was granted or for any other offences of which he appears to have been guilty in connection with the Settlement and shall also become liable to imposition of any penalty under this Act to which such person would have been liable, had not such immunity been granted.

16.1.14 Abatement of proceeding before settlement Commission [Section 245HA]

Proceedings for settlement shall abate from the date given below –

Circumstances in which the proceeding abates	Date of abatement
Where the application is made on or after June 1, 2007 and is rejected within 14 days from the date of application under section 245D(1)	Date on which the application is rejected.
An application made before June 1, 2007 but the tax is not paid before July 31, 2007 and hence it is rejected under section 245D(2D)	July 31, 2007.
An application made under section 245C declared as invalid with or without the report of the Commissioner under section 245D(2C)	The last day of the month in which the application is declared as invalid.
Any application made under section 245C, an order under sub-section (4) of section 245D has been passed not providing for the terms of settlement.	The day on which the order under sub-section (4) of section 245D was passed not providing for the terms of settlement.
An application made under section 245C and the order is not passed within the time prescribed in section 245D(4A)	Date on which the time period specified in section 245D(4A) expires.

Where the proceedings before the Settlement Commission abates, the Assessing Officer or any other Income-tax Authority before whom the proceedings are pending at the time of making the application under section 245C shall reassume jurisdiction and shall dispose of the case in accordance with the provisions of the Act.

For the purpose of disposing the case, Assessing Officer can use-

- Material and other information produced by the Assessee before the Settlement Commission; or
- Result of the inquiry held or evidence recorded by the Settlement Commission in the course of the proceedings before it.

Time limit for Sections 149, 153, 153B, 154, 155, 158BE, 231, 243, 244, 244A will be extended by the period-

- Commencing on and from the date of application; and
- Ending on date of abatement.

16.1.15 Credit of Tax paid in case of abatement of proceedings [Section 245HAA]

Where an application made u/s 245C on or after 1st day of June, 2007, is rejected u/s 245D(1) or any other application made u/s 245C is not allowed to be proceeded or is declared invalid or an order has not been passed within the time period, the Assessing Officer shall allow the credit for the tax and interest paid on or before the date of making the application or during the pendency of the case before Settlement Commission.

16.1.16 Order of the Settlement Commission to be conclusive [Section 245-I]

Order passed by the Commission u/s 245D(4) is conclusive as to the matter stated therein and no matter covered by such order shall be reopened in any proceeding under this Act or under any other law for the time being in force save as provided under Chapter XIXA. The order of the Commission can only be challenged through a written petition under Article 226 of the Constitution of India in a High Court or through Special Leave Petition under Article 136 in the Supreme Court on the ground that while making such order, principles of the natural justice has been violated or mandatory procedural requirements of law were not complied with or if it is found that there is no nexus between the reasons given and the decision taken.

16.1.17 Payment of the sums due under order of settlement [Section 245J]

Any sum specified in an order of settlement passed u/s 245D(4) may be recovered and any penalty for default in making payment of such sum may be impose and recovered in accordance with the provisions of Chapter XVII by the Assessing Officer having jurisdiction over the person who made the application for settlement u/s 245C.

16.1.18 Bar on subsequent application for settlement in certain cases [Section 254K]

(1) Where—

(i) an order of settlement passed under sub-section (4) of section 245D provides for the imposition of a penalty on the person who made the application under section 245C for settlement, on the ground of concealment of particulars of his income; or

(ii) after the passing of an order of settlement under the said sub-section (4) in relation to a case, such person is convicted of any offence under Chapter XXII in relation to that case; or

(iii) the case of such person was sent back to the Assessing Officer by the Settlement Commission on or before the 1st day of June, 2002,

then, he or any person related to such person (herein referred to as related person) shall not be entitled to apply for settlement under section 245C in relation to any other matter.

(2) Where a person has made an application under section 245C on or after the 1st day of June, 2007 and if such application has been allowed to be proceeded with under sub-section (1) of section 245D, such person or any related person shall not be subsequently entitled to make an application under section 245C.

16.1.19 Proceedings before the Settlement Commission to be judicial proceedings [Section 245L]

Any proceedings under Chapter XIXA before the Settlement Commission shall be deemed to be a judicial proceeding within the meaning of Sec. 193 and 228, and for the purposes of Sec. 196 of the Indian Penal Code.

16.2 ADVANCE RULING

Finance Act, 1993 inserted a Chapter XIX-B in the Income-tax Act, 1961 to provide provisions of **Advance Rulings** to avoid dispute in respect of assessment of Income-tax liability in the case of non-resident. W.e.f. 1.10.1998, the scheme has been extended to cover notified resident applicants also. The Chapter XIX-B contains sections 245N to 245V.

'Advance Ruling' means a determination by the Authority for Advance Rulings, in relation to (i) a transaction which has been undertaken or is proposed to be undertaken by a non-resident or by a resident with a non-resident, including a determination of a question of law or of fact, and (ii) issues relating to computation of income pending before the Income-tax authority or the tribunal including a determination of a question of a law or of fact. [Sec. 245N(a)]

An application may be made by (i) non-resident, (ii) a resident entering into transaction with a non-resident, or (iii) a resident of the notified class or category i.e. a public sector company or a person indulging in a transaction with a non-resident. [Sec. 245N(b)]

Some of the advantages of seeking advance rulings from the Authority are as under:

(i) The non-resident investor can be sure of its liability towards Income-tax even before the start of investment in India. Hence, he can plan his investment accordingly and thus would be able to avoid long-drawn litigation.

(ii) The Authority constituted as above, is best suited to sort out complex issues of Income-tax including those concerning Double Taxation Avoidance Agreements (DTAA) which arise as a result of differences of opinion between the tax collectors and the taxpayers.

(iii) The notified resident i.e. the Public Sector Companies can also take advantage of getting a ruling on questions of facts or law pending before any Tax Authority or Appellate Tribunal.

(iv) The rulings of the Authority are binding on the applicant as well as the Commissioner of Income-tax and authorities below him, not only for one year but for all the years unless the facts or the law change. Therefore, having obtained the ruling on a given set of facts the taxpayer may be sure about his tax liability in future.

(v) The authority is to pronounce its rulings within six months of the receipt of the application. This enables the investor to obtain the ruling and draw up the details of his transaction without undue delay on this account and ensures full certainty regarding its tax implications.

Application for advance ruling should be in the prescribed form as below duly verified, along with a payment of fee of ₹ 2,500 shall be submitted to the authority for advance rulings.

Form No	Class of Assesses
34C	Non- resident desires of obtaining an advance ruling.
34D	Resident persons seeking advance ruling in relation to a transaction with a non-resident.
34E	Resident person of notified class or category.

As per section 245Q, the Central Government shall constitute an authority for giving advance rulings, to be known as Authority for Advance Rulings.

The Authority for Advance Rulings will consist of the following members appointed by the Central Government:

(a) A chairman who will be a retired judge of the Supreme Court,

(b) An officer of the Indian Revenue Service who is qualified to be member of CBDT, and

(c) an officer of the Indian Legal Service who is qualified to be an Additional Secretary to the Government of India.

The office of the Authority shall be located in Delhi.

The constitution of the Authority is such that it functions as an independent quasi-judicial body and for the purpose of exercising its powers, it shall have all the powers of a civil court under the Code of Civil Procedure, 1908 as are referred to in section 131 of the Income Tax Act.

The Authority shall be deemed to be a civil court for the purposes of section 195, but not for the purposes of Chapter XXVI of the Code of Criminal Procedure, 1973 and every proceeding before the Authority shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228, and for the purpose of section 196, of the Indian Penal Code.

Although, all the three Members of the Authority function as a body in disposing off the applications before them, but section 245P makes it clear that no proceeding before the Authority, or the pronouncement of advance ruling by the Authority, shall be questioned or shall be invalid on the ground merely of the existence of any vacancy or defect in the Constitution of the Authority [Section 245P].

An applicant desirous of obtaining an advance ruling under this chapter may take the following:

(1) An application for obtaining an advance ruling under section 245Q(1) shall be made in quadruplicate:

(a) in Form No. 34C in respect of a non-resident applicant;

(b) in Form No. 34D in respect of a resident applicant seeking advance ruling in relation to a transaction undertaken or proposed to be undertaken by him with a non-resident; and

(c) in Form No. 34E in respect of a resident, falling within such class or category of persons notified by the Central Government,

and shall be verified in the manner indicated therein.

Public Sector Company as defined in section 2(36A) of the Income-tax Act has been notified as such class of person as applicant for advance ruling [Notification No. 11456, dated 3-8-2000].

(2) The application should state the question on which the advance rulings is sought.

(3) The application should be accompanied by a fee of ₹2,500 (₹10,000 or such fee as may be prescribed in this behalf whichever is higher) in the form of a demand draft drawn in favour of Authority for Advance Ruling.

(4) The application, its verification, the annexures, to the said application and the statements and documents accompanying it shall be signed by a person mentioned in rule 44E of Income Tax Rules, 1962. Where the authorised representative signs the application and the documents, the application shall be accompanied by a Power of Attorney authorising him to append this signature and an affidavit setting out the unavoidable reasons which entitles him to sign it.

(5) The application should be addressed to the Secretary and can be submitted either in person or by registered post. If it is sent by registered post, it shall be deemed to have been made on the date when it is received in the office of Authority.

(6) If the applicant is not hitherto assessed in India, he shall indicate in Annexure 1 to the application:

(1) his head office in any other country,

(2) the place where his office and residence is located or is likely to be located in India, and

(3) the name and address of his representative in India, if any, authorised to receive notices and papers and act on his behalf.

(7) If the application is found to be defective, the Secretary of the Authority may send the application back to the applicant for removing the defect within such time as he may allow. Such application shall in that case be deemed to have been made on the date on which the application after rectification is submitted.

As per section 44E of the Income Tax Rule, 1962 the application for obtaining advancing ruling should be signed:

(1) in the case of an individual,—

(i) by the individual himself;

(ii) where, for any unavoidable reason, it is not possible for the individual to sign the application, by any person duly authorised by him in this behalf. Provided that the person signing the application holds a valid Power of Attorney from the individual to do so, which shall be attached to the application;

(2) in the case of a Hindu Undivided Family,—

(i) by the karta thereof, and

(ii) where, for any unavoidable reason, it is not possible for the karta to sign the application, by any other adult member of such family;

(3) in the case of a company,—

(i) by the Managing Director thereof, or where for any unavoidable reason such Managing Director is not able to sign and verify the application, or where there is no Managing Director, by any Director thereof;

(ii) where, for any unavoidable reason, it is not possible for the Managing Director or the Director to sign the application, by any person duly authorised by the company in this behalf. Provided that the person signing the application holds a valid Power of Attorney from the company to do so, which shall be attached to the application;

(4) in the case of a firm, by the managing partner thereof, or where for any unavoidable reason such managing partner is not able to sign and verify the application or where there is no managing partner as such, by any partner thereof, not being a minor;

(5) in the case of an association of persons, by any member of the association or the principal officer thereof, and

(6) in the case of any other person, by that person or by some person competent to act on his behalf.

The application should be addressed to the Secretary and can be submitted either in person or by registered post. The number and year of receipt of the application will be filled in the office of the Authority for Advance Rulings. If it is sent by registered post, it shall be deemed to have been made on the date when it is received in the office of Authority.

If the application is found to be defective, the Secretary of the Authority may send the application back to the applicant for removing the defect within such time as he may allow. Such application in that case shall be deemed to have been made on the date on which the application after rectification is submitted.

As per the provisions of sub-section (3) of section 245Q, an application can be withdrawn by the applicant within thirty days from the date of filing of a valid application complete in all respects according to the Act and Rules in the office of the Authority. However, this does not preclude the applicant from withdrawing the application after the said period with the permission of the Authority.

Application made to the Authority for Advance Ruling can be withdrawn after the lapse of 30 days period of application with the permission of authority if facts and circumstances so justify [M.K. Jain AAR No. 644 of 2004. Also see Mr. Manfred Stoehr, Germany AAR No. 594 of 2002].

Where the application for withdrawal was made within period of 30 days of the date of filing of the valid application for Advance Ruling, the application was permitted to be withdrawn [AT&S India Pvt. Ltd. AAR No. 63 of 2005].

Where an application is made earlier, was rejected as the applicant was not a non-resident on that date, the revised application was held to be maintainable if the applicant was non-resident at the time of making the revised application [Rajnikant R Bhatt (Dr) vs. CIT (1996) 222 ITR 562 (AAR-New Delhi)].

An advance ruling shall not be allowed where (i) question of law or fact is already pending either before any Income-tax Authority or the Appellate Tribunal (except in case of a resident applicant of notified class or category) or any court, (ii) a transaction, which is designed for the avoidance of Income-tax; or (iii) determination of the fair market value of any property. However, no application shall be rejected unless an opportunity has been given to the applicant of being heard and if the application is rejected, reasons for such rejection shall be given in the order. [Sec. 245R]

The Authority shall pronounce the advance ruling within six months after the receipt of the application. [Sec. 245R(6)]

In case an application for advance ruling has been made, in respect of an issue by a resident applicant, no Income-tax Authority or the Appellate Tribunal shall give a decision on the same issue. [Sec. 245RR]

The Authority shall not allow an application, in the following cases:

(a) Where the question of law or fact raised in the application is already pending in case of the applicant either before (i) any Income Tax Authority, or (ii) the Appellate Tribunal or (iii) any Court. However, this will not be applicable in case of notified residents, if it is pending before Income-tax Authority or the Appellate Tribunal. But the application in case of notified resident shall also not to be entertained if the issue is pending before any court.

(b) Where the question raised relate to the determination of the fair market value of any property.

(c) Where the transaction in relation to which the question is raised, is designed for the avoidance of Income-tax. However, this will not be applicable in case of notified residents or in case of an applicant falling in section 245N(b)(iiia).

The words already pending should, therefore, be interpreted to mean already pending as on the date of the application and not with reference to any future date. Further pendency must be in case of the applicant [Monte Harris vs. CIT (1996) 218 ITR 413 (AAR)].

In this ruling, AAR has observed as follows:

On account of restrictions under the Indian Law, it may be considered more expedient to channelise all foreign investments into India through a single entity rather than various non-residents making investments individually. This was an important factor which would show that the transaction of investment in India through a company in Mauritius was not designed prima facie for the avoidance of Indian Income-tax. The existence of tax concessions under the DTAA may be only one of the several factors considered by the investor while planning the modality of investments in India. The same may not be the only object or a dominant, object of the transaction. Even though there may be certain suspicious features of such transaction, a ruling cannot be declined on the ground that the transaction was designed for the avoidance of Indian Income-tax.

The authority is prohibited from allowing an application where question involves determination of fair market value of any property and as such where a question was sought by applicant as to whether in light of provisions of section 92C, read with rules 10B and 10C 'Transactional Net Margin Method' is most appropriate method for determination of arm's length price in respect of transaction of services between applicant and Morgan Stanley Advantage Services Private Limited (MSAS) is liable to be rejected [Morgan Stanley & Co. USA (2006) 152 Taxman 1 (AAR-New Delhi)].

Although section 245R(2) give discretion the Authority for Advance Ruling to allow or reject the application, but the first proviso to sub-section (2) to section 245R qualifies the operation of main provision by placing certain restrictions or limitation on the exercise of the power and as such application cannot be admitted if question raised in the application is already pending before any Income Tax Authority or Appellate Tribunal except in case of notified residents [Microsoft Operations Pvt. Ltd. in re (2009) 310 ITR 408 (AAR)].

Advance Ruling sought by the applicant regarding the tax implications of its proposed amalgamation with another company cannot be declined on the ground of pendency of proceedings under the Companies Act [Star Television Entertainment Ltd. & Ors In re (2010) 34 DTR 98 (AAR)].

Merely because the Appellate Tribunal in another case, has decided a similar issue in favour of the revenue, it does not mean that applicant cannot seek Advance Ruling on such issue. There is no impropriety in resorting to remedy conferred by law so long as the applicant comes within four corners of the statuary provisions [Burmah Castrol Plc. In re (2008) 174 Taxman 95 (AAR- New Delhi)].

Where the application for Advance Ruling has been allowed, the Authority shall proceed as under:

(1) **Submission of additional facts before the Authority:** The Authority may at its discretion permit or require the applicant to submit such additional facts as may be necessary to enable it to pronounce its advance ruling.

(2) **Hearing of application:** The authority shall notify the applicant and the Commissioner of the date and place of hearing of the application and shall hear them on the day fixed or any other day to which the hearing may be adjourned.

(3) **Continuation of proceeding after the death of the applicant:** Where the applicant dies or is wound up or dissolved or disrupted or amalgamated or succeeded to by any other person or otherwise comes to an end, the application shall not abate and may be permitted by the Authority, where it considers that the circumstances justify it, to be continued by the executor, administrator or other legal representative of the applicant or by the liquidator, receiver or assignee, as the case may be, on an application made in this behalf.

(4) **Hearing of application ex-parte:** Where on the date fixed for hearing or any other day to which the hearing may be adjourned, the applicant or the Commissioner does not appear in person or through an authorised representative when called on for hearing, the Authority may dispose of the application ex-parte on merits. However, where an application has been disposed of as above and the applicant or the Commissioner, as the case may be, applies within 15 days of receipt of the order and satisfies the Authority that there was sufficient cause for his non-appearance when the application was called upon for hearing, the Authority may, after allowing the opposite party a reasonable opportunity of being heard, make an order setting aside the ex-parte order and restore the application for fresh hearing.

(5) **Pronouncement of Advance Ruling:** The Authority shall, after examining such further material as may be placed before it by the applicant or obtained by the authority, pronounce its advance ruling on the question specified in the application.

(6) **Time limit for pronouncement of Advance Ruling:** The authority shall pronounce its advance ruling in writing within 6 months of the receipt of application. However, it is made clear that the time limit of six months for pronouncing advance ruling is not mandatory and an advance ruling given after the expiry of six months is not invalid as being beyond the said period.

(7) **Order of Advance Ruling to be sent:** A copy of the advance ruling pronounced by the authority, duly signed by the members and certified in prescribed manner, shall be sent to the applicant and to the Commissioner, as soon as may be, after such pronouncement. In this connection rule 26 provides as under:

(a) Every order of the Authority under Chapter XIX-B shall be duly signed by the members and bear the official seal of the Authority.

(b) One certified copy of such order of the Authority shall be communicated to the applicant and the Commissioner under the signature of the Secretary or any other officer of the Authority authorised by him in this behalf and bear the official seal of the Authority.

(8) **Modification of the order:** Where the Authority finds suo motu or on a representation made to it by the applicant or the Commissioner or otherwise, but before the ruling pronounced by the Authority has been given effect to by the Assessing Officer, that there is a change in law or facts on the basis of which the ruling was pronounced, it may be order modify such ruling in such respects as it considers appropriate, after allowing the applicant and the Commissioner a reasonable opportunity of being heard.

(9) **Rectification of mistakes:** (i) The Authority may, with a view to rectifying any mistake apparent from the record, amend any order passed by it before the ruling pronounced by the Authority has been given effect to by the Assessing Officer. (ii) Such amendment may be made suo motu or when the mistake is brought to its notice by the applicant or the Commissioner, but only after allowing the applicant and the Commissioner reasonable opportunity of being heard.

The advance ruling shall be binding only on the applicant who has sought it in respect of the specific transaction covered thereunder, on the Commissioner and the Income-tax Authorities subordinate to him, having jurisdiction over the applicant. The advance ruling will continue to remain in force unless there is a change either in law or in fact on the basis of which the advance ruling was pronounced. [Sec. 245S]

Case Laws:

(i) Settlement Commission cannot be equated with CBDT for exercise of power of relaxation under section 119(2)(a) - CIT vs. Anjum M.H. Ghaswala 119 Taxman 352/ 252 ITR 1.

(ii) Commission is not bound to proceed with any application filed under section 245C - CIT vs. Hindustan Bulk Carriers 259 ITR 449/126 Taxman 321.

According to section 245T, the advance ruling shall be void if it is subsequently found by the authority, on a representation made to it by Commissioner or revenue, to have been obtained by fraud or misrepresentation of facts. However on receipt of such representation, a notice shall be issued to the applicant along with a copy of the representation for rebuttal and reasonable opportunity shall be allowed to the applicant and the Commissioner for being heard before passing order declaring the advance ruling to be void.

As per section 245U, the authority has all the powers of a Civil Court in respect of —

(a) discovery and inspection;

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

(c) issuing commissions and compelling the production of books of account and other records.

While considering the maintainability of an application under this Chapter, the basic question to be decided is whether the applicant is a non-resident but the Chapter does not specifically state that he should be a non-resident as on the date of the application. In the case of Robert W. Smith vs. CIT (1995) 212 ITR 275 (ARR-New Delhi), Authority for Advance Ruling has ruled that the question of residence must be determined with reference to the previous year and not with reference to a particular date.

However, such previous year cannot be the previous year in which the application is made as the application may be made very early in a financial year and may be disposed of much before the end of the financial year. In such a case the full picture of the stay of the assessee in the previous year shall not be available at the time of application or even by the date of its disposal by the authority. Thus, the only previous year with reference to which the status of the applicant is determinable for the purpose of section 245N must be the previous year preceding the financial year in which application is made.

An advance ruling is to be sought only in respect of transactions undertaken or proposed to be undertaken by a non-resident. The non-resident cannot seek ruling from the Advance Ruling Authority as to whether its Indian subsidiary would be entitled to tax exemption under section 10A of the Income-tax Act as the tax exemption of the Indian subsidiary is not in consequence of the transaction undertaken or proposed to be undertaken by the non-resident applicant. Hence, the application for advance ruling was not maintainable [Connecteurs Cinch, S.A., In re (2004) 268 ITR 29 (AAR-New Delhi)].

Where non-resident company sought advance ruling on questions relating to a loan transaction between its two Indian subsidiary companies, the Authority for Advance Rulings (AAR) observed that the definition of 'advance ruling' under section 245N(a) has two clauses. For attracting the provisions of clause (i) of this section, the applicant should be a non-resident and the transaction has to be undertaken or proposed to be undertaken by the non-resident applicant. From the facts of the case, it is evident that the applicant is a non-resident but the loan transaction is between 'A Ltd' and 'B Ltd', both of which are residents of India. Therefore, the requirements of clause (i) are not satisfied in this case. Hence, the determination would not fall under clause (i). For the provisions of clause (ii) of this section to be applicable, the question should relate to determination of tax liability of a non-resident in respect of transactions undertaken or proposed to be undertaken by a resident applicant with such non-resident. The applicant is a non-resident and further the transaction of loan was undertaken by two resident companies. The question of tax liability of the non-resident also does not arise. Therefore, it follows that no determination under clause (ii) of this section can be made. Hence, the application was not maintainable due to the aforesaid reasons [X Ltd Netherlands, In re (2005) 275 ITR 327 (AAR-New Delhi)].

The applicant a foreign company entered into a share purchase agreement with the shareholder as well as the Indian company. The Indian company was earlier a partnership firm and it was registered as company under Part IX of the Companies Act. In case such registration under Part IX of the Companies Act may not be held as transfer, the firm, after revaluation of its assets and crediting the excess to the respective partners accounts also satisfied the conditions laid down under section 47(xii) and the erstwhile partners were supposed to hold 50% or more voting power for a period of 5 year from the date of conversion. However, by virtue of transaction with applicant for purchase of shares, that condition of 5 years continuance has been violated and therefore the applicant had filed an application seeking advance ruling on effect of transaction for purchase of share on capital gain tax liability in the hands of the company.

On the facts stated by the applicant, it appears prima facie that the determination sought by the applicant is in relation to the tax liability of an Indian company and, therefore, a doubt has arisen whether the applicant, being a non-resident, can seek 'advance ruling' as per section 245N(a).

Having regard to the wider language of sub-clause (i) of section 245N(a) in contrast with the language employed in sub-clause (ii), the application is maintainable. There is no specific requirement in sub-clause (i) that determination should relate to the tax liability of a non-resident. Going by the averments of the applicant, it is clear that the capital gains tax issue arising in the case of the acquired Indian company has a direct and substantial impact on the applicant's business in view of the stipulations in share purchase agreement. Sub-clause (i) has to be construed in a wider sense and, moreover, a remedial provision shall be liberally construed. Therefore, the question raised by the applicant falls within the definition of 'advance ruling' under section 245N(a). Accordingly, the application is to be allowed under section 245R(2) [Umicore Finance, In re (2009) 184 Taxman 99 (AAR-New Delhi)].

Study Note - 17

GRIEVANCES REDRESSAL PROCEDURE

This Study Note includes

17.1 GRIEVANCES REDRESSAL PROCEDURE

When the assessment order is passed against the assessee, and if he is not satisfied with any order passed by the Assessing Officer, he may appeal to higher court. Procedure for appeal is laid down under the act.

The redressal procedure under the act includes the following:

1. Rectification
2. Appeal
3. Revision

17.2 RECTIFICATION

17.2.1 Rectification of mistake [Section 154]

(1) For rectifying any mistake apparent from the record an Income Tax Authority referred to in section 116 may, —

(a) amend any order passed by it under the provisions of this Act;

(b) amend any intimation or deemed intimation under sub-section (1) of section 143;

(c) amend any intimation under sub-section (1) of section 200A w.e.f. 1.7.12;

(d) amend any intimation under sub-section (1) of section 206CB.

(1A) Where any matter has been considered and decided in any proceeding by way of appeal or revision relating to an order referred to in sub-section (1), the authority passing such order may, notwithstanding anything contained in any law for the time being in force, amend the order under that sub-section in relation to any matter other than the matter which has been so considered and decided.

(2) Subject to the other provisions of this section, the authority concerned-

(a) may make an amendment under sub-section (1) of its own motion, and

(b) shall make such amendment for rectifying any such mistake which has been brought to its notice by the assessee or by the deductor or by the collector, and where the authority concerned is the Commissioner (Appeals), by the Assessing Officer also.

(3) An amendment, which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee or the deductor or the collector, shall not be made under this section unless the authority concerned has given notice to the assessee or the deductor or the collector of its intention so to do and has allowed the assessee or the deductor or the collector a reasonable opportunity of being heard.

17.2.2 At whose instance mistakes can be rectified :

- The concerned authority may [implies discretion] make the necessary amendment of its own motion.
- The concerned authority has to make [implies that there is no discretion] such amendment for rectifying any mistake brought to its notice by the assessee.
- Where the concerned authority is the Commissioner (Appeals) and the mistake has been brought to his notice by the Assessing Officer, it has to make such amendment [implies that there is no discretion].

17.2.3 Procedure for such rectification under sub-section (3),(5) and (6):

- An amendment of the following nature can be made only after the concerned authority has given notice in this respect and also a reasonable opportunity of being heard to the assessee or deductor or the collector-
  - (a) Amendment which enhances an assessment.
  - (b) Amendment which reduces a refund.
  - (c) Amendment which otherwise increases the liability of the assessee or deductor or the collector.
- If any amendment enhances the assessment or reduces a refund already made, a notice of demand is served on the assessee or deductor or the collector. Such notice is deemed to be a notice u/s 156.
- If any amendment reduces the assessment, refund due to the assessee is made unless it is withheld u/s 241.

17.2.4 Time Limit for Rectification:

Period of limitation for making rectification as prescribed in sub-section (7) of section154 is as follows:

- No amendment under this section can be made after the **expiry of 4 years** from the end of the financial year in which the order sought to be amended was passed. It may be noted that an amendment is made when the related order is passed.
- This period of limitation is not applicable in case the provision of section 155 are applicable.
- However, if a valid application has been made by the assessee for rectification within the statutory time limit but is not disposed of by the concerned authority within the time specified, it may be disposed of even after the expiry of such time limit [Circular No. 73, dated 7th January, 1972]. This relief is, however, not admissible in case rectification proceedings are initiated by the department itself.

17.2.5 Action against rectification order:

Following action may be taken against a rectification order:

- Appeal can be made to the Commissioner (Appeals) u/s 246A. Appeal can also be made against an order passed under this section refusing to rectify a mistake [Chennai Prop. & Inv. Ltd. vs. CIT [2001] 247 ITR 226 (Mad.)].
- Appeal can be made to the Appellate Tribunal u/s 253.
- Revision application can be made u/s 264.

17.2.6 Other amendments- For Rectification of Assessment of a Firm [Section 155]:

(1) Where, in respect of any completed assessment of a partner in a firm for the Assessment Year commencing on the 1st day of April, 1992, or any earlier Assessment Year, it is found-

   (a) on the assessment or reassessment of the firm, or

   (b) on any reduction or enhancement made in the income of the firm under this section, section 154, section 250, section 254, section 260, section 262, section 263 or section 264, or

(c) on any order passed under sub-section (4) of section 245D on the application made by the firm, that the share of the partner in the income of the firm has not been included in the assessment of the partner or, if included, is not correct, the Assessing Officer may amend the order of assessment of the partner with a view to the inclusion of the share in the assessment or the correction thereof, as the case may be; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the final order was passed in the case of the firm.

(2) Where as a result of proceedings initiated under section 147, a loss or depreciation has been recomputed and in consequence thereof it is necessary to recompute the total income of the assessee for the succeeding year or years to which the loss or depreciation allowance has been carried forward and set off under the provisions of sub-section (1) of section 72, or sub-section (2) of section 73, or sub-section (1) or sub- section (3) of section 74, or sub-section (3) of section 74A, the Assessing Officer may proceed to recompute the total income in respect of such year or years and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the order was passed under section 147.

(3) Where any deduction in respect of any expenditure on scientific research has been made in any Assessment Year under sub-section (2B) of section 35 and the assessee fails to furnish a certificate of completion of the programme obtained from the prescribed authority within one year of the period allowed for its completion by such authority, the deduction originally made in excess of the expenditure actually incurred shall be deemed to have been wrongly made, and the Assessing Officer may, notwithstanding anything contained in this Act, recompute the total income of the assessee for the relevant Previous Year and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the Previous Year in which the period allowed for the completion of the programme by the prescribed authority expired.

(4) Where as a result of any proceeding under this Act, in assessment for any year of a company is whose case an order under section 104 has been made for that year, it is necessary to recompute the distributable income of that company, the Assessing Officer may proceed to recompute the distributable income and determine the tax payable on the basis of such recomputation and make the necessary amendment; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the final order was passed in the case of the company in respect of that proceeding.

(5) Where in the assessment for any year, a capital gain arising from the transfer of a long-term capital asset, is charged to tax and within a period of six months after the date of such transfer, the assessee has made any investment or deposit in any specified asset within the meaning of Explanation 1 to sub- section (1) of section 54E, the Assessing Officer shall amend the order of assessment so as to exclude the amount of the capital gain not chargeable to tax under the provisions of sub-section (1) of section 54E; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the financial year in which the assessment was made.

(6) Where in the assessment for any year, a capital gain arising from the transfer of any original asset as is referred to in section 54H is charged to tax and within the period extended under that section the assessee acquires the new asset referred to in that section or, as the case may be, deposits or invests the amount of such capital gain within the period so extended, the Assessing Officer shall amend the order of assessment so as to exclude the amount of the capital gain not chargeable to tax under any of the sections referred to in section 54H; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of section 154 being reckoned from the end of the Previous Year in which the compensation was received by the assessee.

(7) Where in the assessment for any year commencing before the 1st day of April, 1988, the deduction under section 80-O in respect of any income, being the whole or any part of income by way of royalty, commission, fees or any similar payment as is referred to in that section, has not been allowed on the ground that such income has not been received in convertible foreign exchange in India, or having been received in convertible foreign exchange outside India, or having been converted into convertible foreign exchange outside India, has not been brought into India, by or on behalf of the assessee in accordance with any law for the time being in force for regulating payments and dealings in foreign exchange and subsequently such income or part thereof has been or is received in, or brought into, India in the manner aforesaid, the Assessing Officer shall amend the order of assessment so as to allow deduction under section 80-O in respect of such income or part thereof as is so received in, or brought into, India; and the provisions of section 154 shall, so far as may be, apply thereto, the period of four years specified in sub-section (7) of that section being reckoned from the end of the Previous Year in which such income is so received in, or brought into, India; so, however, that the period from the 1st day of April, 1988 to the 30th day of September, 1991 shall be excluded in computing the period of four years.

(8) Where in the assessment for any year, the deduction under section 80HHB or section 80HHC or section 80HHD or section 80HHE or section 80-O or section 80R or section 80RR or section 80RRA has not been allowed on the ground that such income has not been received in convertible foreign exchange in India, or having been received in convertible foreign exchange outside India, or having been converted into convertible foreign exchange outside India, has not been brought into India, by or on behalf of the assessee with the approval of the Reserve Bank of India or such other authority as is authorised under any law for the time being in force for regulating payments and dealings in foreign exchange and subsequently such income or part thereof has been or is received in, or brought into, India in the manner aforesaid, the Assessing Officer shall amend the order of assessment so as to allow deduction under section 80HHB or section 80HHC or section 80HHD or section 80HHE or section 80-O or section 80R or section 80RR or section 80RRA, as the case may be, in respect of such income or part thereof as is so received in, or brought into, India; and the provisions of section 154 shall, so far as may be, apply thereto, and the period of four years shall be reckoned from the end of the Previous Year in which such income is so received in, or brought into, India.

(9) Where in the assessment for any year, a capital gain arising from the transfer of a capital asset, being land or building or both, is computed by taking the full value of the consideration received or accruing as a result of the transfer to be the value adopted or assessed by any authority of a State Government for the purpose of payment of stamp duty in accordance with sub-section (1) of section 50C, and subsequently such value is revised in any appeal or revision or reference referred to in clause (b) of sub-section (2) of that section, the Assessing Officer shall amend the order of assessment so as to compute the capital gain by taking the full value of the consideration to be the value as so revised in such appeal or revision or reference; and the provisions of section 154 shall, so far as may be, apply thereto, and the period of four years shall be reckoned from the end of the Previous Year in which the order revising the value was passed in that appeal or revision or reference.

17.3 APPEAL AND APPELLATE HIERARCHY

Appeal is a complaint to a higher court relating to an injustice done by a lower court. The party complaining is called "appellant" and the other party is known as "respondent". There are various provisions in the Income-tax Act relating to appeals and revision of orders.

Under the Income-tax Act, the following remedial measures are available to the assessees if he is not satisfy with any order passed by the Assessing Officer :-

(i) **Appeal** w.e.f. 1.10.1998 first shall lie with the Commissioner of Income Tax (Appeals) against the order of the Assessing Officer (sec. 246A), or

(ii) **Revision** if appeal is not preferred or it could not be filed within the time limit allowed, the assessee can apply u/s. 264 to the Commissioner of Income Tax for revision of orders passed by the Assessing Officer.

The Commissioner of Income-tax can also take up suo moto the case for revision. Where, however, in the opinion of the Commissioner of Income Tax the order passed by the Assessing Officer is erroneous and prejudicial to the interest of revenue, the Commissioner of Income Tax can also take up the case for revision u/s. 263.

The assessee can file an appeal against the orders of the Commissioner (Appeals) or the revision orders of the CIT under section 263 in the following cases:

(a) Second Appeal: If the assessee is not satisfied with the order passed by the Commissioner (Appeals), he can appeal against that order to the Appellate Tribunal. Similarly, the CIT may also direct the Assessing Officer to file an appeal against that order with the Appellate Tribunal if the Revenue is not satisfied with the order of the Commissioner (Appeals).

(b) Appeal against revision: If the revision of the order of Assessing Officer is done under section 264, by CIT which is revision in favour of the assessee, no appeal can be filed against this order under the Income-tax Act. However, writ under Article 226 or 227 is possible. On the other hand, if the revision order is passed under section 263 by CIT, which is known as revision of orders prejudicial to the interest of revenue, the assessee can file an appeal with the Appellate Tribunal.

If the assessee or the CIT is not satisfied with the order of the Appellate Tribunal, the appeal lies to the High Court/National Tax Tribunal, if the High Court/National Tax Tribunal is satisfied that the case involves a substantial question of law.

If the assessee or the CIT is not satisfied with the order passed by the High Court, they may file an appeal against the order of the High Court to the Supreme Court, provided it is treated as a fit case by the High Court. The Supreme Court is the final appellate authority.

17.3.1 Appealable orders before Commissioner (Appeals) [Section 246A]

(1) Any assessee or any deductor or any collector aggrieved by any of the following orders (whether made before or after the appointed day) may appeal to the Commissioner (Appeals) against—

- (a) an order passed by a Joint Commissioner under clause (ii) of sub-section (3) of section 115VP or an order against the assessee where the assessee denies his liability to be assessed under this Act or an intimation under sub-section (1) or sub-section (1B) of section 143 or sub-section (1) of section 200A or sub-section (1) of section 206CB, where the assessee or the deductor or the collector objects to the making of adjustments, or any order of assessment under sub-section (3) of section 143 except an order passed in pursuance of directions of the Dispute Resolution Panel or an order referred to in sub-section (12) of section 144BA or section 144, to the income assessed, or to the amount of tax determined, or to the amount of loss computed, or to the status under which he is assessed;
- (aa) an order of assessment under sub-section (3) of section 115WE or section 115WF, where the assessee, being an employer objects to the value of fringe benefits assessed;
- (ab) an order of assessment or reassessment under section 115WG;
- (b) an order of assessment, reassessment or recomputation under section 147 except an order passed in pursuance of directions of the Dispute Resolution Panel or an order referred to in sub-section (12) of section 144BA or section 150;
- (ba) an order of assessment or reassessment under section 153A except an order passed in pursuance of directions of the Dispute Resolution Panel or an order referred to in sub-section (12) of section 144BA;
- (bb) an order of assessment or reassessment under sub-section (3) of section 92CD;

(c) an order made under section 154 or section 155 having the effect of enhancing the assessment or reducing a refund or an order refusing to allow the claim made by the assessee under either of the said sections [except an order referred to in sub-section (12) of section 144BA;

(d) an order made under section 163 treating the assessee as the agent of a non-resident;

(e) an order made under sub-section (2) or sub-section (3) of section 170;

(f) an order made under section 171;

(g) an order made under clause (b) of sub-section (1) or under sub-section (2) or sub-section (3) or sub-section (5) of section 185 in respect of an assessment for the assessment year commencing on or before the 1st day of April, 1992;

(h) an order cancelling the registration of a firm under sub-section (1) or under sub-section (2) of section 186 in respect of any assessment for the assessment year commencing on or before the 1st day of April, 1992 or any earlier assessment year;

(ha) an order made under section 201;

(hb) an order made under sub-section (6A) of section 206C;

(i) an order made under section 237;

(j) an order imposing a penalty under—

(A) section 221; or

(B) section 271, section 271A, section 271AAA, section 271AAB, section 271F, section 271FB, section 272AA or section 272BB;

(C) section 272, section 272B or section 273, as they stood immediately before the 1st day of April, 1989, in respect of an assessment for the assessment year commencing on the 1st day of April, 1988, or any earlier assessment years;

(ja) an order of imposing or enhancing penalty under sub-section (1A) of section 275;

(k) an order of assessment made by an Assessing Officer under clause (c) of section 158BC, in respect of search initiated under section 132 or books of account, other documents or any assets requisitioned under section 132A on or after the 1st day of January, 1997;

(l) an order imposing a penalty under sub-section (2) of section 158BFA;

(m) an order imposing a penalty under section 271B or section 271BB;

(n) an order made by a Deputy Commissioner imposing a penalty under section 271C, section 271CA, section 271D or section 271E;

(o) an order made by a Deputy Commissioner or a Deputy Director imposing a penalty under section 272A;

(p) an order made by a Deputy Commissioner imposing a penalty under section 272AA;

(q) an order imposing a penalty under Chapter XXI;

(r) an order made by an Assessing Officer other than a Deputy Commissioner under the provisions of this Act in the case of such person or class of persons, as the Board may, having regard to the nature of the cases, the complexities involved and other relevant considerations, direct.

Explanation.—For the purposes of this sub-section, where on or after the 1st day of October, 1998, the post of Deputy Commissioner has been redesignated as Joint Commissioner and the post of Deputy Director has been redesignated as Joint Director, the references in this sub-section for “Deputy Commissioner” and “Deputy Director” shall be substituted by “Joint Commissioner” and “Joint Director” respectively.

(1A) Every appeal filed by an assessee in default against an order under section 201 on or after the 1st day of October, 1998 but before the 1st day of June, 2000 shall be deemed to have been filed under this section.

(1B) Every appeal filed by an assessee in default against an order under sub-section (6A) of section 206C on or after the 1st day of April, 2007 but before the 1st day of June, 2007 shall be deemed to have been filed under this section.

(2) Notwithstanding anything contained in sub-section (1) of section 246, every appeal under this Act which is pending immediately before the appointed day, before the Deputy Commissioner (Appeals) and any matter arising out of or connected with such appeals and which is so pending shall stand transferred on that date to the Commissioner (Appeals) and the Commissioner (Appeals) may proceed with such appeal or matter from the stage at which it was on that day.

Provided that the appellant may demand that before proceeding further with the appeal or matter, the previous proceeding or any part thereof be reopened or that he be re-heard.

Explanation.— For the purposes of this section, "appointed day" means the day appointed by the Central Government by notification in the Official Gazette.

Case Laws:

(1) Non-allowing of interest in rectification order is appealable**:** When the ITO rectifies an assessment under section 154/155 and grants refund but fails to grant interest on the refund, such rectificatory order has the effect of reducing the amount payable to the assessee and hence appealable under section 246(1)(*b*) - *CIT* vs. *Perfect Pottery Co. Ltd.*173 ITR 545

(2) Denial of liability to tax under particular circumstances is also covered - The expression 'denial of liability' is comprehensive enough to take in not only the total denial of liability but also the liability to tax under particular circumstances. Thus, an assessee has a right of appeal against the order of the ITO assessing the AOP instead of the members thereof individually - *CIT* vs. *Kanpur Coal Syndicate* 53 ITR 225

(3) Objection as to place of assessment cannot be raised - No appeal can lie against an order determining the place of assessment - *Rai Bahadur Seth Teomal* vs. *CIT* 36 ITR 9

In case of adverse order passed in the matter of deceased person, his legal heirs can file appeal.

In case of HUF, Karta can file appeal. However, after the partition, if any adverse order is passed in respect of pre-partition HUF, erstwhile coparceners can prefer an appeal.

The right of appeal is not confined merely to the assessee on whom order of assessment has been made but to any assessee aggrieved by the said order e.g. beneficiary may be aggrieved for an order made on the trust [CGT vs. A.C. Mahesh (2001) 252 ITR 440 (Mad)].

As per section 248 where under an agreement or other arrangement, the tax deductible on any income, other than interest, under section 195 is to be borne by the person by whom the income is payable, and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, he may appeal to the Commissioner (Appeals) for a declaration that no tax was deductible on such income.

Dispute relating to the chargeability of income of the non-resident recipient can alone be the subject matter of an appeal under section 248 and not the possibility of assessing of the income of the non-resident in the hands of the resident payer as no procedure of assessment of the income of the non-resident in the hands of the resident payer is contemplated in sub-section 1 of section 195 [CIT vs. Sonata Information Technology Ltd (2010) 38 DTR 350 (Kar)].

However, no appeal lies under the Income-tax Act against the following orders:

(i) Order levying interest under sections 234A, 234B and 234C. However in some special cases there can be waiver of interest by the Chief Commissioner or the Director General of Income-tax;

(ii) Revision order under section 264. However, in this case a writ can be filed in the High Court;

(iii) Order of Authority for Advance Rulings;

(iv) Order of Settlement Commission.

17.3.2 Appeal by person denying liability to deduct tax in certain cases.[Section 248]

Where under an agreement or other arrangement, the tax deductible on any income, other than interest, under section 195 is to be borne by the person by whom the income is payable, and such person having paid such tax to the credit of the Central Government, claims that no tax was required to be deducted on such income, he may appeal to the Commissioner (Appeals) for a declaration that no tax was deductible on such income.

Case Law:

AAC can determine quantum also : In an appeal filed under section 248, AAC has jurisdiction to deal with the quantum of sum chargeable under the provisions of the Act on which the assessee is liable to deduct tax under section 195 - CIT vs. Westman Engg. Co. (P.) Ltd. 188 ITR 327

17.3.3 Procedure for filing appeal [Section 249 & Rules 45 & 46]

(i) An appeal in Form No. 35 should be filed within 30 days of -

   (a) the date of service of notice of demand relating to assessment or penalty if it relates to assessment or penalty; or

   (b) the date of payment of tax, if it relates to any tax deducted u/s. 195(1) in respect of payment to non-resident in certain cases; or

   (c) the date on which intimation of the order sought to be appealed against is served if it relates to any other cases.

   The Commissioner of Income-tax (Appeals) may condone the delay in filing appeal petition if he satisfied that the appellant had sufficient cause for not presenting it within that period.

(ii) No appeal shall be admitted unless at the time of filing of appeal the appellant has paid :–

   (a) the tax due on the income returned by him, or

   (b) where no return has been filed the assessee has paid the amount equal to the amount of advance tax which was payable by him. However, the Commissioner (Appeals) may, for any good and sufficient reason to be recorded in writing, exempt the appellant from the payment of such tax.

(iii) Appeal is required to be made in duplicate. The memorandum of appeal, statement of facts and grounds of appeal should be accompanied by a copy of the order appealed against and the notice of demand in original, if any.

(iv) **Fee for filing appeal :** The memorandum of appeal shall be accompanied by a fee as under :–

(a)	Where assessed income is ₹ 1,00,000 or less	₹ 250
(b)	Where assessed income exceeds ₹ 1,00,000 but does not exceed ₹ 2,00,000	₹ 500
(c)	Where assessed income exceeds ₹ 2,00,000	₹ 1,000
(d)	other case except (a),(b) & (c)	₹ 250

W.e.f. 1.6.1999 fee for filing appeal relating to matters which may not have nexus with the returned income (e.g. TDS defaults, non-filing of return) has been prescribed to be ₹ 250 for appeal before Commissioner (Appeals). [Sec. 249]

The Commissioner (Appeals) after hearing the assessee and the income-tax department will pass an order in writing and communicate his order to the Assessee and the Commissioner of Income Tax. The Commissioner (Appeals) may confirm, reduce, enhance or annul an assessment against which the appeal is made. However, he has no power to set aside the assessment and refer the case back to the Assessing Officer for making a fresh assessment according to his direction. He may confirm or cancel the order of penalty. In other cases, he can pass such orders as he thinks fit. [Sec. 251]

Case Laws:

(1) Demand notice need not be enclosed to memo of appeal - Neither section 249 nor rule 45 makes it incumbent on the assessee-appellant to enclose the demand notice along with the memo of appeal - *Addl. CIT* vs. *Prem Kumar Rastogi* 115 ITR 503

(2) Appellate authority is statutorily bound to consider condonation of delay - Where an application for condonation of delay in filing an appeal is preferred, it is the statutory obligation of the appellate authority to consider whether sufficient cause for not presenting the appeal in time was shown by the appellant - Shrimant Govindrao Narayanrao Ghorpade vs. CIT 48 ITR 54

(3) Where an assessee was served a notice of demand which did not include interest and subsequently another notice of demand was served including the interest, it was held that the period of limitation would begin from the date of service of second notice of demand [CIT vs. Karnani Industrial Bank Ltd. (1978) 113 ITR 380 (Cal)].

(4) Where a notice of demand was served on assessee's partner who subsequently handed over the notice to the assessee, it was held that period of limitation would begin when assessee received the notice [Fatechand Agarwal vs. CIT (1974) 97 ITR 701 (Ori)].

(5) When only the notice of demand is served without a copy of the order, the period of 30 days would be counted from the day assessee receives a copy of the order [Karamchand Thapar (1976) 38 STC 593 (SC)].

(6) When an appeal is sent by an assessee by post, the date of filing of appeal would be the date on which the same is received by the Appellate Authority and not the date of posting the same [Titaghar Paper Mills Co. Ltd. (1980) Tax LR (NOC) 110 (Cal)].

(7) The Appellate Authority may condone the delay even where there is no such application made by the assessee. Appellate Authority is not competent to straightway dismiss an appeal filed belatedly [Markland Pvt. Ltd. vs. State of Gujarat AIR 1989 Guj 44; Naran Annappa vs. Jayanti Lal Chunilal Shah AIR 1987 Guj 205].

(8) The statutory right of appeal must be construed in furtherance of justice and the liberal meaning given to the expression sufficient cause. The Appellate Authority must examine whether there is a good reason for delay and that the appellant did act with reasonable diligence [Sandhya Rani Sarkar vs. Sudha Rani Debi AIR 1978 SC 537].

(9) The quantum of stakes involved and the importance of the issues raised are relevant considerations, while deciding on the condonation of delay [Gupta Rice Mills (1993) 91 STC 208 (All)].

(10) A subsequent decision of the Supreme Court or a High Court resulting in change of legal position may be a sufficient cause for condonation of delay [CIT vs. Sothia Mining & Mfg. Corp. (1990) 186 ITR 182(Cal)].

(11) Time taken in pursuing other remedies may be a valid cause for delay [CIT vs. K.S.P. Shanmugavel Nadar & Ors (1985) 153 ITR 596 (Mad)].

(12) The pendency of a writ before the High Court, and Special Leave Petition before the Supreme Court, has been held as sufficient cause for condoning the delay [Madura Coats Ltd. vs. Collector of Central Excise (1994)119 CTR 63 (SC)].

(13) It is important to bear in mind that there should be a sufficient cause, before the date of limitation. Events subsequent to the expiry of limitation may justify only further delay, but not the delay caused before the original limitation expired [Ajit Singh Thakur Singh vs. State of Gujarat AIR 1981 SC 733].

(14) Where the delay was alleged to be on account of illness but the medical certificate was not filed, in spite of an opportunity having been given, the refusal to condone the delay was justified [Sital Prasad vs. CIT (1991) 187 ITR 135 (All)].

(15) The order refusing the prayer for condonation of delay must be a speaking order, recording reasons. Where the orders do not contain any cogent reasons, the orders cannot be sustained [Jaimangal Lrd. Avantee Hotel vs. State of Bihar AIR 1989 Pat 190].

(16) The power of condonation is expected to be exercised liberally so as to advance the cause of justice [Voltas Ltd. vs. DCIT (2000) 241 ITR 471 (AP)]. This decision is in line with the view taken by the Supreme Court in Collector, Land Acquisition vs. Mst. Katiji (1987) 167 ITR 471 (SC).

(17) The order passed by the Commissioner (Appeals) rejecting the application for exemption from payment of tax which resulted into non-admittance of the appeal amounted to an order disposing of the appeal under section 250 and therefore appeal lies to the Appellate Tribunal [CIT vs. Nanhibai Jaiswal (1988) 171 ITR 646 (MP)].

(18) If the appeal is filed without the payment of tax on returned income but subsequently the required amount of tax is paid, the appeal shall be admitted on payment of tax and appeal has to be decided on merit [Bhumiraj Constructions vs. Addl. CIT (2011) 49 DTR 195 (Trib.) (Mumbai)].

17.3.4 Procedure in appeal [Section 250]

(1) The Commissioner (Appeals) shall fix a day and place for the hearing of the appeal, and shall give notice of the same to the appellant and to the Assessing Officer against whose order the appeal is preferred.

(2) The following shall have the right to be heard at the hearing of the appeal—

(*a*) the appellant, either in person or by an authorized representative;

(*b*) the Assessing Officer, either in person or by a representative.

(3) The Commissioner (Appeals) shall have the power to adjourn the hearing of the appeal from time to time.

(4) The Commissioner (Appeals) may, before disposing of any appeal, make such further inquiry as he thinks fit, or may direct the Assessing Officer to make further inquiry and report the result of the same to the Commissioner (Appeals).

(5) The Commissioner (Appeals) may, at the hearing of an appeal, allow the appellant to go into any ground of appeal not specified in the grounds of appeal, if the Commissioner (Appeals) is satisfied that the omission of that ground from the form of appeal was not wilful or unreasonable.

(6) The order of the Commissioner (Appeals) disposing of the appeal shall be in writing and shall state the points for determination, the decision thereon and the reason for the decision.

(6A) In every appeal, the Commissioner (Appeals), where it is possible, may hear and decide such appeal within a period of one year from the end of the financial year in which such appeal is filed before him under sub-section (1) of section 246A.

(7) On the disposal of the appeal, the Commissioner (Appeals) shall communicate the order passed by him to the assessee and to the [Chief Commissioner or Commissioner].

Case Laws:

1) Appeal once filed cannot be withdrawn - An assessee having once filed an appeal, cannot withdraw it. Even if the assessee refuses to appear at the hearing, the AAC can proceed with the enquiry

and if he finds that there has been an under-assessment, he can enhance the assessment - *CIT* vs. Rai Bahadur Hardutroy Motilal Chamaria 66 ITR 443 (SC)/CIT vs. B.N. Bhattachargee 118 ITR 461

2) Revenue can object to delay in filing appeal - If an appeal by an assessee is admitted without the fact of delay in its presentation having been noticed, it is open to the department to raise the objection at the time of hearing of the appeal - *Mela Ram & Sons* vs. *CIT* 29 ITR 607

17.3.5 Powers of the Commissioner (Appeals) [Section 251]

(1) In disposing of an appeal, the Commissioner (Appeals) shall have the following powers—

(*a*) in an appeal against an order of assessment, he may confirm, reduce, enhance or annul the assessment;

(*b*) in an appeal against the order of assessment in respect of which the proceeding before the Settlement Commission abates under section 245HA, he may, after taking into consideration all the materials and other information produced by the assessee before, or the results of the inquiry held or evidence recorded by, the Settlement Commission, in the course of the proceedings before it and such other material as may be brought on his record, confirm, reduce, enhance or annul the assessment;

(c) in an appeal against an order imposing a penalty, he may confirm or cancel such order or vary it so as either to enhance or to reduce the penalty;

(*d*) in any other case, he may pass such orders in the appeal as he thinks fit.

(2) The Commissioner (Appeals) shall not enhance an assessment or a penalty or reduce the amount of refund unless the appellant has had a reasonable opportunity of showing cause against such enhancement or reduction.

Explanation—In disposing of an appeal, the Commissioner (Appeals) may consider and decide any matter arising out of the proceedings in which the order appealed against was passed, notwithstanding that such matter was not raised before the Commissioner (Appeals) by the appellant.

There is no limitation for exercise of powers of the First Appellate Authority in appeal proceedings. Since the power of enhancement is specifically conferred on the Commissioner, the Commissioner can suo motu deal with the issues which were not the subject matter of appeal [CIT vs. Kashi Nath Chandiwala (2006) 280 ITR 318 (All)].

It has been settled by several decisions, including the decisions of the Supreme Court in CIT vs. McMillan & Co. (1958) 33 ITR 182 (SC); CIT vs. Shapoorji Pallonji Mistry (1962) 44 ITR 891 (SC); CIT vs. Kanpur Coal Syndicate (1964) 53 ITR 225 (SC) and CIT vs. Hardutroy Motilal Chamaria (Rai Bahadur) (1967) 66 ITR 443 (SC) that in disposing of an appeal before him the Appellate Authority can travel over the whole range of the assessment order. He can bring in for assessment sources which have been considered or processed by the Assessing Officer even though the officer may have failed to bring them to tax. In other words, the powers of the Appellate Authority in disposing of an appeal are very wide and plenary, wider than those even of the Tribunal. It is open to him to consider every aspect of the assessment order and given appropriate reliefs or directions.

The Delhi High Court in CIT vs. Sardari Lai & Co. (2002) 120 Taxman 595 (Del) held that the Commissioner (Appeals) has no power to deal with an altogether new source of income or issue, which had not been considered by the Assessing Officer. The High Court suggested that in such a case the remedy lies either under section 147 or 148 or section 263.

With effect from 1-6-2001, the Commissioner (Appeal) does not have any power to set aside the assessment for fresh assessment by the Assessing Officer.

An Appellate Authority cannot give direction or finding in respect of other years. Direction or finding can be given only in respect of year or period which is before the authority [Sun Metal Factory (I) (P) Ltd. vs. ACIT (2010) 124 ITD 14 (Chennai)].

Stay of Disputed Demand

An appeal can be filed by the assessee after depositing the tax due on the returned income, but the Assessing Officer normally continue with the recovery proceedings of the tax, demanded as per notice of demand. In such cases the assessee who has presented an appeal against such order can apply to the Assessing Officer for stay of the disputed demand. Where an assessee has presented an appeal under section 246A, the Assessing Officer may, in his discretion, and subject to such conditions as he may think fit to impose in the circumstances of the case, treat the assessee as not being in default in respect of the amount in dispute in the appeal, even though the time for payment has expired, as long as such appeal remains undisposed off.

Under Board Circular No. 530, dated 6-3-1989, the Assessing Officer will exercise his discretion under section 220(6) of the Act (subject to such conditions as he may think fit to impose) so as to treat the assessee as not being in default in respect of the amount in dispute in the appeal in the following situations:

(1) the demand in dispute has arisen because the Assessing Officer had adopted an interpretation of law in respect of which there exists conflicting decisions of one or more High Courts or the High Court of jurisdiction has adopted a contrary interpretation but the Department has not accepted that judgment, or

(2) the demand in dispute relates to issues that have been decided in favour of the assessee in an earlier order by an Appellate Authority or Court in the assessee's own case.

It is clarified that in the situations mentioned in para 2 above, the assessee will be treated as not in default only in respect of the amount attributable to such disputed points. Further, where it is subsequently found that the assessee has not co-operated in the early disposal of appeal or where a subsequent pronouncement by a Higher Appellate Authority or Court alters the situation referred to in para 2 above, the Assessing Officer will no longer be bound by these instructions and will exercise his discretion independently.

In respect of other cases not covered in para 2 above, the Assessing Officer, while considering the situation for treating the assessees to be not in default, would consider all relevant factors which have a bearing on the demand raised and communicate his decision to the assessee in the form of a speaking order.

The Assessing Officer while acting under section 220(6) should not act as a mere tax-gatherer but as a quasi-judicial authority.

Being a quasi-judicial authority, the powers should be exercised judicially, always remembering that—

(a) The power under section 220(6) is coupled with a duty to take into consideration all relevant grounds. It should not be exercised arbitrarily or, capriciously or should not be based on matters extraneous or irrelevant.

(b) The Assessing Officer should apply his mind to the relevant factors such as the assessment history of the assessee, his conduct and cooperation to the Department, the points raised in appeal, chances of recovery in case the appeal is dismissed, the hardship to the assessee by insistence on immediate payment, etc.

(c) He must remember that he is not the final arbiter of the disputes involved, but only the first among the statutory authorities [Rajan Nair (N.) vs. ITO (1987) 165 ITR 650 (Ker)].

Therefore, on a petition for stay the authority concerned, is required to look into the prima facie question involved in appeal and the pleas raised by the assessee. Merely saying that there is no prima facie case for grant of stay is not sufficient [Bhilwara Spinners Ltd. (1991) 83 STC 181 (Raj)].

Paucity of funds can be a ground for stay [Sakarpatal Vibhag Kamgar Sahakari Mandali Ltd. vs. ITO (1992) 198 ITR 685 (Guj)].

The power as well as the discretion to grant or refuse stay rests primarily with the Assessing Officer, and not with his superiors [Savithri Sam (Mrs N.) vs. ITO (1969) 72 ITR 730 (Mad)].

The Assessing Officer has to exercise his discretion on the application for stay in a judicial manner. Refusal of stay although on the ground that the assessee had filed an appeal indicates that refusal was made without application of mind [New Rupayan Jewellers vs. Union of India (2009) 314 ITR 288 (Cal)].

The Madras High Court has held that the First Appellate Authority i.e. the CIT(A) has power to grant stay of demand as the power to grant stay of collection of tax is an inherent and incidental power of the Appellate Authority [Paulsons Litho Works vs. ITO (1994) 208 ITR 676 (Mad)].

Even when the assessee has not filed an application under section 220(b), he can approach the Appellate Authority for staying collection of tax pending the appeal [Kesav Cashew Company vs. Dy. CIT (1994) 210 ITR 1014 (Ker)].

The power of the Appellate Authority to stay the recovery of the demand of dues which are the subject matter of appeal pending before him is independent of the provisions of section 220(6) and it is not necessary that before invoking the power of the First Appellate Authority, an assessee should approach the Assessing Officer under the aforesaid provision or that the Assessing Officer must reject the assessee's prayer for stay of demand [Tin Manufacturing Co. of India vs. CIT (1995) 212 ITR 451 (All)].

A reading of section 220(6) shows that the discretion to be exercised under the section can only be exercised by the Assessing Officer and not by the Commissioner of Income Tax. However, it can be exercised by Commissioner (Appeal) if stay petition is filed before him [Pradeep Ratanshi vs. ACIT (1996) 221 ITR 502 (Ker)].

17.3.6 Appellate Tribunal [Section 252]

(1) The Central Government shall constitute an Appellate Tribunal consisting of as many judicial and accountant members as it thinks fit to exercise the powers and discharge the functions conferred on the Appellate Tribunal by this Act.

(2) A judicial member shall be a person who has for at least ten years held a judicial office in the territory of India or who has been a member of the Indian Legal Service and has held a post in Grade II of that Service or any equivalent or higher post for at least three years or who has been an advocate for at least ten years.

Explanation—For the purposes of this sub-section,—

(i) in computing the period during which a person has held judicial office in the territory of India, there shall be included any period, after he has held any judicial office, during which the person has been an advocate or has held the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law;

(ii) in computing the period during which a person has been an advocate, there shall be included any period during which the person has held judicial office or the office of a member of a Tribunal or any post, under the Union or a State, requiring special knowledge of law after he became an advocate.

(2A) An accountant member shall be a person who has for at least ten years been in the practice of accountancy as a Chartered Accountant under the Chartered Accountants Act, 1949 (38 of 1949), or as a registered accountant under any law formerly in force or partly as a registered accountant and partly as a Chartered Accountant, or who has been a member of the Indian Income-tax Service, Group A and has held the post of Additional Commissioner of Income-tax or any equivalent or higher post for at least three years.

(3) The Central Government shall appoint :

   (a) a person who is a sitting or retired Judge of a High Court and who has completed not less than seven years of services as a Judge in a High Court; or

(b) The Senior Vice President or one of the Vice President of the Appellate Tribunal

to be the President there of.

(4) The Central Government may appoint one or more members of the Appellate Tribunal to be the Vice President or, as the case may be, Vice Presidents thereof.

(4A) The Central Government may appoint one of the Vice Presidents of the Appellate Tribunal to be the Senior Vice President thereof.

(5) The Senior Vice President or a Vice President shall exercise such of the powers and perform such of the functions of the President as may be delegated to him by the President by a general or special order in writing.

In the absence of any specific provision empowering the Tribunal to hear appeal against fixation of audit fees payable to special auditors appointed under section 142(2A), appeal filed by the assessee against the order under section 142(2D), is not maintainable [Sony Mony Electronics Ltd vs. Dy. CIT (2010) 45 DTR 431 (Mum)(Trib)].

17.3.7 Appeals to the Appellate Tribunal [Section 253]

(1) Any assessee aggrieved by any of the following orders may appeal to the Appellate Tribunal against such order—

(a) an order passed by a Deputy Commissioner (Appeals) before the 1st day of October, 1998 or, as the case may be, a Commissioner (Appeals) under section 154, section 250, section 271, section 271Aor section 272A; or

(b) an order passed by an Assessing Officer under clause (c) of section 158BC, in respect of search initiated under section 132 or books of account, other documents or any assets requisitioned under section 132A, after the 30th day of June, 1995, but before the 1st day of January, 1997; or

(ba) an order passed by an Assessing Officer under sub-section (1) of section 115VZC; or

(c) an order passed by a Principal Commissioner or Commissioner under section 12AA or under clause (vi) of sub-section (5) of section 80G or under section 263 or under section 271 or under section 272A or an order passed by him under section 154 amending his order under section 263 or an order passed by a Principal Chief Commissioner or Chief Commissioner or a Principal Director General or Director General or a Principal Director or Director under section 272A; or

(d) an order passed by an Assessing Officer under sub-section (3), of section 143 or section 147 or section 153A or section 153C in pursuance of the directions of the Dispute Resolution Panel or an order passed under section 154 in respect of such order;

Following clause (e) shall be inserted after clause (d) of sub-section (1) of section 253 by the Finance Act, 2013, w.e.f. 1-4-2016 :

(e) an order passed by an Assessing Officer under sub-section (3) of section 143 or section 147 or section 153A or section 153C with the approval of the Principal Commissioner or Commissioner as referred to in sub-section (12) of section 144BA or an order passed under section 154 or section 155 in respect of such order;

(f) an order passed by the prescribed authority under sub-clause (vi) or sub-clause (via) of clause (23C) of section 10.

(2) The Principal Commissioner or Commissioner may, if he objects to any order passed by a Deputy Commissioner (Appeals) before the 1st day of October, 1998 or, as the case may be, a Commissioner (Appeals) under section 154 or section 250, direct the Assessing Officer to appeal to the Appellate Tribunal against the order.

(2A) The Principal Commissioner or] Commissioner may, if he objects to any direction issued by the Dispute Resolution Panel under sub-section (5) of section 144C in respect of any objection filed on or after the 1st day of July, 2012, by the assessee under sub-section (2) of section 144C in pursuance of which the Assessing Officer has passed an order completing the assessment or reassessment, direct the Assessing Officer to appeal to the Appellate Tribunal against the order.

(3) Every appeal under sub-section (1) or sub-section (2) shall be filed within sixty days of the date on which the order sought to be appealed against is communicated to the assessee or to the Principal Commissioner or Commissioner, as the case may be.

Provided that in respect of any appeal under clause (b) of sub-section (1), this sub-section shall have effect as if for the words "sixty days", the words "thirty days" had been substituted.

(3A) Every appeal under sub-section (2A) shall be filed within sixty days of the date on which the order sought to be appealed against is passed by the Assessing Officer in pursuance of the directions of the Dispute Resolution Panel under sub-section (5) of section 144C.

(4) The Assessing Officer or the assessee, as the case may be, on receipt of notice that an appeal against the order of the Deputy Commissioner (Appeals) or, as the case may be, the Commissioner (Appeals) or the Assessing Officer in pursuance of the directions of the Dispute Resolution Panel has been preferred under sub-section (1) or sub-section (2) or sub-section (2A) by the other party, may, notwithstanding that he may not have appealed against such order or any part thereof; within thirty days of the receipt of the notice, file a memorandum of cross-objections, verified in the prescribed manner, against any part of the order of the Assessing Officer (in pursuance of the directions of the Dispute Resolution Panel) or Deputy Commissioner (Appeals) or, as the case may be, the Commissioner (Appeals), and such memorandum shall be disposed of by the Appellate Tribunal as if it were an appeal presented within the time specified in sub-section (3) or sub-section (3A).

(5) The Appellate Tribunal may admit an appeal or permit the filing of a memorandum of cross-objections after the expiry of the relevant period referred to in sub-section (3) or sub-section (4), if it is satisfied that there was sufficient cause for not presenting it within that period.

(6) An appeal to the Appellate Tribunal shall be in the prescribed form and shall be verified in the prescribed manner and shall, in the case of an appeal made, on or after the 1st day of October, 1998, irrespective of the date of initiation of the assessment proceedings relating thereto, be accompanied by a fee of,—

(a) Where the total income is ≤ ₹1,00,000	Fee ₹ 500
(b) Where the total income is > ₹1,00,000 ≤₹2,00,000	Fee ₹ 1,500
(c) Where the total income is > ₹2,00,000	Fee of 1% of the assessed income (Maximum of ₹ 10,000)
(d) Where the subject matter of an appeal is not covered under (a), (b) and (c) above	Fee ₹ 500
(e) Application for stay of demand	Fee ₹ 500

Provided that no such fee shall be payable in the case of an appeal referred to in sub-section (2) or a memorandum of cross-objections referred to in sub- section (4).

Case Law:

Where Tribunal found that cross-objections were belated by a period of one year and eleven months and Tribunal came to conclusion that no sufficient cause had been made out explaining delay, Tribunal was justified in holding that delay in filing cross-objections could not be condoned - *Vareli Textile Industries* vs. *CIT* 154 Taxman 33.

17.3.8 Orders of Appellate Tribunal [Sec. 254]

(1) The Appellate Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit.

(2) The Appellate Tribunal may, at any time within four years from the date of the order, with a view to rectifying any mistake apparent from the record, amend any order passed by it under sub-section (1), and shall make such amendment if the mistake is brought to its notice by the assessee or the Assessing Officer.

Provided that an amendment which has the effect of enhancing an assessment or reducing a refund or otherwise increasing the liability of the assessee, shall not be made under this sub-section unless the Appellate Tribunal has given notice to the assessee of its intention to do so and has allowed the assessee a reasonable opportunity of being heard.

Provided that any application filed by the assessee in section 254(1) on or after 1.10.1998, shall be accompanied by a fee of ₹ 50.

(2A) In every appeal, the Apellate Tribunal, where it is possible may hear and decide such appeal within a period of 4 years from the end of the financial year in which such appeal is filed u/s 253 (1), (2) or (2A).

Provided that the Appellate Tribunal may, after considering the merits of the application made by the assessee, pass an order of stay in any proceedings relating to an appeal filed under sub-section (1) of section 253, for a period not exceeding one hundred and eighty days from the date of such order and the Appellate Tribunal shall dispose of the appeal within the said period of stay specified in that order.

Provided further that where such appeal is not so disposed of within the said period of stay as specified in the order of stay, the Appellate Tribunal may, on an application made in this behalf by the assessee and on being satisfied that the delay in disposing of the appeal is not attributable to the assessee, extend the period of stay, or pass an order of stay for a further period or periods as it thinks fit; so, however, that the aggregate of the period originally allowed and the period or periods so extended or allowed shall not, in any case, exceed three hundred and sixty-five days and the Appellate Tribunal shall dispose of the appeal within the period or periods of stay so extended or allowed.

Provided also 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, the order of stay shall stand vacated after the expiry of such period or periods.

(2B) The cost of any appeal to the Appellate Tribunal shall be at the discretion of that Tribunal.

(3) The Appellate Tribunal shall send a copy of any orders passed under this section to the assessee and to the Commissioner.

(4) Save as provided in section 256 or section 260A, orders passed by the Appellate Tribunal on appeal shall be final.

Case Laws:

1. Jurisdiction is not higher than that of ITO – The jurisdiction of the Tribunal in the hierarchy created by the Act is no higher than that of the ITO; it is also confined to the year of assessment *ITO* vs. *Murlidhar Bhagwan Das* 52 ITR 335.
2. Tribunal cannot assume powers inconsistent with statutory provisions –CIT vs. Manick Sons 74 ITR
3. Jurisdiction is restricted to subject-matter of appeal- The powers of the Tribunal in dealing with appeals are expressed in section 254(1) in the widest possible terms. The word ‘thereon’ of course restricts the jurisdiction of the Tribunal to the subject-matter of the appeal Hukumchand Mills Ltd. vs. CIT 63 ITR 232.

17.3.9 Procedure of Appellate Tribunal [Sec. 255]

(1) The powers and functions of the Appellate Tribunal may be exercised and discharged by Benches constituted by the President of the Appellate Tribunal from among the members thereof.

(2) Subject to the provisions contained in sub-section (3), a Bench shall consist of one judicial member and one accountant member.

(3) The President or any other member of the Appellate Tribunal authorised in this behalf by the Central Government may, sitting singly, dispose of any case which has been allotted to the Bench of which he is a member and which pertains to an assessee whose total income as computed by the Assessing Officer in the case does ≤ 15,00,000, and the President may, for the disposal of any particular case, constitute a Special Bench consisting of three or more members, one of whom shall necessarily be a judicial member and one an accountant member.

(4) If the members of a Bench differ in opinion on any point, the point shall be decided according to the opinion of the majority, if there is a majority, but if the members are equally divided, they shall state the point or points on which they differ, and the case shall be referred by the President of the Appellate Tribunal for hearing on such point or points by one or more of the other members of the Appellate Tribunal, and such point or points shall be decided according to the opinion of the majority of the members of the Appellate Tribunal who have heard the case, including those who first heard it.

(5) Subject to the provisions of this Act, the Appellate Tribunal shall have power to regulate its own procedure and the procedure of Benches thereof in all matters arising out of the exercise of its powers or of the discharge of its functions, including the places at which the Benches shall hold their sittings.

(6) The Appellate Tribunal shall, for the purpose of discharging its functions, have all the powers which are vested in the Income Tax Authorities referred to in section 131, and any proceeding before the Appellate Tribunal shall be deemed to be a judicial proceeding within the meaning of sections 193 and 228 and for the purpose of section 196 of the Indian Penal Code (45 of 1860), and the Appellate Tribunal shall be deemed to be a civil court for all the purposes of section 195 and Chapter XXXV of the Code of Criminal Procedure, 1898 (5 of 1898).

Case Laws :

1. **Statement to be relied upon must be got recorded:** If the Tribunal desires to rely upon a statement, it should formally call upon counsel for the assessee to record the statement in writing so as to enable the ITO to meet the case - *CIT* vs. *Thayaballi Mulla Jeevaji Kapasi* 66 ITR 147.

2. **Fiscal matters must be disposed of expeditiously :** Law must move quickly not only in the Courts but also before the Tribunals and officers charged with the duty of expeditious administrative justice. Indeed administrative officers and Tribunals are taking much longer time than is necessary, thereby defeating the whole purpose of creating quasi-judicial Tribunals calculated to produce quick decisions especially in fiscal matters ITO vs. Ramnarayan Bhojnagarwala 103 ITR 797.

17.3.10 Statement of case to Supreme Court in certain cases [Section 257]

If, on an application made [against an order made under section 254 before the 1st day of October, 1998,] under section 256 the Appellate Tribunal is of the opinion that, on account of a conflict in the decisions of High Courts in respect of any particular question of law, it is expedient that a reference should be made direct to the Supreme Court, the Appellate Tribunal may draw up a statement of the case and refer it through its President direct to the Supreme Court.

17.3.11 Appeal to the High Court [Section 260A & 260B]

An appeal shall lie to the High Court from every appellate order passed in appeal by the Tribunal, before the date of establishment of the National Tax Tribunal if the High Court is satisfied that the case involves a substantial question of law. The appeal may be filed by the Chief Commissioner or the Commissioner or the assessee. The Memorandum of Appeal shall precisely state the substantial question of law involving the appeal. An appeal along with a fee (as per Court Fees Act), shall be filed within 120 days of the date of receipt of the order appealed against. The question of law shall be formulated by the High Court, then the appeal shall be heard by a bench of at least two judges and decided by majority opinion. [Secs. 260A and 260B]

Case Laws :

1. Even if the High Courts have consistently taken an erroneous view, it would be worthwhile to let the matter rest, since large number of parties have modulated their legal relationship based on this settled position of law *Union of India* vs. *Azadi Bachao Andolan* 132 Taxman 373/263 ITR 706.
2. *Revenue authorities to follow decision of jurisdictional High Court*: Revenue authorities within State cannot refuse to follow jurisdictional High Court's decision on ground that decision of some other High Court was pending disposal by Supreme Court *CIT* vs. G.M. Mittal Stainless Steel (P.) Ltd. 130 Taxman 67/263 ITR 255.

Some of the instances which have been accepted as question of law with the High Court are as under:

A view contrary to the one taken by Supreme Court in a subsequent decision [CIT vs. Kalyan Das Rastogi (1992) 193 ITR 713 (SC)].

Admissibility and relevancy of evidence [Hukamchand Jagadharmal vs. CIT (1935) 3 ITR 211(Lah)].

Amount spent on taking leases of land for brick kilns whether capital or business expenditure [Sardar Saheb Sardar Singar Singh & Son vs. CIT (1942) 10 ITR 441 (Oudh)].

Assessment under section 144 whether made arbitrarily, recklessly or capriciously without the Income-tax Officer exercising his judgment in the matter [Somchand Maluk Chand vs. CIT (1937) 5 ITR 336 (Lah)].

Cash credit and interest whether income [CIT vs. Bhagwandas & Bros. (1992) 108 CTR 401 (All)].

Cash payments in aggregate on a day whether hit by section 40A(3) [Shiv Trading Co. vs. CIT (1989) 176 ITR 410 (All)].

Cash payment under section 40A(3), whether deductible [CIT vs. Sapna Traders (1993) 109 CTR 503 (All)].

Charitable trust, whether the assessee is? [CIT vs. Jewellers Association (1991) 191 ITR 568 (Raj)].

Charity object whether of general public utility [Trustees of the Tribune, In re (1939) 7 ITR 415 (PC)].

Concealment of income whether wilful or not [CIT vs. Ess Ess Kay Engineering Co. Pvt. Ltd (1978) 114 ITR 410 (P&H)].

Concealment whether assessee liable to penalty [CIT vs. Abdul Majeed (T.) (1992) 193 ITR 339 (Ker)].

Concealing particulars of his income failure to substantiate claim for deductions whether amounts to concealment? [Jankilal Jaju vs. CIT (1981) 127 ITR 805 (MP)].

Whether there was any material for conclusion of the Tribunal that there was concealment? [Laddha Traders vs. CIT (1996) 222 ITR 754 (MP)].

Concealment under section 271(1)(c) based on its earlier findings in the quantum appeals, without examining further whether the assessee was guilty of concealment or furnishing wrong particulars [Rajasthan Textile Industries vs. CIT (1992) 196 ITR 598 (Raj)].

Clubbing of receipts for and on behalf of other [CIT vs. George Thomas (Dr K.) (1993) 199 ITR 110 (Ker)].

Competency of an appeal before the Appellate Tribunal [Mulla Irshad Ali vs. CIT (1958) 33 ITR 454 (MP)].

Decision of Supreme Court whether applicable to the facts [CIT vs. Maharani Sethu Parvathi Bayi (H.H.) (1993) 199 ITR 625 (Ker)].

Whether the assessee is entitled to depreciation? [G.N.A. Enterprises Pvt. Ltd vs. CIT (1996) 133 Taxation 569 (P&H)].

Whether eligible under section 80HH? [CIT vs. Poyilakada Fisheries Pvt. Ltd (1996) 221 ITR 692 (Ker)].

Whether capital expense or revenue? [CIT vs. Nagmmal Mills Ltd (1996) 217 ITR 309 (Mad)].

Head of income [CIT vs. Carvanserai Ltd (1991) 192 ITR 694 (Del)].

Whether the interest paid on borrowed capital was allowable when the income was assessed by application at a net profit rate [Naraindas Goyal Contractor vs. CIT (1982) 134 ITR 96 (MP)].

Jurisdiction under section 154 to rectify the assessment [CIT vs. Usha Devi (1983) 13 Taxman 463 (MP)].

Limitation period for reassessment or assessment [Krishna Gopal Bhadra vs. ITO (1980) 124 ITR 580 (Cal)].

Profit from land sale, whether business income or capital gains? [Bari Doab Bank Ltd vs. CIT (1989) 177 ITR 454 (P&H)].

Whether the Assessing Officer had jurisdiction under section 154 to rectify the assessment order? [CIT vs. Usha Devi (1983) Tax LR 476 (MP)].

Rectification of original order by Appellate Tribunal so as to increase the cost of certain machinery in exercise of its power under section 254 whether competent? [CIT vs. Bombay Dyeing and Manufacturing Co. Ltd (1971) 82 ITR 892 (SC)].

Salary paid by the company whether any part attributable to extra commercial considerations and liable to be disallowed? [Gwalior Rayon Silk Mfg. (Wvg.) Co. Ltd vs. CIT (1982) 134 ITR 97 (MP)].

Status of an association of persons whether proper? [CIT vs. Sarika Saree House (1991) 191 ITR 517 (All)].

Status whether that of HUF? [CIT vs. Jitendra Kumar Vidya Devi (1990) 184 ITR 247 (All)].

Transactions of sale and purchase of shares whether trading or in the nature of investment? [Holck Larsen (H.) vs. CIT (1972) 85 ITR 285 (Bom)].

Transfer whether under section 2(47)? [CIT vs. Chandra Mohan Swahney (1988) 67 CTR 13 (Del)].

Year in which credit has to be given for TDS [CIT vs. Carvanserai Ltd (1991) 192 ITR 684 (Del)].

Whether the goodwill was computed in accordance with law [S.C. Cambatta & Co, Pvt. Ltd vs. Commissioner of Excess Profits Tax (1961) 41 ITR 500 (SC)].

Whether the Method of Accounting adopted by the Assessing Officer was a legal method? [Narayan Atmaram Patkar vs. CIT (1934) 2 ITR 486 (Bom)].

Adventure in the nature of trade whether the Tribunal was right in holding that the transaction amounted to an adventure in the nature of trade? [CIT vs. Kamla Devi Khazanchi & Ors (1986) 157 ITR 367 (Raj)].

Question as to whether assessee is liable to deduct tax at source under section 194C is a substantial question of law [CIT vs. Ambuja Darla Karssog Transport Co-operative Society Ltd (2008) 168 Taxman 223 (SC). Also See CIT vs. Sirmour Truck Operators Union (2008) 170 Taxman 242 (SC)].

Some of the instances which have not been accepted as question of law by the High Court are as under:

Where Tribunal recalled its appellate order having found as a fact that its decision was based on wrong assumption that a particular document was not filed [CIT vs. Dongre (M.R.) (1993) 113 CTR 351 (Del)].

A question already referred at the instance of one party against decision in opposite party's appeal, need not be referred again [CIT vs. J.K. Synthetics Ltd (1992) 14 CTR (Del) 193].

Question directly covered by decision of jurisdictional High Court need not be referred notwithstanding pendency of Special Leave Petition [CIT vs. Khosla (S.S.) (1997) 136 Taxation 466 (P&H)].

A question of law the answer to which is self-evident [CIT vs. India Mica Supply Co. Pvt. Ltd (1970) 77 ITR 20 (SC)].

A question of law which is academic [CIT vs. Jardine Henderson Ltd (1979) 117 ITR 568 (SC)].

No useful purpose can be served in referring a question where the Tribunal decided the issue in absence of any material in the possession of the Department [CIT vs. Anand Iron & Steel Industries (1989) 179 ITR 620 (Del)].

Where the matter is remanded to the authorities below for fresh examination, no question arising out of such remand order is to be referred [Subeer Singh Tamra vs. CIT (1987) 165 ITR 95 (Raj)].

A question raised which is only explanatory or is argumentative and in effect is an aspect of another question already, need not be referred [CWT vs. Suresh Kumar Kaushik (1991) 187 ITR 343 (All)].

17.3.12 Appeal to the Supreme Court [Section 261]

An appeal lies before the Supreme Court, against an order of the High Court in a reference, or in an appeal. Such appeal can be filed only if the High Court certifies it to be a fit case for appeal to the Supreme Court. If the High Court refuses to grant such a certificate, the assessee can file a Special Leave Petition (SLP)before the Supreme Court. If the SLP is granted, the Supreme Court will hear and decide the appeal on merits. [Sec. 261]

Case Laws :

1. Certificate will not issue against judgment of single Judge: Under article 133(3) of the Constitution, no appeal shall lie to the Supreme Court from the judgment, decree or final order of one Judge of the High Court. Consequently, no certificate can be issued in respect of such a judgment, decree or order State Bank of India vs. State Bank of India Employees' Union 169 ITR 675 .
2. Question must be of great public or private importance A certificate under section 261 which does not set out precisely the grounds or does not raise a question of great public or private importance does not comply with the requirements of the Act. The jurisdiction of the Supreme Court to entertain an appeal from the opinion recorded under the Act arises only when a certificate is properly issued by the High Court or when the Supreme Court grants special leave under article 136 of the Constitution. India Machinery Stores (P.) Ltd. vs. CIT 78 ITR 50 ; CIT vs. Central India Industries Ltd. 82 ITR 555.

17.3.13 Hearing before Supreme Court [Section 262]

(1) The provisions of the Code of Civil Procedure, 1908 (5 of 1908), relating to appeals to the Supreme Court shall, so far as may be, apply in the case of appeals under section 261 as they apply in the case of appeals from decrees of a High Court :

    Provided that nothing in this section shall be deemed to affect the provisions of sub-section (1) of section 260 or section 265.

(2) The costs of the appeal shall be in the discretion of the Supreme Court.

(3) Where the judgment of the High Court is varied or reversed in the appeal, effect shall be given to the order of the Supreme Court in the manner provided in section 260 in the case of a judgment of the High Court.

Case Law :

Question not raised earlier cannot be raised: An independent issue, not considered by Tribunal or High Court, could not be permitted to be raised for first time before Supreme Court RM. Arunachalam vs. *CIT* 93 Taxman 423/227 ITR 222.

17.4 REVISION

Provisions relating to powers of revision of the Commissioner of Income Tax provides in sections 263 and 264 of the Income-tax Act which are analysed in a tubular form as under :

Section 263	**Section 264**
I. Scope:	
(a) Revision of order erroneous and prejudicial to the interest of revenue passed by the Assessing Officer	Revision of other orders by any sub- ordinate authority.
(b) Two circumstances must exist to enable the Commissioner to exercise the power of revision viz. (i) the order should be erroneous; and (ii) by virtue of the order being erroneous prejudice must have been caused to the interest and of the Revenue. CIT vs. Gabriel India Ltd., 203 ITR 108(Bom).	The Commissioner shall not revise any order where the appeal against the order is pending before the first or second appellate authorities (or) where the time for filing appeal has not lapsed the assessee has not waived his right of appeal.
II. Procedure :	
(a) Commissioner of Income Tax may call for and examine the records and revise the orders after hearing the assessee.	Commissioner of Income-tax either on his own motion or on an application by the assessee can call for the records and revise the order.
(b) Record shall include all records relating to any proceeding available at the time of examination of the file by the Commissioner of Income-tax.	Every application for revision should be accompanied by a fee ₹ 500.
III. Nature of order :	
(a) An order enhancing, modifying or cancelling the assessment can be passed by the Commissioner.	An order which is not prejudicial to the interest of the assessee can be passed.
(b) If the Income-tax Officer makes any mistake in carrying out the directions of the Appellate Assistant Commissioner or the Tribunal, his order can be revised by the Commissioner of Income Tax. Warner Lambert Co.vs. CIT, 205 ITR 395(Bom).	Commissioner declining to interfere will not amount to passing of an order prejudicial to the assessee.
(c) The Commissioner of Income Tax has jurisdiction and powers to initiate proceedings in respect of issues not touched by the CIT(Appeals) in his Appellate Order- CIT vs. Jayakumar B. Patil, 236 ITR 469(SC).	Where depreciation was not claimed before the Income-tax Officer or the Appellate Assistant Commissioner but was claimed for the first time before the Commissioner of Income Tax in an application u/s 264, the Commissioner must allow the claim on merits. Rashtriya Vikas Ltd. vs. CIT,196 ITR694(All.)
IV. Time limit :	
(a) No order can be passed after the expiry of 2 years from the end of the Financial Year in which the order to be revised was passed.	Commissioner should pass an order disposing of the revision petition within one year from the end of the Financial Year in which the revision petition was filed by the assessee.

(b) An order in revision may be passed at any time in the case of an order which has been passed in consequence of or to give effect to any finding or direction contained in an order of the Appellate Tribunal, the High Court or the supreme court.	On assessee's application- within one year from the end of financial year in which the application was filed.
V. Remedy : Appeal can be filed to the Appellate Tribunal.	There is no right of appeal but appeal vests under constitution.

Case Law :

In view of the vastness of the powers of the Commissioner under section 263, the Courts have often come to the rescue of the tax payer, against indiscriminate exercise of the powers as the following decisions will show:

(1) The Commissioner did not come to a positive finding that the claim of the assessee was erroneous. He simply asked the Assessing Officer to re-examine the matter. This was not possible [CIT vs. Gabriel India Ltd (1993) 203 ITR 108 (Bom)].

(2) The Commissioner of Income-tax noted that the assessee was holding large chunk of shares in different companies. The Commissioner of Income-tax remanded the case to the Assessing Officer for making enquiries. The Tribunal observed that the Commissioner of Income-tax did not indicate even one instance of any shareholding being bogus. The Tribunal cancelled the order under section 263 [Mayur Finance Ltd (1994) 122 Taxation 539 (All)].

(3) The revisionary jurisdiction cannot be allowed to be exercised by the Commissioner either for substituting his own opinion for that of the Assessing Officer or for making a fishing or roving enquiry [Jhulelal Land Development Corpn. vs. DCIT (1996) 56 ITD 345 (Bom)].

(4) The orders of subordinate authorities should not be cancelled or set aside on mere whims and fancies [Ichhopani (N.S.) vs. CIT (Asst.) (1995) 55 ITD 88 (Chd)(AT)].

(5) There is no bar on the Assessing Officer bringing the relevant material to the notice of the Commissioner. The only requirement of the section is that upon being informed by the Assessing Officer about the infirmities in the order, the Commissioner cannot straightaway invoke the revisional powers and issue a show-cause notice. If he initiates proceedings without applying his mind and without considering all the facts and circumstances of the case, his order cannot be upheld [CIT vs. Bhagat Shyam & Co. (1991) 188 ITR 608 (All); Sumitra Devi Khirwal vs. CIT (1912) 84 ITR 26 (Cal)].

(6) Exercise of revisional jurisdiction by the Commissioner solely on the ground that earlier orders of the Tribunal in favour of the assessee were pending reference, was not valid [CIT vs. Orissa State Financial Corp. (1993) 203 ITR 747 (Ori)].

Where it was found that the Assessing Officer had raised specific queries in regard to all relevant points involved in the assessment and the assessee had met those queries with supporting evidence, but where the Assessing Officer made a brief assessment without recording therein all facts, and accepted assessee's version, the assessment order could not be set aside on the ground that no proper enquiry was made [Krishnamurthy (V.G.) vs. CIT (1985) 152 ITR 683 (Karn)].

(7) Where the assessment is made in undue haste, and without enquiry, it will be erroneous and prejudicial to the interests of revenue [Ram Pyari Devi Saraogi vs. CIT (1968) 67 ITR 84 (SC)].

(8) When the Assessing Officer has passed an order on the basis of law laid down by the High Court, the order cannot be erroneous [Garden Silk Mills Ltd vs. CIT & Anr (1996) 221 ITR 861 (Guj)].

(9) Where the Assessing Officer follows the decision of the Tribunal, it cannot be said that his decision is erroneous [Agarwal (K.N.) vs. CIT (1991) 189 ITR 769 (All)].

(10) Similarly, while making assessment, if the Assessing Officer had made reasonable and requisite enquiries on issues raised by the Commissioner during proceedings under section 263, no order under section 263 could be passed [Jagjit Industries Ltd vs. CIT (Asst.) (1997) 60 ITD 295 (Del)].

(11) In response to the show cause notice, the assessee can rely upon any ground, whether taken at the time of assessment or not, to establish that the order is not prejudicial to the interest of revenue. The Commissioner must examine the ground taken by the assessee. The Commissioner cannot direct the Assessing Officer to take into consideration such objections before making a fresh assessment. He must himself decide the merit of the assessee's objection [J.P. Srivastava & Sons (Kanpur) Ltd vs. CIT (1978) 111 ITR 326 (All)].

(12) Where the Income-tax Officer computed capital gains by taking correct cost of acquisition and not fair market value of asset as on 1st January, 1964 (now 1-4-1981), for which the assessee had not opted, his order is not erroneous or prejudicial to the interest of the revenue. The option for substitution lies with the assessee and the Income-tax Authorities cannot have powers to exercise the option [CIT vs. Duncan Brothers & Co. Ltd (1994) 209ITR 44 (Cal)].

(13) Where an assessment order is passed, keeping in view not only the provisions of the Act, but also Boards Circulars and instructions, the order cannot be erroneous [CIT vs. Tukaram Ramchandra Shinde (1994) 121 Taxation 251 (Bom)].

(14) Where the basic issues were fully covered by the Supreme Court judgment, and where the said judgments were cited by the assessee before the Commissioner, the order of the Commissioner without considering the judgments had to be quashed [CIT vs. Paul Brothers (1995) 216 ITR 548 (Bom)].

(15) However, an assessment order can be revised by the Commissioner, if it is found to be contrary to a Supreme Court judgment, even if it were made as per Board's instructions [CIT vs. United Commercial Bank (1993) 201 ITR 162 (Cal)].

(16) It was held that as the Department had examined the fundamental nature of the transaction in the earlier years and its nature remained unchanged, the Department could not have changed its view as regards the nature of the transaction by dubbing it as erroneous. The Department is not entitled to re-open an assessment based on a fresh inference of transactions accepted by the revenue for several preceding years on the pretext of dubbing them as erroneous [Associated Food Products 280 ITR 377 (MP), Sirpur Paper Mills Ltd 114 ITR 404 (AP) & CIT vs. Gopal Purohit 228 CTR 582 (Bom) followed by CIT vs. Escorts Ltd (Delhi High Court)].

(17) AO having not made any enquiry in relation to late payment of employee's contribution towards ESI and PF, by assessee, CIT was justified in invoking the provisions of 263 and setting aside the order of the AO for redoing the same [Star Drugs & Research Labs Ltd. vs. Asstt. CIT(2010) 42 DTR 343 (Chennai)(TM)(Trib)].

Cases where Commissioner's action under section 263 was upheld:

(1) Where income has not been earned and is not assessable, but is assessed in his or her hands simply because the assessee wants it to be so assessed in order to assist someone else who would have been assessed on a larger income, the assessment is erroneous and prejudicial to the interests of the revenue [Tara Devi Aggarwal vs. CIT(1973) 88 ITR 323 (SC)].

(2) Audit report as required for claiming deduction was not filed along with the return or thereafter till the assessment was made. There was nothing to show that accounts were audited. The Income-tax Officer was wrong in allowing deduction. Commissioners action under section 263 is justified [CIT vs. Shivanand Electronics (1994) 209 ITR 63 (Bom)].

(3) Assessment made without considering valuation report for which a reference had already been made to the Valuation Officer in the course of assessment was erroneous and prejudicial to the interests of the revenue [CIT vs. S.M. Oil Extraction Pvt. Ltd (1991) 190 ITR 404 (Cal)].

(4) The assessee claimed and was allowed a deduction under section 35CCA of the donations to an approved institution. It was established that the approval was withdrawn before the date of the assessment. The Commissioner was justified in canceling the assessment [CIT vs. Bankam Investment Ltd. (1994) 208 ITR 208 (Cal)].

(5) Where the Assessing Officer followed the orders of the First Appellate Authority and where the said appellate order had been challenged at the instance of the revenue, the order passed by the Assessing Officer was erroneous [KEC International Ltd. vs. Dy. CIT (1994) 51 ITD 178 (Bom)(AT)].

(6) Where the point at issue is debatable, the Commissioner of Income-tax is justified in canceling the order passed under section 154 [Madhu Jayanti Pvt. Ltd. vs. CIT (1995) 125 Taxation 362 (Cal)].

(7) Where the Assessing Officer omitted to take into account the benefit or perquisites arising to the assessee as a result of provision of free boarding and lodging, the action of Commissioner under section 263 is justified, even though ultimately no amount was added on merits [Hyundai Heavy Industries Co. Ltd. vs. ITO (1995) 52 TTJ 42 (Del) (AT)].

(8) Simply because the facts have been disclosed by the assessee, it does not give immunity from revisional jurisdiction of the Commissioner [CIT vs. Emery Stone Mfg. Co. (1995) 213 ITR 843 (Raj)].

(9) Where the Commissioner after scrutiny found that the assessee paid higher rate of interest on its borrowings, while it charged interest as a lesser rate on advances made to a firm, action of the Commissioner in setting aside the order is justified [Duggal & Co. vs. CIT (1996) 220 ITR 456 (Del)].

(10) Where the Assessing Officer failed to consider unexplained investment, the Commissioner was justified in setting aside the assessee [Kanhaiyalal vs. CIT(1982) 136 ITR 243 (Raj)].

(11) To facilitate assessments of assessees having small income and small capital, under a scheme the Department completed spot assessments without any enquiry. The Patna High Court had held that where such assessment was made without inquiring into the source of initial capital, the setting aside was competent [CIT vs. Happy Medical Stores (1990) 185 ITR 413 (Pat)].

(12) Where the assessment was set aside with the direction that relief under section 8OL should be given after setting off the business loss against income from other sources, the revisional order was held proper [Warner Lambert Co. vs. CIT (1994) 205 ITR 395 (Bom)].

(13) Where a stereotype order is passed, which simply accepts what the assessee has said in the return and fails to make enquiries which are called for in the circumstances of the case, the Commissioner is justified in holding that the order is erroneous and prejudicial to the interests of the revenue [Tara Devi Aggarwal vs. CIT (1973) 88 ITR 323 (SC)].

(14) Where the assessee did not file an appeal to the Tribunal against the revisional orders under section 263 passed by the Commissioner, he cannot challenge the order of the Assessing Officer giving effect to the order of the Commissioner [Hardillia Chemicals Ltd. vs. CIT (1996) 221 ITR 194 (Bom)].

Following are the cases related to section 264:

(1) The Court, in the case of Pravin V. Ashar vs. Jaidev, CIT (2001) 247 ITR 828 (Guj), held that in determining and deciding the revision u/s 264, the Commission must afford an opportunity of hearing and also consider the merits of the assessee's claim as per the revision application and in the absence of the same one could not go to the root of the matter.

(2) Where inspite of the notices given by the Commissioner, the petitioner i.e. the assessee defaulted in appearance, it was held that apart from the non-appearance of default on the part of the assessee it was and still is the duty of the Revisional Authority to exercise his power u/s 264 to examine the legality and validity of the impugned order, particularly when the assessee comes with a grievance of violation of the natural justice [City Express Super Market vs. CIT (2001) 248 ITR 728 (Cal)].

(3) While passing order u/s 264, it is open to Commissioner to entertain even a new ground or claim or plea not urged before the lower authority [Parekh Bros. vs. CIT (1984) 150 ITR 105 (Ker)]. SLP filed by the Department was dismissed by Supreme Court.

(4) Where the assessee failed to claim exemption u/s 54F due to mistake of her counsel and made application within the prescribed time u/s 264 to the CIT for revision, it was held that the Commissioner should give the benefit by revising the order [Smt. Snehlata Jain vs. CIT (2004) 140 Taxman 156 (J&K)].

(5) Where after passing of the assessment order, the assessee found that mistake she had not claimed a deduction which she was entitled to in respect of the investment. Therefore, she made an application u/s 264 to the CIT along with the evidence showing investment for exemption. The Commissioner rejected the revision application holding that from the perusal of the assessment records and the report of the Assessing Officer, it appears that despite opportunity being given, the assessee failed to produce evidence regarding investment made by the petitioner. It was held that there is nothing in section 264 which places any restriction on the CIT's revisional power to give relief to the assessee in a case where the assessee detects mistakes, on account of which he was over assessed after the assessment was completed. It is open to the CIT to entertain even a new ground not urged before the lower authorities while exercising revisional powers [Phool Lata Somani vs. CIT (2005) 197 CTR 339 (Cal)].

(6) The return of income filed on 31.07.2002, the assessee did not claim exemption u/s 10(10C) by mistake. Revised return filed on 24.09.2002 claiming exemption u/s 10(10C) was held to be invalid. The assessee preferred a revision application to the Commissioner u/s 264 for granting exemption. The Commissioner rejected the application by holding that the petition was beyond the period of limitation. It was held that regardless of whether the revised return was filed or not, once, an assessee is in a position to show that the assessee has been over-assessed under the provisions of the Act, regardless of whether the over-assessment is a result of assessee's own mistake or otherwise, the Commissioner has the power to correct such an assessment u/s 264(1). If the Commissioner refuses to give relief to the assessee, in such circumstances, he would be acting de hors the power under the Act and the provisions of the Act and, therefore, is duty bound to give relief to an assessee, where due, in accordance with the provisions of the Act [S.R. Koshi vs. CIT (2005) 276 ITR 165 (Guj)].

(7) Where an application u/s 197 relating to obtaining a certificate from Assessing Officer for no deduction or deduction of tax at lower rate is rejected by the Assessing Officer, it can be revised by the Commissioner u/s 264 [Larsen & Toubro Ltd. vs. CIT (2010) 190 Taxman 373 (Bom)].

(8) The provision dealing with the Appellate Authorities do not bar an appellate from invoking Appellate Jurisdiction, if he has invoked revisionary jurisdiction, even though for invoking revisionary jurisdiction it is a precondition that the Appellate Jurisdiction should have been invoked. Thus, there is nothing in the law that prevents an assessee to move Appellate Jurisdiction u/s 246A if the effort made u/s 264 is proved unsuccessful. It was held that the Commissioner (Appeals) would be justified in entertaining an appeal against the assessment by condoning the delay even though the Commissioner has passed an order u/s 264 against the assessee. The present law provides more than one remedy to the assessee and the assessee can certainly invoke all of them [CIT vs. D. Lakshminarayanpathi (2001) 250 ITR 187 (Mad)].

For the purposes of this section, an order passed by the Assessing Officer shall be deemed to be erroneous in so far as it is prejudicial to the interests of the revenue, if, in the opinion of the Principal Commissioner or Commissioner,—

(a) the order is passed without making inquiries or verification which should have been made;

(b) the order is passed allowing any relief without inquiring into the claim;

(c) the order has not been made in accordance with any order, direction or instruction issued by the Board under section 119; or

(d) the order has not been passed in accordance with any decision which is prejudicial to the assessee, rendered by the jurisdictional High Court or Supreme Court in the case of the assessee or any other person.

17.5 GENERAL PROVISIONS

17.5.1 Tax to be paid notwithstanding reference, etc. [Section 265]

Notwithstanding that a reference has been made to the High Court or the Supreme Court or an appeal has been preferred to the Supreme Court, tax shall be payable in accordance with the assessment made in the case.

17.5.2 Execution for costs awarded by Supreme Court [Section 266]

The High Court may, on petition made for the execution of the order of the Supreme Court in respect of any costs awarded thereby, transmit the order for execution to any court subordinate to the High Court.

17.5.3 Amendment of assessment on appeal [Section 267]

Where as a result of an appeal under section 246 or section 246A or section 253, any change is made in the assessment of a body of individuals or an association of persons or a new assessment of a body of individuals or an association of persons is ordered to be made, the Commissioner (Appeals) or the Appellate Tribunal, as the case may be, shall pass an order authorising the Assessing Officer either to amend the assessment made on any member of the body or association or make a fresh assessment on any member of the body or association.

17.5.4 Exclusion of time taken for copy [Section 268]

In computing the period of limitation prescribed for an appeal or an application under this Act, the day on which the order complained of was served and, if the assessee was not furnished with a copy of the order when the notice of the order was served upon him, the time requisite for obtaining a copy of such order, shall be excluded.

17.5.5 Filing of appeal or application for reference by Income Tax Authority [Section 268A]

(1) The Board may, from time to time, issue orders, instructions or directions to other Income-tax Authorities, fixing such monetary limits as it may deem fit, for the purpose of regulating filing of appeal or application for reference by any Income-tax Authority under the provisions of this Chapter.

(2) Where, in pursuance of the orders, instructions or directions issued under sub-section (1), an Income-tax Authority has not filed any appeal or application for reference on any issue in the case of an assessee for any Assessment Year, it shall not preclude such authority from filing an appeal or application for reference on the same issue in the case of-

    (a) The same assessee for any other Assessment Year; or

    (b) any other assessee for the same or any other Assessment Year.

(3) Notwithstanding that no appeal or application for reference has been filed by an income-tax authority pursuant to the orders or instructions or directions issued under sub-section (1), it shall not be lawful for an assessee, being a party in any appeal or reference, to contend that the income-tax authority has acquiesced in the decision on the disputed issue by not filing an appeal or application for reference in any case.

(4) The Appellate Tribunal or Court, hearing such appeal or reference, shall have regard to the orders, instructions or directions issued under sub-section (1) and the circumstances under which such appeal or application for reference was filed or not filed in respect of any case.

(5) Every order, instruction or direction which has been issued by the Board fixing monetary limits for filing an appeal or application for reference shall be deemed to have been issued under sub-section (1) and the provisions of sub-sections (2)(3) and (4) shall apply accordingly.

Study Note - 18

PENALTY & PROSECUTION

This Study Note includes

18.1 Penalties and Prosecution for defaults

18.1 PENALTIES AND PROSECUTION FOR DEFAULTS

Section	Nature of Default	Minimum Penalty	Maximum Penalty
158BFA	Undisclosed income determined by the Assessing Officer u/s 158BC(c)	100% of the tax on undisclosed income	300% of the tax on undisclosed income
221(1)	Default in making a payment of tax within prescribed time	Such amount as the Assessing Officer may impose	Amount of Tax in arrears
271(1)(b)	Failure to comply with a notice u/s 142(1) or 143(2) or with a direction issued u/s 142(2A).	₹ 10,000 for each failure	₹ 10,000 for each failure.
271(1)(c)	Concealment of the particulars of income or furnishing inaccurate particulars of income.	100% of Tax sought to be evaded.	300% of Tax sought to be evaded.
271A	Failure to keep or maintain books of A/c, document as required u/s 44AA.	₹ 25,000	₹ 25,000
271AA	Failure to keep and maintain information and document in respect of international transaction, (specified domestic transaction) or failure to report international transaction or furnishing of incorrect information.	A sum equal to two per cent of the value of each international transaction entered into by such person.	A sum equal to two per cent of the value of each international transaction entered into by such person.
271AAA	Penalty where search has been initiated — Undisclosed income	A sum computed at the rate of 10% of the undisclosed income of the specified Previous Year.	A sum computed at the rate of 10% of the undisclosed income of the specified Previous Year.
271AAB	Undisclosed income in the case of search (applicable if search is initiated on or after July 1, 2012)	Admit the undisclosed income — 10% of undisclosed income No admit the undisclosed income — 20% of undisclosed income	Admit the undisclosed income — 10% of undisclosed income No admit the undisclosed income — 20% of undisclosed income
271B	Failure to get accounts audited u/s 44AB or to furnish such report along with return of income by due date	1/2% of Total Sales, Turnover or Gross receipts.	₹ 1,50,000
271BA	Failure to submit report u/s 92E	₹ 1,00,000	₹ 1,00,000

Section	Nature of Default	Minimum Penalty	Maximum Penalty
271C	Failure to deduct the whole or any part of tax u/s 192 to 195 or (w.e.f. 1.6.97) failure to pay the whole or any part of tax u/s 115 O(2) or 2nd proviso to Sec. 194B.	Amount of Tax required to be deducted at source.	Amount of Tax required to be deducted at source.
271CA	Penalty for failure to collect tax at source	A sum equal to the amount of tax failed to collect	A sum equal to the amount of tax failed to collect
271D	Taking or accepting any loan or deposit specified sum in contravention of the provisions of Section 269SS	Amount of Loan/ Deposit specified sum so taken or accepted	Amount of Loan/ Deposit specified sum so taken or accepted
271E	Repaying any deposit or loan specified sum otherwise than in accordance with the provisions of Sec. 269 T	Amount of loan or deposit specified sum so repaid.	Amount of loan or deposit specified sum so repaid.
271F	(i) Failure to furnish return of income u/s.139(1) before the end of the relevant Assessment Year (w.e.f. 1.4.99) (ii) Failure to furnish return of income as per proviso to Sec.139(1) by the end of relevant Assessment Year.	₹ 5000 ₹ 5000	₹ 5000 ₹ 5000
271FA	Failure to furnish statement of financial transaction or reportable account return within the prescribed time under section 285BA(1)	₹ 100 for every day during the failure continue ₹ 500 for everyday during which the failure continues (if notice is issued)	₹ 100 for every day during the failure continue ₹ 500 for everyday during which the failure continues (if notice is issued)
271FAA	Person referred to in section 285BA(1)(k) provides inaccurate information in the statement	₹50,000	₹50,000
271FAB	failure to furnish statement or information or document by an eligible investment fund	₹5,00,000	₹5,00,000
271FB	Penalty for failure to furnish return of fringe benefits [Fringe Benefit Tax is not applicable from A.Y. 2010-11 onwards]	a sum of one hundred rupees for every day during which the failure continues.	a sum of one hundred rupees for every day during which the failure continues.
271G	Failure to furnish information or documents under section 92D(3) to AO or the TPO as referred to in section 92CA	2% of value of the international transaction (specified domestic transaction) for each failure	₹ 10,000 for each default
271GA	failure to furnish information or document under section 285A	**Indian concern** – 2% of the value of the transaction **Other Case** - ₹5,00,000	**Indian concern** – 2% of the value of the transaction **Other Case** - ₹5,00,000
271H	Failure to submit in quarterly TDS/ TCS returns	₹ 10,000	₹ 1,00,000
271-I	failure to furnish information or furnishing inaccurate information under section 195	₹1,00,000	₹1,00,000

Section	Nature of Default	Minimum Penalty	Maximum Penalty
272A(1)(a)	Refuses to answer any question put to a person regarding his assessment by an I.T. Authority.	₹ 10,000 for each default	₹ 10,000 for each default
272A(1)(b)	Refuses to sign any statement made by a person in course of I.T. Proceeding.	₹ 10,000 for each default	₹ 10,000 for each default
272A(1)	Failure to comply with summons issued u/s 131(1)	₹ 10,000 for each default	₹ 10,000 for each default
272A(2)	Failure to comply with a notice u/s 94, 176(3), 133, 206, 206C, 285B, 134 to furnish return of Income u/s 139(4A) or 139(4C) or to delivery in due time a declaration mentioned in section 197A or 206C(1A), to furnished certificate u/s 203 or 206C	₹ 100 for every day during the failure continues but restricted to amount of tax.	₹ 100 for every day during the failure continues but restricted to amount of tax.
272AA	Failure to comply with provisions of Sec. 133B.	Any amount upto ₹ 1,000	₹ 1,000
272B	Failure to comply with the provisions of section 139A or for quoting or intimating a PAN which is false. [w.e.f. 1.6.2002]	₹ 10,000	₹ 10,000
272BB(1)	Failure to comply with the provisions of of Sec. 203A	Up to ₹ 10,000	₹ 10,000
272BB	Failure to comply with the provisions of section 203A (i.e. failure to obtain TAN or after obtaining failure to quote TAN in all challans, certificates and returns etc.)	₹ 10,000	₹ 10,000
272BBB	Failure to comply before 1.10.2004 with the provisions of section 206CA relating to obtaining & quoting TCAN.	₹ 10,000	₹ 10,000

As per section 275, the time limits in various situations for imposing penalty are as under:

			Situation	**Time Limit for passing the penalty order**
1.			Where penalty is to be levied for concealment or furnishing inaccurate particulars of income under section 271(1)(c)	
	(A)		Where the penalty is to be levied by the Assessing Officer in an assessment made by him	
		(i)(a)	Where an appeal has been filed against the assessment order to Commissioner (Appeal) [Section 275(1)(a) and its proviso]	Penalty order can be passed by the Assessing Officer— (i) on or before the expiry of the financial year in which assessment proceedings are completed, Or (ii) on or before the expiry of one year from the end the month in which the order of Commissioner (Appeal) is received by the Chief Commissioner or Commissioner of Income Tax whichever period expires later.

		(i)(b)	In a case, where further appeal has been filed to Appellant Tribunal [Section 275(1)(a)]. [Rayala Corpn. Pvt. Ltd vs. Union of India (2007) 161 Taxman 127 (Mad)]	Penalty order can be passed by the Assessing Officer— (i) on or before the expiry of the financial year in which assessment proceedings are completed, Or (ii) on or before the expiry of six months from the end of the month in which the order of Appellant Tribunal is received by the Chief Commissioner or Commissioner of Income Tax whichever period expires later.
		(ii)	Where revision application is filed against such assessment to Commissioner under section 264	Six months from the end of the month in which order is passed by the Commissioner under section 264
		(iii)	Where no appeal has been filed against the assessment order or no application is made for revision under section 264	Penalty order can be passed by the Assessing Officer— (i) on or before expiry of the financial year in which the assessment proceedings are completed Or (ii) on or before the expiry of 6 months from the end of the month in which the action for imposition of penalty is initiated whichever period expires later
	(B)		Where the penalty is to be levied by the Commissioner (Appeal) in an order passed by him under section 250	
		(i)	Where an appeal has been filed to ITAT against such order	Penalty order can be passed by the Commissioner (Appeal)— (i) on or before the expiry of the financial year in which order under section 250 is passed Or (ii) on or before the expiry of 6 months from the end of the month in which order of ITAT is received by the Commissioner of Income tax whichever period expires later
		(ii)	Where no appeal has been filed against such order to ITAT	Penalty order can be passed— (i) On or before the expiry of the financial year in which order under section 250 was passed Or (ii) On or before 6 months from the expiry of the month in the which the penalty proceedings were initiated by Commissioner (Appeal) whichever period expires later
	(C)		Where the relevant assessment order is the subject matter of revision under section 263 (i.e. income is enhanced)	

		(i)	Where an appeal against order under section 263 is filed to ITAT	Penalty order can be passed by the Commissioner — (i) on or before the expiry of the financial year in which order under section 263 was passed by the Commissioner Or (i) on or before the expiry of six months from the end of the month in which order of ITAT is received by the Commissioner whichever period expires later
		(ii)	Where no appeal is filed against order under section 263	Penalty order can be passed by the Commissioner on or before six months from the end of the month in which order under section 263 is passed
2.			Where penalty is to be levied for any default other than concealment of income	
		(i)	Where penalty is levied during the course of assessment proceedings	Time limit for passing the penalty order is same as given under point No. 1(A)(ia), (ib), (ii) and (iii) above
		(ii)	Where penalty is levied after completion of assessment or no assessment is to be made	Penalty order can be passed — (i) on or before expiry of the financial year in which the penalty proceedings were initiated Or (ii) within 6 months from the end of the month in which penalty proceedings were initiated whichever period expires later
3.			Where relevant assessment or other order is the subject matter of appeal to Commissioner (Appeal) or to the Appellate Tribunal, to the High Court or to the Supreme Court or is subject matter of revision under section 263 or section 264 but the penalty order has been passed before the order of Commissioner (Appeal) or Appellate Tribunal or High Court or Supreme Court is received by the Chief Commissioner or the Commissioner of Income Tax or before the order of revision under section 263 or 264 is passed by the Commissioner [Section 275(1A)]	An order imposing or enhancing or reducing or canceling penalty or dropping the proceedings for the imposition of penalty may be passed on the basis of assessment as revised by giving effect to such order of the Commissioner (Appeal) or the Appellate Tribunal or the High Court or the Supreme Court or order of revision under section 263 or section 264. However, in the above case no order of imposing or enhancing or reducing or canceling or dropping the proceeding for the imposition of penalty shall be passed. (a) unless the assessee has been heard or has been given a reasonable opportunity of being heard; (a) after the expiry of 6 months from the end of the month in which the order of the Commissioner (Appeals) or the Appellate Tribunal or the High Court or the Supreme Court is received by the Chief Commissioner or the Commissioner or the order of revision under section 263 or section 264 is passed.

No order imposing a penalty shall be made —

(1) by the ITO where the penalty exceeds ₹10,000.

(2) by the Assistant Commissioner or Deputy Commissioner where the penalty exceeds ₹20,000 except with the prior approval of the Joint Commissioner.

Even after inserting the proviso to section 275(1)(a) which has extended the period of limitation from 6 months to one year, where the appeal has been filed against the assessment order to Commissioner (Appeal), such proviso shall not be applicable to cases where further appeal has been preferred to Tribunal under section 253 against the order of Commissioner (Appeal). In such cases, the limitation period for levy of penalty would be as provided for in section 275(1)(b) i.e. six months from the end of the month in which order of Tribunal is received by Chief Commissioner or Commissioner [Rayala Corporation (P) Ltd vs. Union of India (2007) 161 Taxman 127 (Mad)].

However, as per Explanation to section 275, in computing the period of limitation the following period shall be excluded:

(i) the time taken in giving an opportunity to the assessee to be reheard under the proviso to section 129;

(ii) any period during which the immunity granted under section 245H remained in force; and

(iii) any period during which a proceeding under this Chapter for the levy for penalty is stayed by an order or injunction of any court.

		Rigorous imprisonment	
Section	**Nature of Default**	**Minimum Period**	**Maximum Period**
275A	Dealing with seized assets in contravention of the order made by the officer conducting search	Any period up to 2 years and fine	2 years and fine
275B	Failure to comply with the provision of section 132(1)(iib)	Any period up to 2 years and fine	2 years and fine
276	Removal, concealment, transfer or delivery of property to tax recovery	Any period up to 2 years and fine	2 years and fine
276A	Failure to comply with the provisions of section 178(1) & (3) by liquidator of a company	Any period up to 2 years but not less than 6 months in absence of special and adequate reasons	2 years
276B	Failure to pay tax to the Government's treasury or failure to pay to the Government tax payable by him as required by section 115-O(2) or second proviso to section 194B	3 months and fine	7 years and fine
276BB	Failure to pay to the credit of Central Government tax collected u/s 206C	3 months and fine	7 years and fine
276C(1)	Wilful attempt to evade tax penalty or interest imposable under the Act (non-cognizable as per Sec. 279A)	If tax evaded exceeds ₹1,00,000, then for 6 months & fine; otherwise 3 months and fine.	If tax evaded exceeds ₹1,00,000, 7 years & fine; otherwise 3 years and fine.
276C(2)	Wilful attempt to evade the payment of any tax, penalty or interest (non-cognizable as per Sec. 279A).	3 months and fine	3 years and fine

276CC	Wilful failure to file return of income in time u/s. 139(1), or in response to notice u/s. 142(1) or sec. 148(Non-cognizable as per Sec. 279A)	If tax evaded exceeds ₹1,00,000, 6 months and fine In any other case, 3 months and fine. Note: No prosecution if : (i) the return is filed before the expiry of the Assessment Year; or (ii) the tax payable on regular assessment, as reduced by TDS and advance tax does not exceed ₹3,000	If tax evaded exceeds ₹1,00,000, 7 years & fine; otherwise 3 years and fine
276CCC	Wilful failure to furnish in due time the return of total income which is required to be furnished u/s 158BC.	3 months and fine	3 months and fine
276D	Wilful failure to produce books of account and documents u/s 142(1) or wilful failure to comply with a direction to get the accounts audited u/s 142(2A)	Any period upto 1 year and/or fine of ₹4 for every day during which default continues.	1 year and/or fine of ₹10 every day during which default continues.
277	Making a false statement in verification or delivering a false account or statement (non-cognizable as per Sec. 279A)	If tax evaded exceeds ₹ 1,00,000; 6 months & fine; otherwise 3 months and fine.	If tax evaded exceeds ₹1,00,000, 7 years; otherwise 3 years and fine.
278	Abetment to make a false statement or declaration. (non- cognizable as per, Sec. 279A)	If tax evaded exceeds ₹1,00,000; 6 months; otherwise 3 months and fine.	If tax evaded exceeds ₹1,00,000, 7 years; otherwise 3 years and fine.
278A	Punishment for second and subsequent offences under sections 276B, 276C(1), 276CC, 277 or 278.	6 months for every offence	7 years for every offence & fine
278B and 278C	Offences committed by companies/ firms or HUFs- Criminal liability of managing director managing partner, karta or any such officer, who wilfully committed the offence for the company/firm or HUF.	Same as in the case of the company/firm/ HUF	Same as in the case of the company/firm/ HUF
280(1)	Disclosure of particulars by public servants in contravention of Sec. 138(2) (prosecution to be instituted with the approval of Central Government)	Up to 6 months and fine.	6 months and fine.

If there is a reasonable cause, it can be offered as a defense against penalty, prosecution, etc.

Reasonable cause can be reasonably said to be a cause which prevents a man of average intelligence and ordinary prudence, acting under normal circumstances, without negligence or inaction or want of *bona fides* - *Azadi Bachao Andolan* vs. *Union of India* 252 ITR 471 (Delhi).

'Reasonable cause' as applied to human action is that which would constrain a person of average intelligence and ordinary prudence. It means an honest belief founded upon reasonable grounds, of the existence of a state of circumstances, which, assuming them to be true, would reasonably lead any ordinary prudent and cautious man, placed in the position of the person concerned, to come to the conclusion that the same was the right thing to do - *Woodward Governors India (P.) Ltd.* vs. *CIT* 118 Taxman 433 (Delhi).

The words "reasonable cause" in the section must necessarily have a relation to the failure on the part of the assessee to comply with the requirement of the law which he had failed to comply with. *Kalakrithi* vs. *ITO* 125 Taxman 97 (Mad.).

Liability of directors of private company in liquidation.

Under certain circumstances directors of private company in liquidation are liable to tax liability of the company. Care should be taken to ensure that directors are not exposed to this risk.

Section 179 provides that where any tax due from a private company in respect of any income of any Previous Year or from any public company of any Previous Year during which such other company was a private company cannot be recovered, then, every person who was a director of the private company at any time during the relevant Previous Year shall be jointly and severally liable for the payment of such tax.

No recovery can be made from a director if the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company.

Section 179 operates without regard to any contrary provision about limited liability, etc. contained in the Companies Act, 2013.

Following Explanation 4 shall be substituted for the existing Explanation 4 of sub-section (1) of section 271 by the Finance Act, 2015, w.e.f. 1-4-2016 :

Explanation 4.— For the purposes of clause (iii) of this sub-section,—

(a) the amount of tax sought to be evaded shall be determined in accordance with the following formula—

(A – B) + (C – D)

where,

A = amount of tax on the total income assessed as per the provisions other than the provisions contained in section 115JB or section 115JC (herein called general provisions);

B = amount of tax that would have been chargeable had the total income assessed as per the general provisions been reduced by the amount of income in respect of which particulars have been concealed or inaccurate particulars have been furnished;

C = amount of tax on the total income assessed as per the provisions contained in section 115JB or section 115JC;

D = amount of tax that would have been chargeable had the total income assessed as per the provisions contained in section 115JB or section 115JC been reduced by the amount of income in respect of which particulars have been concealed or inaccurate particulars have been furnished:

Provided that where the amount of income in respect of which particulars have been concealed or inaccurate particulars have been furnished on any issue is considered both under the provisions contained in section 115JB or section 115JC and under general provisions, such amount shall not be reduced from total income assessed while determining the amount under item D:

Provided further that in a case where the provisions contained in section 115JB or section 115JC are not applicable, the item (C – D) in the formula shall be ignored;

(b) where in any case the amount of income in respect of which particulars have been concealed or inaccurate particulars have been furnished has the effect of reducing the loss declared in the return or converting that loss into income, the amount of tax sought to be evaded shall be determined in accordance with the formula specified in clause (a) with the modification that the amount to be determined for item (A – B) in that formula shall be the amount of tax that would have been chargeable on the income in respect of which particulars have been concealed or inaccurate particulars have been furnished had such income been the total income;

(c) where in any case to which Explanation 3 applies, the amount of tax sought to be evaded shall be the tax on the total income assessed as reduced by the amount of advance tax, tax deducted at source, tax collected at source and self-assessment tax paid before the issue of notice under section 148.

Example:

The following information is noted from the records of X Ltd. for the assessment year 2016-17:

	General provisions (₹)	MAT (₹)
Income/book profit as per return of income	7,00,000	16,00,000
Add: Addition on estimate basis (not representing concealed income)	10,000	Nil
Add: Amount of concealed income (sale to A Ltd. not recorded in books of account as discovered by the Assessing Officer) (as per assessment order)	30,000	30,000
Add: Amount of concealed income (being deliberate attempt to conceal income by claiming higher deduction under section 35, even no explanation is offered) (as per assessment order)	70,000	Nil
Add: Deferred tax (being deliberate attempt by X Ltd. to declare lower book profit by not adding deferred tax which appeared on the debit side or profit and loss account) (as per assessment order)	Nil	80,000
Net income/book profit (as per assessment order)	8,10,000	17,10,000
Tax liability/MAT	2,50,290	3,25,840

Tax payable as per assessment order is ₹ 3,25,840. What is tax sought to be evaded for the purpose of concealment penalty under section 271(1)(c)?

Solution:

Tax sought to be evaded will be calculated as follows -

		₹
A	= Normal tax on ₹ 8,10,000	2,50,290
B	= Normal tax on (₹ 8,10,000 - ₹ 30,000 - ₹ 70,000)	2,19,390
C	= MAT on ₹ 17,10,000	3,25,840
D	= MAT on (₹ 17,10,000 - ₹ 80,000) (₹ 30,000 will not be reduced as it is also considered for computing normal income)	3,10,597
Tax sought to be evaded = (A- B) + (C - D)		46,143

Case Laws:

(1) Where assessee produced all the books and records, the Assessing Officer rejected the books and estimated income and did not record the finding of willful neglect on part of the assessee, penalty cannot be levied [Ambassador Dry Cleaners vs. UOI (1994) 210 ITR 292 (Raj)].

(2) When a claim was made relying on several High Court decisions, the assessee's claim cannot be said to be mala fide. Mere rejection of claim would not amount to concealment [CIT vs. Bombay Pipe Traders (1995) 213 ITR 282 (Bom)].

(3) Where inflation in purchases and difference in cash credits was due to totaling errors and non-posting of cash book entries in the ledger, there was no willful neglect on part of the assessee. Penalty not leviable [CIT vs. Raja Corporation (1994) 205 ITR 533 (Mad)].

(4) Where assessee discovered mistakes in the books of account which were brought to the notice of tax authorities, followed by a revised return, penalty cannot be levied for concealment [Varkey Chacko vs. CIT (1993) 203 ITR 885 (SC)].

(5) No penalty order can be passed unless assessment is completed or if assessment order has been cancelled [Ripudaman Singal vs. ITO (1995) 83 Taxman 173 (Chd)(AT)].

(6) Where the Assessing Officer rejected books of account in the absence of expense vouchers, and a flat rate of 10% was adopted as profit, it was not a case of detection of concealed income and it was only a suspicion of concealment [CIT vs. J.V. Apadurai Chettiar Co.(1996) 221 ITR 849 (Mad)].

(7) Where assessee filed confirmatory letter from lender in respect of cash credit and the lender subsequently denies the loan, followed by a revised return by assessee offering additional amount of cash credit before assessment, there was no concealment [CIT vs. Kusum Products Ltd (1993) 203 ITR 672 (Cal)].

(8) Where assessee disclosed that it had received interest on tax refunds and claimed that the same was assessable in the earlier year and the Tribunal found that the same was assessable in the earlier year and not current year, there was no concealment [CIT vs. Shah (P.M.) (1993) 203 ITR 792 (Bom)].

(9) Cash credits were added as income, and no other material was shown to prove concealment. It was held that mere rejection of assessee's Explanation did not amount to concealment [CIT vs. Bimla Devi Sharma (1991) 192 ITR 482 (Patna)].

(10) Where it was found that the disparity was because the management of business had suddenly passed to young and inexperienced persons, the penalty could not be levied [CIT vs. Dajibhai Kanjibhai (1991) 189 ITR 41 (Bom)].

(11) No penalty merely because of disallowance of certain expenses bona fide claimed by assessee [CIT vs. Rose Lock Factory (1993) 117 Taxation 366 (Guj)].

(12) Where creditors confirmed transactions or were produced before the Tax Officer, no addition of cash credit stands and hence penalty quashed [Orissa Oil Industries Ltd vs. Dy. CIT (1996) 58 ITD 403 (Cuttack)(AT)].

(13) Where the assessee trust disclosed its income fully, but did not pay tax at the correct rate of tax, it cannot be said to have concealed income or furnished inaccurate particulars thereof. Therefore penalty is not leviable [Harshvardhan Chemicals & Minerals Ltd vs. Dy. CIT (1991) 39 TTJ 212 (Jp) (AT)].

(14) In respect of cash credits added under section 68, the lenders filed confirmations and affidavits indicating source of money given to the assessee. It was held that assessee had substantiated its Explanation with evidence. Penalty was held to be not justified [Ram Commercial Enterprises Ltd. vs. ACIT (1995) 52 ITD 147 (Del)(AT)].

(15) The assessee claimed depreciation and investment allowance on certain machinery claimed to be installed during the year. The Assessing Officer did not accept the date of installation to be true and disallowed the claim and also levied concealment penalty. It was held by the Tribunal that assessees claim of deprecation and investment allowance was made on certain basis and even though the same was not considered to be conclusive proof of installation on particular dates, no penalty can be levied for furnishing inaccurate particulars [Gulamrasul M. Pathan vs. CIT (Asst.) (1996) 57 ITD 129 (Ahd)(AT)].

(16) The company received cash subscription towards its equity share capital. The company furnished names and address of the subscriber. The Income-tax Officer levied penalty on the ground that the assessee did not prove credit-worthiness of subscribers and it had concealed income from undisclosed sources. The Tribunal held that the Assessing Officer could have carried out further enquires by issuing summons to various subscribers. He could not have expected the assessee to have all the information about the shareholders. Further, penalty cannot be levied on the basis of findings in the assessment proceedings. There must be independent finding that there was concealment. Accordingly, penalty was deleted [Union Electric Corporation vs. ACIT (1995) 78 Taxman 29 (Ahd)(AT)].

(17) Where Income-tax Officer made additions in respect of initial capital shown in the books of account without verifying the fact that assessee could have some money out of his savings from earlier years income, no penalty could be levied [Geo Sea Foods vs. ITO (1991) 37 ITD 233 (Coch)(AT)(TM)].

(18) The assessee following cash method made certain payment for import of machinery. The accountant by mistake debited the amount to cost of plant and machinery and depreciation thereon was claimed although machinery was not received during the relevant year. The Tribunal held that this was a case of bona fide mistake and penalty deserved to be deleted [Bangalore Steel Distributors vs. ITO (1995) 51 TTJ 125 (Bang)(AT)].

ILLUSTRATIONS ON PENALTY & PROSECUTION

Illustration 1.

Ram, an individual had filed a return of income of ₹4,00,000 for the Assessment Year 2016-17. He paid a sum of ₹10,000 as tax whereas the tax payable on such income was ₹20,600 (including Education Cess + SHEC). His income is assessed at ₹4,90,000 and the tax payable on the assessed income is ₹29,870. Ram wishes to file an appeal against the above order. Advise Ram about the procedure of filing an appeal?

Solution:

(a) Ram should deposit tax of ₹10,600 i.e. tax payable on returned income minus tax deposited by him (₹ 20,600 - ₹ 10,000).

(b) Ram should deposit ₹1,000 as filing fee as the income assessed is more than ₹2,00,000.

(c) He should file an appeal in Form 35 (in duplicate).

(d) Appeal should be filed within 30 days of the receipt of the assessment order.

(e) He should apply to the Assessing Officer for stay of demand of ₹9,270 (₹29,870 - ₹20,600).

Illustration 2.

X did not file any return of income for the Assessment Year 2015-16. The Assessing Officer assessed his income at ₹3,20,000 under section 144 after giving him show cause notice to which X did not respond. Besides the tax, the interest was charged under sections 234A, 234B and 234C. The notice of demand of ₹22,500 (including interest) was sent to X on 5-3-2016 which was received by him on 7-3-2016. Advise X, the procedure of filing an appeal?

Solution:

(a) The appeal against the order passed by the Assessing Officer under section 144 should be filed to Commissioner (Appeal) within 30 days of the receipt of notice of demand i.e. on or before 6-4-2016 (within 30 days starting from 8-3-2016).

(b) A filing fee of ₹1,000 shall have to be deposited before filing such appeal.

(c) X should apply to the Commissioner (Appeal) for exemption of the payment of tax and interest of ₹22,500 on or before 6-4-2016. If the Commissioner (Appeals) exempts the payment of tax, then appeal filed shall be valid appeal. On the other hand, if the Commissioner (Appeal) asks the assessee to deposit full/part amount of the demand say by 31-5-2016 then the appeal shall be admitted only if the money is deposited by 31-5-2016 and proof of same is filed.

Illustration 3.

Can a CIT make a revision in regard to an order that has been earlier rectified due to some mistake?

Solution: Where an original order of assessment has been rectified, there remains no initial order in existence and as such the Commissioner cannot exercise his power of revision with reference to the original order [CIT vs. Vippy Solvex Products (P) Ltd (1997) 228 ITR 587 (MP)].

Illustration 4.

Can a CIT direct an Assessing Officer under section 263 to pass an order?

Solution:

The Commissioner is not empowered under section 263 to direct the Assessing Officer to pass an order [Dinwala (P.P.) vs. CIT (1995) 78 Taxman 421 (Cal)].

Illustration 5.

Is it necessary for the order of the Assessing Officer to be served before making it subject matter of proceedings under section 263?

Solution:

An order passed by the Assessing Officer is not effective till it is served on the assessee. Therefore, where the assessment order was passed but was not served it could not be made the subject-matter of proceedings under section 263 [Jijeebai Shinde vs. CIT (1986) 157 ITR 122 (MP)].

Illustration 6.

Can a CIT revise the order of the Income Tax Officer even if the same has been passed with the directions of the superior authorities?

Solution:

The Commissioner of Income-tax has jurisdiction under section 263 to revise an order passed by the Income-tax Officer with the approval of superior authority under section 144A or 144B [T.N. Civil Supplies Corpn. Ltd vs. CIT (2003) 260 ITR 82 (SC)].

Illustration 7.

Can you make a revision petition u/s 264 if application made u/s 197 is rejected by the Assessing Officer?

Solution:

If an application u/s 197 relating to obtaining a certificate from Assessing Officer for no deduction or deduction of tax at lower rate is rejected by the Assessing Officer, it can be revised by the Commissioner under section 264 [Larsen & Toubro Ltd. vs. CIT (2010) 190 Taxman 373 (Bom)].

Illustration 8.

Who is responsible for initiating penalty? Can the First Appellate Authority initiate penalty on the findings of Assessing Officer?

Solution:

Penalty should be imposed by the Assessing Officer or the First Appellate Authority on their respective findings only [CIT vs. Shadiram Balmukund (1972) 84 ITR 183 (All)]. The fact that during the original assessment proceedings, the Assessing Officer did not initiate penalty proceeding, is no bar to the exercise of such power by the First Appellate Authority [Kamlapat Motilal vs. CIT (1962) 45 ITR 266 (SC)].

Illustration 9.

If the facts of the transactions are disclosed in the return can a penalty for concealment be imposed?

Solution:

Penalty should not be imposed, if the assessee has claimed any exemption after disclosing the relevant basic facts of the transaction of the income and under ignorance of the provisions of the Act of 1961 has not offered that amount for tax. In such cases rather it is the duty of the Assessing Officer to ask for further details and tax the income if it is liable to tax. If the assessee had shown 'Long-term Capital Gain' and claimed exemption, but the transaction had been disclosed in the return. There was no concealment of income and penalty could not be imposed [Chandrapal Bagga vs. Income-tax Appellate Tribunal (2003) 261 ITR 67 (Raj)].

Illustration 10.

Sampat filed a return of income declaring an income of ₹6,25,000. Assessing Officer added unexplained cash credits of ₹2,00,000 and assessed the income at ₹8,25,000. Sampat filed an appeal to Commissioner (Appeal) who further enhanced the income by ₹1,12,500 to ₹9,37,500. Now, Sampat decided not to go for further appeal. Assessing Officer wants to levy penalty under section 271(1)(c) on ₹3,12,500. Is the Assessing Officer justified?

Solution:

The Supreme Court held in CIT vs. Shadiram Balmukund (1972) 84 ITR 183 (All) that the Assessing Officer can levy penalty on the additions made by him and not on the additions made by Commissioner (Appeal). Similarly Commissioner (Appeal) can levy penalty on the additions made by him and not on the additions made by the Assessing Officer. Therefore Assessing Officer can levy penalty on ₹2,00,000 and is not justified in levying penalty on ₹3,12,500.

In this case Assessing Officer had initiated the penalty proceedings before completing the assessment, but Commissioner (Appeal) had not initiated the penalty proceedings before passing the order under section 250. If the Assessing Officer had levied penalty on ₹3,12,500, in view of the above judgement, he will revise the penalty order and levy penalty on ₹2,00,000. Commissioner (Appeal) cannot levy penalty since he has not initiated the penalty proceedings before passing the order under section 250.

Illustration 11.

If there were certain disallowances while computing income under normal provisions but the assessment was made on income computed under section 115JB, will the penalty for concealment be leviable?

Solution:

Where Assessing Officer made certain disallowance while computing income under normal provisions of the Act and still the tax on income so computed is less than tax payable under section 115JB and the assessment was made on income computed under section 115JB, penalty under section 271(1)(c) cannot be levied as concealment in the form of disallowance of expenditures did not lead to tax evasion [CIT vs. Nalwa Sons Investments Ltd (2010) 194 Taxman 387 (Del)].

Illustration 12.

The unexplained investment for Assessment Year 2016-17 was found to be ₹8,00,000 which the assessee claimed to have come from the intangible additions which have been made in the past years as follows:

Assessment Year	Amount (₹)
2015-16	4,00,000
2014-15	3,00,000
2013-14	2,00,000
2012-13	1,00,000
2011-12	1,00,000

You are required to describe how will penalty proceeding be initiated in this case?

Solution:

In the above case penalty proceedings will be initiated on the intangible additions as follows:

For Assessment Year	Amount (₹)
2015-16	4,00,000
2014-15	3,00,000
2013-14	1,00,000

If the entire/part of the intangible additions has already been subject to penalty in the past then no such penalty proceedings shall be initiated on such intangible additions which have been claimed to be the source of unexplained investment etc. of the current year.

Illustration 13.

Unexplained investment of ₹15,00,000 was found for Assessment Year 2016-17 and the source of such investment was claimed to have come from intangible additions made in the past. The following addition has been made and penalty imposed in the past years:

Assessment Year	Total addition	Amount of addition on which penalty levied
2015-16	5,00,000	Penalty levied on intangible additions of ₹2,00,000 only
2014-15	5,00,000	Penalty levied on intangible addition of ₹3,00,000
2013-14	5,00,000	Nil

You are required to describe how will penalty proceeding be initiated in this case?

Solution:

In the above case penalty proceedings will be initiated for Assessment Year 2016-17 on the amount mentioned in last column, calculated as under:

Assessment Year	Intangible Additions made starting from immediately preceding Assessment Years in which intangible addition is made	Penalty already levied	Balance amount on which penalty is leviable in respective Assessment Years
1	2	3	4
2015-16	5,00,000	2,00,000	3,00,000
2014-15	5,00,000	3,00,000	2,00,000
2013-14	5,00,000	—	5,00,000

Illustration 14.

Return of income submitted by a Hindu Undivided Family for Assessment Year 2016-17 was ₹ 2,90,000

Additions made by Assessing Officer are as follows:

	Amount (₹)
On account of question of law	30,000
On account of question of facts	1,10,000
Intangible additions	70,000

Compute the tax payable and penalty imposable under section 271(1)(c)

Solution :

	Amount (₹)	Amount (₹)
Return of income submitted		2,90,000
Add: Additions made by Assessing Officer		
On account of question of law	30,000	
On account of question of facts	1,10,000	
Intangible additions	70,000	2,10,000
Assessed Income		5,00,000
Tax payable		
Tax payable on Assessed Income of ₹5,00,000 (including education cess @ 2% + SHEC @ 1%)		30,900
Less: Tax paid on returned income		9,270
Balance tax payable		21,630

Penalty payable		
Tax sought to be evaded shall be determined as under:		
Tax on Assessed Income		30,900
Less: Tax on Assessed Income as reduced by concealed income i.e. Tax on ₹3,90,000 (₹5,00,000 - ₹1,10,000)		19,570
Tax sought to be evaded		11,330
Minimum penalty @ 100%		11,330
Maximum penalty @ 300%		33,990

Note:

(1) Intangible additions are normally not treated as concealed income and therefore are not subject to any penalty. Similarly, additions due to question of law are not concealment of income.

(2) In addition to tax, the HUF will have to pay interest as applicable.

Illustration 15.

Who is liable for prosecution for the offences made by HUF under Income Tax Act?

Solution :

As per section 278C(1), where an offence under the Income Tax Act has been committed by a Hindu Undivided Family, the karta thereof shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.

The karta shall not be liable to any punishment if he proves that the offence was committed without his knowledge or that he had exercised all due diligence to prevent the commission of such offence.

As per section 278C(2), where an offence under this Act has been committed by a Hindu Undivided Family and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of, any member of the Hindu Undivided Family, such member shall also be deemed to be guilty of that offence and shall be liable to be proceeded against and punished accordingly.

Illustration 16.

Kunal feels that an offer of additional income cannot be avoided during the course of hearing, but before concealment was established against him. What are the alternatives available to him?

Solution :

An admission of concealment prima facia attracts penalty. Following are the alternatives available to him:

(1) He can offer additional income and claim that the admission or offer of a higher amount as income is to purchase peace and that penalty is not attracted in such circumstances.

(2) He can claim waiver of penalty, if it is exigible, before Commissioner u/s 273A by showing that admission is prior to detection, if he pays the tax and otherwise co-operates with the Department.

(3) He can file a petition before Settlement Commission, if he can show that computation of income is complex, so that he can get immunity from penalty and prosecution.

Study Note - 19

TAX ADMINISTRATION

This Study Note includes

19.1 Tax Administration

19.1 TAX ADMINISTRATION

19.1.1 Income Tax Authorities [Section 116]

In order to discharge executive and administrative functions relating to the Act, the following Income-tax Authorities have been constituted –

(a) The Central Board of Direct Taxes;

(aa) Principal Directors General of Income-tax or Principal Chief Commission of Income-tax;

(b) Directors General of Income-tax or Chief Commissioners of Income-tax;

(bb) Principal Directors of Income-tax or Principal Commissioners of Income-tax;

(c) Directors of Income-tax or Commissioners of Income-tax or Commissioners of Income-tax (Appeals);

(cc) Additional Directors of Income-tax or Additional Commissioners of Income-tax or Additional Commissioners of Income-tax (Appeals);

(cca) Joint Directors of Income-tax or Joint Commissioners of Income-tax;

(d) Deputy Director of Income-tax or Deputy Commissioner of Income-tax or Deputy Commissioner of Income-tax (Appeals);

(e) Assistant Directors of Income-tax or Assistant Commissioners of Income-tax;

(f) Income-tax Officers;

(g) Tax Recovery Officers;

(h) Inspectors of Income-tax.

19.1.2 Appointment of Income-Tax Authorities [Section 117]

(1) The Central Government may appoint such persons as it thinks fit to be Income-tax Authorities.

(2) Without prejudice to the provisions of sub-section (1), and subject to the rules and orders of the Central Government regulating the conditions of service of persons in public services and posts, the Central Government may authorize the Board, or a Director-General, a Chief Commissioner or a Director or a Commissioner to appoint Income-tax Authorities below the rank of an Assistant Commissioner or Deputy Commissioner.

(3) Subject to the rules and orders of the Central Government regulating the conditions of service of persons in public services and posts, an Income-tax Authority authorised in this behalf by the Board may appoint such executive or ministerial staff as may be necessary to assist it in the execution of its functions.

19.1.3 Control of Income-Tax Authorities [Section 118]

The Board may, by notification in the Official Gazette, direct that any Income-tax Authority or authorities specified in the notification shall be subordinate to such other Income-tax Authority or authorities as may be specified in such notification.

19.1.4 CENTRAL BOARD OF DIRECT TAXES (CBDT) [Section 119]

The Central Board of Direct Taxes (CBDT) has been constituted under the Central Board of Revenue Act, 1963. It works under the Ministry of Finance. The important powers of CBDT are:

(i) To make rules for carrying out purposes of the Act [Sec. 295].

(ii) To decide jurisdiction of the Income-tax Authorities [Sec. 120].

(iii) To issue instructions, orders and directions to other Income-tax Authorities for proper administration of this Act and all other persons employed in the execution of this Act. However, it cannot issue instructions to the Commissioner of Income-tax (Appeals). It cannot issue a direction to any Income-tax Authority to dispose of a case in a particular manner. [Sec. 119]

(iv) To declare an organization as company [Sec. 2(17) (iv)].

(v) To entertain objections in respect of search and seizure under the Act. [Sec. 132(1)].

(vi) To relax the provisions of Sections 139, 143, 144, 147, 148, 154, 155, 158BFA, 201(1A), 210, 211, 234A, 234B, 234C, 271 and 273 or otherwise [Section 119(2)(a)].

(vii) Power of relaxing any requirement contained in Chapter IV (provisions for computation of income under various heads) or Chapter VI-A (provisions for deductions from Gross Total Income) [Section 119(2)(c)].

(viii) To issue such general or special orders for relaxation of the provisions of sections relating to FBT viz; 115WD, 115WE, 115WF, 115WG, 115WH, 115WJ and 115WK [Section 119(2)(a)].

(ix) To prescribe categories of transactions and documents pertaining to business or profession, where quoting of PAN is necessary [Sec, 139A(4)].

(x) Prescribing qualifications for Authorized Representatives [Sec. 288].

(xi) To condone delay for seeking CBDT's approval, where it is required [Sec. 293B] and authorize any Income Tax Authority not being Commissioner of Income-tax (Appeals), to admit belatedly ant claim for exemption, deduction, refund or relief [Section 119(2)(b)].

(xii) The Act also assign powers and functions in Sections 2(18), 11(1)(c), 35(3), 36(1)(iv), 44AA, 80RRA, 80U, 118, 124(2), 127, 132(1), 138, 197(2A), 200, 228A, 246, 273A(2), 279, the Second Schedule and the Forth Schedule.

Circulars issued by the CBDT are legally binding on the revenue and this binding character attaches to the circulars even if they are found not in accordance with the correct interpretation of a statutory provision and they depart or deviate from such construction - *K.P. Varghese* vs. *ITO* 131 ITR 597 (SC).

It is well-settled that circulars can bind the ITO but will not bind the appellate authority or the Tribunal or the Court or even the assessee - *CIT* vs. *Hero Cycles (P.) Ltd.* 228 ITR 463 (SC).

CBDT has power, interalia, to tone down the rigor of the laws and ensure fair enforcement of its provision by issuing circular.

Circular contemplated in Sec.119 (2)(a) cannot be adverse to the assessee. Power is given for the purpose of just, proper and efficient management of work of assessment. Circular, however are not meant for contradicting or nullifying any provision of the statue. They are meant to mitigate the rigor of application of a particular provision. So long as such a circular is in favour, it would be binding on the departmental authorities in view of the provision of sec. 119 to ensure a uniform and proper administration & application of the IT Act - UCO Bank vs. CIT 237 ITR 899 (SC).

As per section 120, Income-tax Authorities shall exercise all or any of the powers and perform all or any of the functions conferred on or, assigned to such authorities by or under this Act in accordance with such directions as the Board may issue or the Board may authorise any other Income-tax Authority to issue orders in writing for the exercise of the powers and performance of the functions by all or any of the other Income-tax Authorities who are subordinate to it.

W.r.e.f. assessment year 1988-89, Explanation to sub-section (1) of section 120 has been inserted so as to provide that any Income-tax Authority, being an authority higher in rank, may exercise the powers and perform the functions of the Income-tax Authority lower in rank, if it is so directed by the Board under the said section. It has also been provided that any such direction issued shall be deemed to be a direction issued by the Board under the said sub-section (1).

As per section 120(3) in issuing the directions or orders, the Board or other Income-tax Authority authorised by it may have regard to any one or more of the following criteria, namely:

(a) territorial area;

(b) persons or classes of persons;

(c) incomes or classes of incomes; and

(d) cases or classes of cases.

According to section 120(4), the Board may, by general or special order, and subject to such conditions, restrictions or limitations as may be specified therein

(a) authorise any Director General or Director to perform such functions of any other Income-tax Authority as may be assigned to him by the Board;

(b) empower the Director General or Chief Commissioner or Commissioner to issue orders in writing that the powers and functions conferred on, or assigned to, the Assessing Officer by or under this Act in respect of any specified area or persons or classes of persons or incomes or classes of income or cases or classes of cases, shall be exercised or performed by a Joint Commissioner.

Further, the Board may require two or more Assessing Officers (whether or not of the same class) to exercise and perform, concurrently, the powers and functions in respect of any area or classes of cases.

Notification issued under section 120 conferring jurisdiction acts only prospectively and cannot be retrospective in effect [West Bengal State Electricity Board vs. DCIT (2005) 278 ITR 218 (Cal)].

Where the assessee claims the status as non-resident, then the AO (International Taxation) had the jurisdiction to make the assessment. [Manoj Kumar Reddy vs. ITO (2010) 42 DTR 171 (Bang)(Trib)].

As per section 129, whenever in respect of any proceeding under this Act an Income-tax Authority ceases to exercise jurisdiction and is succeeded by another who has and exercises jurisdiction, the Income-tax Authority so succeeding may continue the proceeding from the stage at which the proceeding was left by his predecessor:

However, the assessee concerned may demand that before the proceeding is so continued the previous proceeding or any part thereof to be reopened or that before any order of assessment is passed against him, he be reheard.

Such period which the Assessing Officer has taken to rehear the case, on the request of assessee, shall be excluded while determining the time limit of completion of assessment given under section 153.

19.1.5 Director General/Director

The Central Government has power to appoint Director General and Director [Sec. 117]. The CBDT authorize them to perform such functions as may be assigned to them by [Sec. 120]. The powers enjoyed by them include:

(i) To appoint an Income-tax Authority below the rank of Assistant Commissioner/Deputy Commissioner, if authorised by the Board [Sec. 117].

(ii) To direct the Joint Commissioner to function and assume the powers of Assessing Officer, if so authorised by the Board [Sec. 120].

(iii) To transfer cases from one or more Assessing Officers to any other Assessing Officer who is subordinate to him [Sec. 127].

(iv) To enquire or investigate concealed income of any person within his jurisdiction [Sec. 131(1A)].

(v) Authorise any Joint Director / Joint Commissioner, Deputy Director / Deputy Commissioner, Assistant Director / Assistant Commissioner or Assessing Officer to enter, search and seize valuables [Sec. 132(1)].

(vi) To give instructions to Income Tax Officers [Sec. 119(2)].

(vii) To enquire or investigate into concealment [Sec. 131(1A)].

(viii) To search and seizure [Sec. 132].

(ix) To requisition books of accounts, etc.[Sec. 132A].

(x) To survey [Sec. 133A].

(xi) To make an enquiry [Sec. 135].

19.1.6 Commissioners of Income-tax

Commissioners of Income-tax are appointed by the Central Government. A Commissioner of Income-tax enjoys the following administrative as well as judicial powers and functions under the different provisions of the Act.

(i) powers pertain to registration of a charitable trust or institution [Sec. 12A(1)(a)];

(ii) approval of an annuity contract [Sec. 80E];

(iii) appointment of Income-tax Officers (Class II) and Inspectors of Income-tax [Sec. 117(2)];

(iv) instructions to subordinate authorities [Sec. 119] ;

(v) shifting of jurisdiction [Sec. 125] ;

(vi) transfer of cases [Sec. 127] ;

(vii) assignment of functions to Inspectors of Income-tax [Sec. 1281;

(viii) discovery, production of evidence [Sec. 131] ;

(ix) search and seizure [Sec. 132] ;

(x) requisite books of account [Sec. 132A] ;

(xi) any enquiry [Sec. 135] ;

(xii) disclosure of information respecting assesses [Sec.138] ;

(xiii) granting sanction for issue of notice to reopen assessment after the expiry of 4 years [Sec. 151(2)];

(xiv) authorising Income-tax Officers to recover any arrear of tax due from an assessee by distraint and sale of his movable property [Sec. 226(5)] ;

(xv) set off of refunds against tax remaining payable [Sec. 245] ;

(xvi) directing the Assessing Officer to prefer an appeal to Appellate Tribunal against the order of the Commissioner (Appeals) [Sec. 253(2)] ;

(xvii) appeal to High Court [Sec. 260A] ;

(xviii) revision of orders passed by Assessing Officer which are prejudicial to the revenue [Sec. 263] ;

(xix) revision of orders passed by subordinate authorities on his own motion or on the application of the assessee [Sec. 264] ;

(xx) reduction or waiver of penalty in certain cases [Sec. 273A] ;

(xxi) to award and withdraw recognition to provident funds [Schedule IV].

19.1.7 Commissioner of Income-Tax (Appeals)

Appointment is made by the Central Government. The following are important powers:

(i) Power regarding discovery, production of evidence etc. [Sec. 131]

(ii) To condone delay in filing of appeal.

(iii) Power to call for information. [Sec. 133]

(iv) Power to inspect register of companies. [Sec. 134]

(v) To dispose of an appeal and to confirm, reduce, enhance or annul the assessment. - [Sec. 251]

(vi) Power to impose a penalty. [Sec. 271 and 272A]

(vii) Power to set off any refund against arrears of tax. [Sec. 245].

(viii) The Commissioner (Appeals) has inherent powers to stay recovery proceedings *Paulsons Litho Works* vs. *ITO* 208 ITR 676 (Mad.).

19.1.8 Joint Commissioner of Income Tax

They are appointed by the Central Government. They enjoy the following powers :-

(i) Power regarding discovery, production of evidence, etc. [Sec. 131]

(ii) Power of search and seizure, if authorised. [Sec. 132]

(iii) Power to call for information [Sec. 133]

(iv) Power to survey [Sec. 133A]

(v) Power to make an enquiry [Sec. 135]

(vi) Power to collect certain information [Sec. 133B]

(vii) Power to inspect register of companies [Sec. 134]

(viii) To sanction reopening of assessment after the expiry of 4 years, if the assessment is made under any section other than sections 143(3) and 147.

(ix) Instruction to the Assessing Officers. [Sec. 119(3)]

19.1.9 Assessing Officer

'Assessing Officer' means the Assistant Commissioner or Deputy Commissioner or Assistant Director or Deputy Director or the Income-tax Officer who is vested with the relevant jurisdiction by virtue of directions or orders issued under Section 120 or any other provision of this Act, and the *Additional Commissioner or Additional Director or* Joint Commissioner or Joint Director who is directed under the said section 120 to exercise or perform all or any of the powers and functions conferred on, or assigned to, an Assessing Officer under this Act [Sec. 2(7A)]

The following are some of the powers of Income-tax Officers —

(i) Power regarding discovery, production of evidence, etc. [Sec. 131]

(ii) Power of search and seizure, if authorised. [Sec. 132]

(iii) Power to requisition books of accounts. [Sec. 132A]

(iv) To apply the assets seized and retained u/s. 132 in satisfaction of the existing liabilities of the assessee under Direct Taxes Act. [Sec. 132B]

(v) Power to call for information. [Sec. 133]

(vi) Power to survey. [Sec. 133A]

(vii) Power to collect certain information [Sec. 133B]

(viii) Power to inspect register of companies. [Sec. 134]

(ix) Power to allot Permanent Account Number. [Sec. 139A]

(x) Power to impose penalties. [Sec. 142]

(xi) Power to issue direction for setting accounts audited. [Sec. 142]

(xii) Power to make assessment. [Sec. 143, 144]

(xiii) Power to reassess income which has escaped assessment. [Sec. 147]

(xiv) Power to rectify mistakes apparent from the records, either on his own or on an application made by the assessee. [Sec. 154]

(xv) Power to grant a certificate to an assessee to receive a payment without deduction of tax at source or deduction of tax at source at a lower rate than prescribed [Sec. 197]

(xvi) Power to grant refund. [Sec. 237, 240]

As per section 127(1), the Director General or Chief Commissioner or Commissioner may, after giving the assessee a reasonable opportunity of being heard in the matter, wherever it is possible to do so, and after recording his reasons for doing so, transfer any case from one or more Assessing Officers subordinate to him (whether with or without concurrent jurisdiction) to any other Assessing Officer or Assessing Officers (whether with or without concurrent jurisdiction) also subordinate to him.

There may be situations where the Assessing Officer from whom the case is transferred and the Assessing Officer to whom the case is transferred do not fall under the control of the same Director General or Chief Commissioner or Commissioner of Income tax. In such cases, the Director General or the Chief Commissioner or Commissioner of Income Tax from whose jurisdiction the case is transferred shall pass an order, if such concerned higher authorities mutually agree for such transfer.

If the higher authorities are not in agreement about the transfer, then, the Board or any such authority authorised by the Board may pass the order.

If the case is transferred between Assessing Officers within the same city or locality or place, then, it is not necessary to give the assessee an opportunity of being heard.

The transfer of a case may be made at any stage of the proceedings and it is not necessary to reissue any notice already issued by the Assessing Officer or Assessing Officers from whom the case is transferred.

As per section 127, the case of any assessee may be transferred from jurisdiction of an Assessing Officer or Assessing Officers (whether or not holding concurrent jurisdiction) to the jurisdiction of another Assessing Officer or Assessing Officers (whether or not holding concurrent jurisdiction). However, before such order of transfer is made, reasons there for have to be recorded and where the transfer is to the jurisdiction of the Assessing Officer or Assessing Officers which is not situated in the same city, locality or place, the assessee has to be given an opportunity of being heard and the reasons recorded for transfer have also to be intimated to him [Ajantha Industries vs. CBDT and Ors (1976) 102 ITR 281(SC)].

It is mandatory to record reasons for transferring the case, hence, transfer of case without any notice and reasons quashed [Chaitanya vs. CIT (2010) 328 ITR 208 (Bom)].

Impugned order made under section 127(2) without reflecting any reasons for transferring the cases from one Assessing Officer to another Assessing Officer cannot be sustained [Hemang Ashvinkumar Baxi (Dr) vs. Dy. CIT & Anr. (2010) 45 DTR 38 (Guj)].

Not only is the requirement of recording reasons under section 127(1) a mandatory direction under the law, but that non communication thereof is not saved by showing that the reasons exist in the file although not communicated to the assessee. Further, opportunity of being heard has to be provided before making the order of transfer of case [Madhu Khurana vs. CIT (2010) 47 DTR 289 (Guj)].

Reasons are not required to be recorded nor an opportunity of being heard required to be given when the case is transferred from one Assessing Officer to another at the same station [Kashtram Agarwalla vs. UOI and Ors (1965) 56 ITR 14 (SC)].

In the case of intra-city transfers, though opportunity of hearing as postulated in section 127(1) and 127(2) has been dispensed with other statutory formalities, which include issuing an order are required to be complied, with Assessing Officer on his own could not transfer an income tax file to another officer without an order under section 127(3) [Kusum Goyal vs. ITO (2010) 48 DTR 343 (Cal)].

In the matter of transfer of a case under section 127 of the Act, it is necessary that the authority which proposes to transfer the case must, wherever it is possible to do so, give the assessee a reasonable opportunity of being heard with a view to enable him to show cause against the proposed transfer. The notice must propose to give a personal hearing. It is also necessary to mention in the notice the reasons for proposed transfer so that the assessee could make an effective representation with reference to the reasons set out. It is not sufficient merely to say in the notice that the transfer is proposed to 'facilitate detailed and coordinated investigation'. The reason cannot be too vague and general in nature and should be based on material facts. It is again not sufficient to record reasons in the file but it is also necessary to communicate the same to the affected party [Melco India Pvt. Ltd. and Ors vs. CIT (2003) 260 ITR 450 (Del)].

Where the assessee had made a representation against the proposed transfer, a speaking order is required to be passed in his case [Parmeshwar Nath Rai vs. Chief CIT and Ors (2002) 258 ITR 591 (Cal)]. The order of transfer has to be made by a Commissioner, Chief Commissioner or Director General to whom the Assessing Officer holding jurisdiction over the assessee is subordinate. However, where the Assessing Officer to whom case is to be transferred is subordinate to another Director General, Chief Commissioner who is not in agreement with his counterpart, the order of transfer is to be made by the Board or a Director General or Chief Commissioner notified by it.

No assessee has a vested right to have his assessment decided by any officer at any place. It is for the head of the Department to allocate work among the officers under him subject to the Act and Rules. There is no scope for interference by the High Court in these matters which are purely administrative in nature, except when there is allegation of mala fides or want of jurisdiction [Redwood Hotel Pvt. Ltd. vs. Chief CIT (2003) 259 ITR 191 (Ker)].

Where there is any change in the address or status of the assessee or there is a change in the employment or any other reason due to which the jurisdiction of the Assessing Officer has changed, the assessee can make an application for the transfer of income-tax file.

For getting the file transferred, the assessee should take the following steps:

Step 1: The assessee should submit an application in duplicate before the following authority:

(a) Where the Assessing Officer from whom the case is to be transferred and to whom the case is to be transferred, are subordinate to the same Director General or Chief Commissioner of Income-tax or Commissioner of Income Tax :— The application stating full facts in duplicate should be filed before the concerned Director General or Chief Commissioner of Income Tax or CIT, as the case may be. In this case such officer shall pass necessary orders after recording the reasons and giving opportunity to the assessee of being heard, if necessary.

(b) Where the transferor and transferee Assessing Officers are within the jurisdiction of different Director General/Chief Commissioner of Income Tax/CIT :— The application giving full facts and particulars should be filed before the DGIT/CCIT or CIT, as the case may be, from whose jurisdiction the file is to be transferred, with a copy to the Commissioner to whose jurisdiction the file is to be transferred and to both the transferor and transferee Assessing Officers. After receiving the application if both the Commissioners are in agreement, then the DGIT/ CCIT/CIT from whose jurisdiction the file is to be transferred shall pass the necessary order giving effect to such transfer. However, if they are not in agreement, the order may be passed by CBDT.

Step 2: The assessee should clearly mention the reasons for seeking the transfer of file in the application. In case of a transfer to a new place, new address should also be mentioned.

Step 3: An appropriate Court Fee stamp (presently Re 1) should be affixed on the original copy of the application.

19.1.11 Inspectors of Income Tax

Inspectors are appointed by the Commissioner of Income Tax.

They have to perform such functions as are assigned to them by the Commissioner or any other Income-tax Authority under which they are appointed to perform their functions.

In case of survey, inspectors have power to inspect books of account and other documents, place marks of identification, to take statements at any function, ceremony or event [Sec. 133A].

19.1.12 Change of incumbent of an Office [Section 129]

Whenever in respect of any proceeding under this Act an Income-tax Authority ceases to exercise jurisdiction and is succeeded by another who has and exercises jurisdiction, the Income-tax Authority so succeeding may continue the proceeding from the stage at which the proceeding was left by his predecessor.

Provided that the assessee concerned may demand that before the proceeding is so continued the previous proceeding or any part thereof be reopened or that before any order of assessment is passed against him, he be reheard.

19.1.13 Powers of Income Tax Authority

(1) Power to issue summons, etc. regarding discovery, production of evidence, etc. [Section 131].

(A) **Same power as of Court [Section 131(1)]:** The Assessing Officer, Joint Commissioner, Commissioner (Appeals), Commissioner and Chief Commissioner shall have the same powers as are vested in a Court under the Code of Civil Procedure, 1908, (when trying a suit) in respect of the following matters:

(i) Discovery and inspection;

(ii) Enforcing the attendance of any person including any officer of a Banking Company and examining him on oath;

(iii) Compelling the production of books of account and other documents; and

(iv) Issuing commissions.

These powers can be exercised by the aforesaid authorities only in respect of proceedings pending before them. Summons under this section will have to be issued by the Assessing Officer at the request of the assessee where the burden of proof lies on the assessee.

(B) **Power can be exercised whether any proceedings are pending or not [Section 131(1A)]:** If the Director General or Director or Joint Director or Deputy Director or Assistant Director or the Authorised Officer referred to in section 132(1), before he takes action regarding search and seizure, has reason to suspect that any income has been concealed or is likely to be concealed by any person within his jurisdiction, then for the purpose of making an enquiry or investigation relating thereto, he will be competent to exercise the powers mentioned in section 131(1) above, whether any proceedings in respect of such person or class of persons are pending before him or any Income-tax Authority or not.

Power can also be exercised for making an inquiry or investigation in respect of any person on request from Tax Authorities outside India [Section 131(2) inserted by the Finance Act, 2011, w.e.f. 1-6-2011].

For the purpose of making an enquiry or investigation in respect of any person or class of persons in relation to an agreement referred to in section 90 or section 90A, it shall be competent for any Income-tax Authority, not below the rank of Assistant Commissioner of Income Tax, as notified by the Board in this behalf, to exercise the powers currently conferred on Income-tax Authorities referred to in section 131(1). The authority so notified by the Board shall be able to exercise the powers under section 131(1) notwithstanding that no proceedings with respect to such person or class of persons are pending before it or any other Income-tax Authority.

(C) **Power to impound and retain books of account and documents [Section 131(3)]:** The Officers mentioned in sections 131(1), (1A) and (2) above, may impound and retain in its custody for such period as it thinks fit any books of account or other documents produced before it in any proceedings under this Act.

However, an Assessing Officer or an Assistant Director/Deputy Director shall not impound any books of account or documents without recording his reasons for doing so. Further, he cannot retain in his custody such books of account and documents for a period exceeding 15 days (exclusive of holidays) without obtaining the approval of the Chief Commissioner or Director General or Commissioner/Director.

The books of account and documents can be requisitioned for a period beyond 3 years.

Section 131(3) empowers Income-tax Authorities to impound and retain, inter alia, any documents produced before them and there is no precondition that such power can be exercised only when some proceedings are pending against a particular or specified individual [Suman Sehgal vs. Union of India (2006) 154 Taxman 195 (Del)].

Consequence of defaults in compliance with the terms of summons issued under section 131

As per section 272A(1), a penalty of ₹10,000 can be imposed on a person for each of the following defaults—

(i) Omission to attend to give evidence or produce the books of account or documents called for,

(ii) Refusal to answer questions put to him,

(iii) Refusal to sign the statement made by him.

(2) Power to call for information [Section 133]: The Assessing Officer, the Joint Commissioner or the Commissioner (Appeals) may require the furnishing of the following information for the purpose of this Act,—

(I) require any firm to furnish him with a return of the names and addresses of the partners of the firm and their respective shares;

(II) require any Hindu Undivided Family to furnish him with a return of the names and addresses of the manager and the members of the family;

(III) require any person whom he has reason to believe to be a trustee, guardian or agent, to furnish him with a return of the names of the persons for or of whom he is trustee, guardian or agent, and of their addresses;

(IV) require any assessee to furnish a statement of the names and addresses of all persons to whom he has paid in any previous year, rent or interest or commission or royalty or brokerage or any annuity, not being any annuity taxable under the head 'Salaries' amounting to more than one thousand rupees, or such higher amount as may be prescribed, together with particulars of all such payments made;

(V) require any dealer or broker or agent or any person concerned in the management of a stock or commodity exchange to furnish a statement of the names and addresses of all persons to whom the exchange has paid any sum in connection with the transfer, whether by way of sale, exchange or otherwise, of assets, or on whose behalf or from whom he or the exchange has received any such sum, together with particulars of all such payments and receipts;

(VI) require any person, including a banking company or any officer thereof, to furnish information in relation to such points or matters, or to furnish statements of accounts and affairs verified in the manner specified by the Assessing Officer or the Joint Commissioner or the Commissioner (Appeals) giving information in relation to such points or matters as, in the opinion of the Assessing Officer or the Joint Commissioner or the Commissioner (Appeals) will be useful for, or relevant to, any inquiry or proceeding under this Act.

However, the powers referred to in section 133(6) may also be exercised by the Director-General, the Chief Commissioner, the Director and the Commissioner.

Further that the power in respect of an inquiry, in a case where no proceeding is pending, shall not be exercised by any Income-tax Authority below the rank of Director or Commissioner without the prior approval of the Director or the Commissioner, as the case may be.

Power to collected information on requests received from Tax Authorities outside India [Thirdproviso to section 133] [Inserted by the Finance Act, 2011, w.e.f. 1.6.2011]: For the purposes of an agreement referred to in section 90 or section 90A, an Income Tax Authority not below the rank of Assistant Commissioner as may be notified by the Board under section 131(2) may exercise all the powers conferred under this section notwithstanding that no proceedings are pending before it or any other Income Tax Authority.

Failure to furnish details, information, etc. requisitioned under section 133 shall attract a penalty under section 272AA of ₹100 per day for the period during which the default continues.

(3) Power to collect certain information [Section 133B]: An Income-tax Authority may, for the purpose of collecting any information which may be useful for, or relevant to the purposes of Income-tax Act, enter:

(a) any building or place within the limits of the area assigned to such authority; or

(b) any building or place occupied by any person in respect of whom he exercises jurisdiction,

at which a business or profession is carried on, whether such place be the principal place or not of such business or profession, and require any proprietor, employee or any other person who may at that time and place be attending in any manner to, or helping in, the carrying on of such business or profession to furnish such information as may be prescribed in Form 45D.

The Income-tax Authority may enter any place of business or profession only during the hours at which such place is open for the conduct of business or profession.

The Income-tax Authority shall, on no account, remove or cause to be removed from the building or place wherein he has entered, any books of account or other documents or any cash, stock or other valuable article or thing.

The Income-tax Authority who is authorised to collects information under section 133B shall be —

(a) Joint Commissioner of Income Tax or Additional Commissioner of Income Tax.

(b) Assistance Director of Income Tax or Deputy Director of Income Tax.

(c) Assessing Officer.

(d) An Income Tax Inspector, so authorised by the Assessing Officer.

Failure to furnish information in Form No. 45D shall attract a maximum penalty of ₹1,000 under section 272AA.

(4) Power to call for information by prescribed income-tax authority [Section 133C]: The prescribed income-tax autority, may for the purposes of verification of information in its possession relating to any person, issue a notice to such person requiring him, on or before a date to be specified therein, to furnish information or documents verified in the manner specified therein, which may be useful for, or relevant to, any inquiry or proceeding under this Act.

(5) Power to inspect registers of companies [Section 134]: The Assessing Officer, the Joint Commissioner or the Commissioner (Appeals), or any person subordinate to him authorised in writing in this behalf by the Assessing Officer or the Joint Commissioner or the Commissioner (Appeals), may inspect, and if necessary take copies, or cause copies to be taken, of any register of the members, debenture holders or mortgages of any company or of any entry in such register.

Failure to allow inspection of such register or to allow copies to be taken shall attract a penalty under section 272A(2)(d) of ₹100 for every day during which the failure continues.

(6) Power of DGIT/DIT/CCIT/CIT/JCIT to make enquiry [Section 135]: The Director General or Director, the Chief Commissioner or Commissioner and the Joint Commissioner are competent to make any enquiry under this Act and for that purpose they shall have all the powers that an Assessing Officer has under this Act in relation to the making of enquiries.

Study Note - 20

LIABILITY FOR SPECIAL CASES

This Study Note includes
20.1 Liability for Special Cases

20.1 LIABILITY FOR SPECIAL CASES

20.1.1 Tax liability after the death of an individual

Where an individual assessee dies, the following situations can arise vis-a-vis the tax payable by him:

(a) The income earned by the assessee during his life time has been received by him. It only remains to be assessed or the taxes on the income, already assessed, is still to be recovered. This situation is covered by section 159.

(b) Items of income of the deceased are received after his death by his legal heirs, executors or administrators. In this situation, the income of the deceased is normally part of the estate and hence capital in the hands of the legal representatives may be assessable in their hands by virtue of special provisions such as section 176(3) or (4) i.e. liability in case of discontinued business.

(c) On the death, the assets of the estate vest, by testate or intestate succession on the heirs or legatees in specie or in specified shares and the income from the time of death accrues or arises to and is received by them. In this situation, the assessment has to be made in normal course in the hands of the heirs or legatees.

(d) On death, the estate vests in the executors or administrators for the purposes of administration and, pending such administration, the executors or administrators are in receipt of the income of the estate. This situation is provided for in section 168 i.e. liability in case of executors.

20.1.2. Liability of Legal Representatives [Section 159]

Where a person dies, his legal representatives shall be liable to pay any sum which the deceased would have been liable to pay if he had not died, in the like manner and to the same extent as the deceased.

Legal representative means a person who in law represents the estate of a deceased person, and includes any person who intermeddles with the estate of the deceased and where a party sues or issued in a representative character, the person on whom the estate devolves on the death of the party so suing or sued [Section 2(29)]

The legal representatives have been made liable to pay out of the estate, any sum which the deceased would have been liable to pay. Thus, the liability is not confined only to the amount of tax but it also extends to liability in respect of penalties, interest or any other sum that would have been payable by the deceased.

However the liability of the legal representative is limited to the extent to which the estate is capable of meeting the liability.

Consequences if the legal representative is taxable [Section 159(2) and 159(3)]: For the purpose of making an assessment (including reassessment u/s 147) of the income of the deceased and for the purpose of levying any sum in the hands of the legal representatives, the following procedure shall apply:

(a) any proceeding taken against the deceased before his death shall be deemed to have been taken against the legal representative and may be continued against the legal representative from that stage;

(b) any proceedings, which could have been taken against the deceased if he had survived, may be taken against the legal representative;

(c) all the provisions of the Act shall apply accordingly;

(d) the legal representative of the deceased shall be deemed to be an assessee;

However, the liability of the legal representative shall be limited to the extent to which the estate of the deceased is capable of meeting the liability.

Where the deceased has furnished a return and he died before the completion of assessment, fresh notice under section 143(2) and 142(1) have to be issued to the legal representative and all the provisions of the Act would apply accordingly

Personal liability of legal representative in some cases [Section 159(4)]: If the legal representative of a deceased person creates a charge on or disposes of or parts with any asset of the estate of the deceased, while the liability for tax on the income of the deceased remains undischarged, the legal representative shall be personally liable for any tax payable by him in his capacity as legal representative. However, such liability shall be limited to the value of the asset charged, sold or parted with and the personal liability mentioned above is restricted only to the tax payable and does not extend to interest/penalty or any other sum.

Case Laws

(1) Although income arising after the date of death is treated as income of the estate and is taxable in the hands of the executors u/s 168 but it will be assessed in the hands of the legal representatives u/s 159. [CIT vs. Hukumchand Mohanlal (1971) 82 ITR 624 (SC)].

(2) Where the death occurs in the middle of an accounting year, it may be necessary to apportion the accrued income on a time basis except where the income accrues, not de in diem, but on a specific day which may fall after the date of death. [Palmer vs. Cattlemore (1937) 21 TC 191 & Arvind Bhogilal vs. CIT (1976) 105 ITR 764 (Bom)].

(3) Where an assessee dies, pending any assessment proceedings, it is the duty of the Assessing Officer to ensure compliance of section 159(2) (i.e. bring the legal representative on record) before passing any orders. Hence, the assessment order passed by the Assessing Officer without bringing the legal representative on record was not justified. [CIT vs. Dalumal Shyamumal (2005) 276 ITR 62 (MP)].

(4) In case of death of assessee before proceedings for assessment are completed, legal representatives must be brought on record otherwise the assessment is void ab initio. [CIT vs. Prabhawati Gupta (1998) 231 ITR 188 (MP) and R.C. Jain (Decd.) through his legal heir R.K. Jain vs. CIT (2005) 273 ITR 384 (Del)].

(5) Where the assessee's appeal had been received by the Appellate Tribunal, the Department appeal against the order could be proceeded with after bringing on record the legal representative if the assessee has since died. [Prakash vs. ITO (2009) 312 ITR 40 (Bom)].

(6) When proceedings are taken against an individual in his representative capacity, the name of that individual should first be specified. This should be followed by words describing his capacity or characters to whether he is legal representative, or an executor or administrator. Otherwise the assessment proceedings would be illegal and of no value. The principle that should be borne in mind is that it is not the deceased or the estate of the deceased that is the assessee; he is the individual who represents the estate and it is he that is taxed in his own name and, hence, his name and identity should be clearly specified in the order of assessment. [CIT vs. Amarchand N. Shroff (1963) 48 ITR 59 (SC)].

Some exceptions have however been recognised to the operation of the rule that the assessment on a dead person is a nullity. These are as follows:

(a) Where the proceedings had come to a conclusion during the lifetime of the deceased but the assessment order was passed in the name of the deceased though by that time the officer had come to know of the death, the assessment order has been upheld as valid. [Joseph Joseph vs. ITO (Ag.) (1973) 92 ITR 114 (Ker)].

(b) Where the legal representatives have in fact appeared voluntarily or in response to notices and have allowed the proceedings to continue against the deceased without objection, the assessment may be only set aside for being done afresh, not annulled. [CIT vs. Roshan Lal (1982) 134 ITR 145 (Del)].

(c) Where one of the legal representatives filed a return in response to a notice on the deceased and did not point out to the officer that there were also other representatives, the assessments cannot be annulled. [Sajjan Kumar Saraf vs. CIT (1978) 114 ITR 155 (Cal)].

(d) The Supreme Court in the case of CIT vs. Jai Parkash Singh (1996) 85 Taxman 407 (SC) held that where after the death of an individual, one of his ten legal representatives filed returns and notice was issued to another legal representative under sections 142(1) and 143(2) and he complied with it and the assessment was duly computed, omission to service notice to all legal representative of the deceased was only an irregularity and not a nullity. Similarly, in another case where an assessment order was made without notice to all the legal representatives, it was held that such assessment order suffered from procedural irregularity which was liable to be corrected. Such assessment order was neither void nor liable to be annulled. [CIT vs. Pushpa Devi (2003) 132 Taxman 506 (Raj)].

As per section 159(1), legal representative shall be liable to pay any sum which the deceased would have been liable to pay if he had not died, "in the like manner and to the same extent as the deceased". These words imply not only that there should be a separate assessment in respect of the deceased estate (separate from the personal assessment of the legal representative) but also that the computation of the income of the deceased estate shall have to be made in the status applicable to the deceased, granting all reliefs, which the deceased may be entitled to in respect of that status, and calculating the deductions and allowances and rebates that the deceased may be entitled to, and finally levying the tax at the average rate applicable to the deceased.

Section 159 applies only in respect of income of the deceased only upto the date of death and not upto the end of the accounting year in which the death occurs. If there is a will of the deceased and the executor is appointed, the income of the estate for the period from the date of death upto the end of the accounting year in which the death occurs and thereafter till the estate is distributed shall be separately assessed in the hands of the executors. Thus, in respect of the year of death two separate and distinct assessment would have to be made, the prior one on legal representatives and the later one on the executors under section 168. It will not make any difference even if the legal representative and the executor are one and the same person.

Penalty proceeding for a default committed by the deceased can be started or continued against the legal representative under this section which applies not only in respect of tax but also any other sum i.e. penalty, fine or interest. [Smt. Tapati Pal vs. CIT (2000) 241 ITR 468 (Cal)]. Further, under this Act, the legal representative, being an assessee for the purposes of Act, is liable to a penalty for him own default e.g. penalty under section 221 for his own default in paying the tax assessed on him or on the deceased or penalty under section 271(1) for having himself submitted an incorrect return of the income of the deceased or having failed to file the return on time. A penalty already imposed on the deceased prior to his death may be demanded from the legal representative and collected out of the estate. However, a legal representative is not liable to prosecution and offences under this Act.

Under wealth tax, no penalty can be levied on legal representative for default of the deceased assessee as provisions of section 18 of Wealth tax Act, 1957, relating to penalty, are outside the ambit of section 19 dealing with liability to assessment in special cases. [CIT vs. H.S. Chauhan (2000) 245 ITR 704 (Del)].

20.1.3. Executors [Section 168]

Section 168 applies to a case where succession is a testamentary succession i.e. by will. However, in the case of intestate succession, i.e. where there is no will, section 168 will have no application.

As per Explanation to section 168 "executor" includes an administrator or other person administering the estate of a deceased person.

An executor is a person who is appointed by the testator to carry out and execute his wishes and for that purpose, to administer his estate after his death. An administrator is a person who is not appointed by the testator, but who is granted letters of administration by a court to the administrator the estate. The capacity of the executors to represent the estate is derived under the will from the date of death and does not depend on whether he has obtained probate or not.

Executors and administrators are charged under this section, not as representative assessees, but in their own right as persons in whom the estate of the deceased vests until it is completely administered. Where the administration of the estate is not complete, the assessment has to be made on the executors.

The income chargeable in the hands of the executor or administrator is the income of the period commencing from the date of the death of the deceased. Any income in respect of any period prior to that date should be assessed in the hands of the legal representatives under section 159. So, there would be two assessments in respect of the accounting year of death:

(i) one for the period commencing from the first day of the accounting year and ending with the date of death (in the hands of the legal representative), and

(ii) the other commencing from the date of death, and ending with the last day of the accounting year (in the hands of the executor or administrator).

Whereas against the legal representative, there would be an assessment qua legal representative only for one year, namely, the assessment year corresponding to the accounting year of death, against the executor or administrator, there would be yearly assessments commencing from the assessment year corresponding to the accounting year of death, and lasting upto the year till the administration of the estate is completed.

Thus, if the accounting year of the deceased is the financial year and the deceased died, say, on 06.06.2013, the first assessment year applicable to the executor or administrator would be assessment year 2014-15. In that assessment, all income that accrued or arose or was received by the executor or administrator commencing from 06.06.2013 and ending with 31.03.2014 would be included in the total income. In respect of income which accrued or arose or received by the executor or administrator during the accounting year 1.4.2014 to 31.3.2015, assessment would have to be made on the executor or administrator in the assessment year 2015-16, and so on. This procedure would have to be observed till the date of complete distribution to the beneficiaries of the estate according to their several interests.

The words "according to their several" qualify the immediately preceding words complete distribution to the beneficiaries; they should not be understood as requiring separate assessments on the executors in respect of the respective shares of the several beneficiaries.

According to Section 168(1), the income of the estate of a deceased person shall be chargeable to tax in the hands of the executor:

(i) If there is only one executor as if the executor were an individual

(ii) If there are more executors than one as if the executors were an Association of Persons

The executor shall be deemed to be resident or nonresident according as the deceased person was a resident/non-resident during the previous year in which the death took place.

The assessment of a person qua legal representative or qua executor or administrator is different from the assessment of these individuals in their personal or private capacity. Sub-section (2) of section 168 provides that their personal or private incomes shall have to be assessed separately and ought not to be included in their representative assessments, as made clear by this sub-section.

Sub-section (4) of section 168 provides that in calculating the total income of any accounting year, the executor is entitled to deduct any specific legacy distributed to or applied to the benefit of a specific legatee. This legacy shall be included in the total income of the specific legatee in the year of receipt.

In computing the income from the estate, the executor is not entitled to deduct probate duty or any other expenses directed to be incurred under the will of deceased. All payments are made out of the income of the estate coming into the hands of the executor and such payments, though directed to be made by the testator, cannot be said to have been diverted away from the hands of the executor by any overriding title. The executor stands in the shoes of the testator and the entire income belongs to the estate; and he would not be entitled to any deductions which the deceased himself would not have been entitled to claim, had he been alive. Also he cannot an executor seek to deduct any sums that he might have paid by way of death duties on the ground that the same had to be paid in order to enable him to carry on the testators business in those countries.

Section 169 provides the right of executor to recover tax paid. The provisions of section 162 shall, so far as may be, apply in the case of an executor in respect of tax paid or payable by him as they apply in the case of a representative assessee i.e. the executor will be able to recover such tax from the estate or from the persons on whose behalf it is paid.

Case Laws:

(1) Where a person leaves a will, the estate of the deceased would rest in the executor, who would be assessable under section 168, so that there is no scope for application of the clubbing provision under section 64(1)(iii) [Now substituted by section 64(1A) for aggregation of the minor's income]. [CIT vs. Abdulgafur A. Mistry (2007)292 ITR 515(Guj)].

(2) The Supreme Court in the case of ITO (First Addl) vs. Suseela Sadanandan & Another (1965) 57 ITR 168 (SC) held that if a person dies executing a will appointing more than one executor or dies intestate leaving behind him more than one heir, the ITO shall proceed to assess the total income of deceased against all the executors or the legal representatives, as the case may be.

(3) A single assessment is to be made under section 168 in respect of the income of the entire estate of the deceased even if he has made separate wills appointing different executors in respect of different properties. [H.H. Maharani Vijaya Kunverba Saheb vs. CIT (1983) 136 ITR 18(Guj)].

(4) The Bombay High Court in CIT vs. Usha D Shah (1981) 127 ITR 850 (Bom) held that the effect of section 168 is that it is made obligatory that the estate of a deceased person is charged to tax in the hands of an executor. The provision does not seem to leave any discretion to the Income-tax Authorities in this matter.

20.1.4. Liabilities of a representative assessee as regards the income in respect of which he is a representative assessee of another person [Section 160 to 167]

Assessment on the legal representative or other person administering the estate of a deceased person is dealt with sections 159 and 168. However, legal representative is not a representative assessee within the meaning of this Act.

Where on behalf of or for benefit of another, income is legally receivable by a person, the assessment and collection of tax thereon may present some problems. For ensuring the smooth furnishing of machinery for assessment and collection of tax in such cases, specific provisions have been made in Income-tax Act for assessment and collection of tax from person (i.e. representative assessee) receiving such income.

Income of an assessee is taxable in the hands of a representative assessee either because the assessee is —

(a) not competent to contract (say a minor or lunatic); or

(b) not present in India (say a non-resident);

(c) an artificial person and thus has to be represented by some human being.

A "Representative Assessee" means—

(i) In respect of the income of a non-resident specified in section 9(1) (i.e. income deemed to accrue or arise in India) — the agent of the non-resident, including a person who is treated as an agent under section 163.

(ii) In respect of the income of a minor, lunatic or idiot — the guardian or manager who is entitled to receive or is in receipt of such income on behalf of such minor, lunatic or idiot.

(iii) If the Court of Wards/Administrator General/Official Trustee/receiver or manager etc., is appointed by or under any order of a court to receive any income on behalf of some other person — the representative assessee shall be such Court of Wards/Administrator General/ Official Trustee/receiver or manager, etc.

(iv) In respect of any income under a trust declared by a duly executed instrument in writing, whether testamentary or otherwise (including Wakf deed) for the benefit of any person — the trustee or trustees so appointed who receive or are entitled to receive any income on behalf of the beneficiary.

(v) in respect of income which a trustee appointed under an oral trust receives or is entitled to receive for the benefit of any person — the trustee or trustees so appointed.

A representative assessee shall be deemed to be an assessee for the purpose of this Act.

Besides the legal representatives mentioned above, there are certain cases, where the income received by one person can be assessed in the hands of another. The person who is liable to be assessed on behalf of other because of their association with the real recipient of the income is known as representative assessee.

Every representative assessee, as regards the income in respect of which he is a representative assessee, shall be subject to the same duties, responsibilities and liabilities as if the income were income received by him, or accruing to him, or in favour of him beneficially, and shall be liable to assessment in his own name in respect of that income; but any such assessment shall be deemed to be made upon him in his representative capacity only, and the tax shall, subject to the other provisions, be levied upon and recovered from him in like manner and to the same extent as it would be leviable upon and recoverable from the person represented by him. Analysis of the above reveals that —

(i) The income of the representative assessee as such should be kept distinct from such income as he may have in his individual capacity except where he is also a beneficiary. These cannot be clubbed together merely because the person being assessed is the same.

(ii) Status to be assigned to representative assessee is the same as that of beneficiary or beneficiaries.

(iii) If there is only one representative assessee, the income will be computed in the same manner as it would have been computed in the hands of the beneficiary and the deduction/exemption and all other relief that the person represented may be entitled to claim shall be allowed to the representative assessee. On the other hand, if there are more than one representative assessee, each has to be assessed in respect of the income he is entitled to receive. These representative assessees would also be entitled to claim deduction, exemption and all other reliefs that the person represented would be entitled to.

(iv) Where there are more than one beneficiary of a private trust and the share falling to each of the beneficiary are determinate, the assessments are to be made on the trustee(s) as a representative assessee u/s 161. Such assessment will have to be made at the rate applicable to the total income of each beneficiary. Accordingly, separate assessment for each of the beneficiary on whose behalf the income is received by the trustee will have to be made. However as per section 166, the Income-tax Department has an option to make direct assessment in the hands of each beneficiary entitled to the income.

(v) Tax liability of representative assessee cannot exceed the sum total of the tax liabilities of each beneficiary separately computed.

(vi) If the several persons represented have each a trustee, each such trustee shall have to be assessed separately as a representative assessee in respect of individual interest of the respective person represented.

(vii) Though a representative assessee may be taxed only in respect of a part of the beneficiary income, the tax has to be charged at the rate applicable to the total income. The problems are occurred where there are more than one representative assessee. For the representative assessees, they may not be aware of the other income of the beneficiary and may be able to return only that part of the income which he is entitled to receive. So also, the officer will have to get an idea of the total income of the beneficiary on the basis of all the returns filed by the representative assessees or the beneficiary, if any, before he can complete any of the assessments and if the representative assessees and sources of income are scattered in several places, the difficulty created may be quite considerable.

Exceptions to the rule that the representative assessee is assessable only in like manner and to the same extent as the beneficiary

Where Trust income includes business income [Section 161(1A)]: If the trust income consists of or includes profits and gains of business, the tax shall be charged on the whole of the income in the hands of the representative assessee at the maximum marginal rate and not at the rate applicable to the beneficiary. However such maximum marginal rate will not be applicable where such profits and gains are receivable under a trust declared by any person under a will, exclusively for the benefit of any relative dependent upon him for support and maintenance and such trust is the only trust declared by him.

Where share of the beneficiaries are indeterminate or unknown [Section 164(1)]: In the case of a private discretionary trust, declared by a duly executed instrument in writing where the shares of the beneficiaries are unknown, trustee(s) is liable to tax as a representative assessee at the maximum marginal rate.

However, the maximum marginal rate of income tax will not apply in the following cases:

(i) Where none of the beneficiaries has any other income exceeding the exemption limit as applicable to an association of persons nor is he a beneficiary under any other private trust; or

(ii) Where the relevant income or part of the relevant income is receivable under a trust declared by any person by will and such trust is the only trust so declared by him; or

(iii) Where the trust, yielding the relevant income or part thereof was created by a non-testamentary instrument (before March 1970) bonaftde exclusively for the benefit of the relatives of the settlor, or where the settlor is Hindu Undivided Family, exclusively for the benefit of members of such family in circumstances where such relatives or members were mainly dependent on the settlor for their support and maintenance; or

(iv) Where the relevant income is receivable by the trustees on behalf of a provident fund, superannuation fund, gratuity fund, pension fund or any other fund created bona fide by a person carrying on a business or profession exclusively for the benefit of his employees.

If the case falls within any of the above four exceptions, the relevant income or part thereof is to be taxed at the rate applicable to an association of person.

From the assessment year 1985-86 and subsequent years, the exemption from maximum marginal rate of tax in the aforesaid cases will not apply in case where the income of a private discretionary trust [assessable in the hands of a trustee as representative assessee under section 160(1)(iv)] consists of, or includes profits and gains of business. In such cases the entire income of the trust would be charged at the maximum marginal rate of tax except in cases where the profits and gains are receivable under a trust declared by any person by will exclusively for the benefit of any relative dependent on him for support and maintenance and such trust is the only trust declared by him. In that case, the income of the discretionary trust would be charged to tax at normal rates applicable to an association of persons.

Where any person is, in respect of any income, assessable in the capacity of a representative assessee, he shall not, in respect of that income, be assessed under any other provision of this Act.

Case Laws:

It was held that even if the trust in question had to be regarded as a discretionary trust in as much as the profits had, during the relevant assessment years, been credited to the respective accounts of the beneficiaries, the income was to be assessed in the hands of the beneficiaries. [Moti Trust vs. CIT (1999) 236 ITR (SC)].

Taxability of income of the charitable or religious trust [Section 164(2)]: Such income of the charitable or religious trust which is not exempt under section 11 shall be assessable as income of an association of persons. However, if the whole or any part of the relevant income is not exempt under section 11 or 12 due to the following it shall be charged at the maximum marginal rate:

(i) if any part of the income of the charitable trust created or established after 1.4.1962 enures directly or indirectly for the benefit of any person referred to in section 13(3), or

(ii) if any part of such income or any property of the trust, which during the previous year is used or applied for any persons referred to in section 13(3), or

(iii) if funds of the trust are not invested in the mode specified under section 11(5).

Charge of tax in case of oral trust [Section 164A]: Where a trustee receives or is entitled to receive any income on behalf or for the benefit of any person under an oral trust, then, notwithstanding anything contained in any other provision of this Act, tax shall be charged on such income at the maximum marginal rate.

Where option to tax beneficiary instead of trustees is exercised [Section 166]: Although in the case of discretionary trust, trustees are the representative assessee, but according to Section 166 there can be a direct assessment of the person on whose behalf or for whose benefit the income is received by representative assessee.

The general principle is to charge all income only once. The Assessing Officer should keep this point in view at the time of making the initial assessment either of the trust or the beneficiary and adopt a course beneficial to the Revenue. Having exercised his option once it will not be open to the Assessing Officer to assess the same income for that assessment year in the hands of the other person. [Circular No. 157, dated 26.12.1974].

Further section 166 provides that even in a case where the assessment has been made on the representative assessee, the tax may be recovered from the person beneficially entitled to the income. [CIT vs. Trustees of Miss Gargiben Trust (No. 1) and Others (1981) 130 ITR 479 (Bom)].

Where right to receive income by the beneficiary is postponed, it does not mean that the trust cannot be assessed in respect of such income. The fact, that the beneficiaries were entitled to the income only after majority, does not mean that it would not be the income of the trust. Such income was being merely accumulated before disbursement. Since the income had already accrued and since the law provides for liability on the part of the representative assessee under section 161(1), an assessment is justified in the respective years of accrual. Such income is assessable in the hands of the trustee in the view that it is not that the beneficiary has no income during the year, but his right to the income stands postponed, so that it should be possible to assess the trust. [Ganesh Chhababhai Vallabhai Patel vs. CIT (2002) 258 ITR 193 (Guj)].

Right of representative assessee to recover tax paid [Section 162]: Every representative assessee who, as such, pays any sum under this Act, shall be entitled to recover the sum so paid from the person on whose behalf it is paid, or to retain out of any moneys that may be in his possession or may come to him in his representative capacity, an amount equal to the sum so paid.

Any representative assessee or any person who apprehends that he may be assessed as a representative assessee, may retain out of any money repayable by him to the person on whose behalf he is liable to pay tax (hereinafter referred to as the principal) a sum equal to his estimated liability under this Chapter and in the event of disagreement between the principal and such respective assessee such representative person may secure from the Assessing Officer a certificate stating the amount to be so retained pending final settlement of liability. The certificate shall be his warrant for retaining that amount.

The amount recoverable from such representative assessee or person at the time of final settlement shall not exceed the amount specified in such certificate, except to the extent to which such representative assessee or person may, at such time, have in his hands additional assets of the principal.

Cases where part of trust income is chargeable [Section 165]: Where part only of the income of a trust is chargeable under this Act, that proportion only of the income receivable by a beneficiary from the trust which the part so chargeable bears to the whole income of the trust shall be deemed to have been derived from that part.

Remedies against property in cases of representative assessees [Section 167]: The Assessing Officer shall have the same remedies against all property of any kind vested in or under the control or management of any representative assessee as he would have against the property of any person liable to pay any tax, and in as full and ample a manner, whether the demand is raised against the representative assessee or against the beneficiary direct.

Agent in relation to a non-resident [Section 163]

The person who may be regarded as an agent of non-resident in India may belong to one of the following five categories:

(i) One who is employed by or on behalf of the non-resident; or

(ii) One who has any business connection with the non-resident; or

(iii) One, from or through whom the non-resident is in receipt of any income, whether directly or indirectly; or

(iv) One who is the trustee of the non-resident; or

(v) One, whether a resident or non-resident, who has acquired by means of a transfer, a capital asset in India.

In the first four cases, it is further necessary that the person sought to be assessed as an agent should be in India.

It is the Assessing Officer who has jurisdiction to decide the question whether a particular person should be treated as an agent of the non-resident or not. Amongst these five categories of persons, the Assessing Officer should select the particular person who is connected with the particular income to be assessed as enumerated in section 9(1) and treat him as the agent of the non-resident for that particular income. The principle is that the person who helps the non-resident to make income in India should be saddled with the responsibility of payment of tax due by the non-resident in respect of that income. There is, of course, the added facility of easier assessment and collection of tax from the agent so treated, who is a person in India.

However, a broker in India who, in respect of any transactions, does not deal directly with or on behalf of a non-resident but deals with or through a non-resident broker shall not be deemed to be an agent under this section in respect of such transactions, subject to the fulfillment of following conditions, namely:—

(i) the transactions are carried on in the ordinary course of business through the first mentioned broker; and

(ii) the non-resident broker is carrying on such transactions in the ordinary course of his business and not as a principal.

Sub-section (2) of section 163 lays down that a person cannot be treated as the agent of a non-resident unless and until he has had an opportunity of being heard by the Assessing Officer as to his liability. Since an order under this section is appealable, a written order is essential.

Power of attorney does not answer the description of agent in relation to a non-resident, as envisaged under section 163(3)(1), hence, the assessment order framed in the case of NRI in the name of power of attorney treating as an agent held to be illegal and void. [CIT vs. Mukesh B. Shah (2010) 40 DTR 297 (Guj)].

Single transaction of purchase of shares by assessee from non-resident. Consideration remitted by assessee after deduction of tax at source. Assessee can be treated as an agent of non-resident, that assessee has deducted tax at source will not preclude liability to be treated as agent. [Utkal Investments Ltd vs. Astt. DIT (2010) 5 ITR (Trib) 481 (Mum)].

20.1.5. Succession to business otherwise than on death [Section 170]

Section 170 applies to cases of succession to a business profession or vocation and not cases of succession to any other income producing source.

Succession involves change of ownership; i.e. the transferor goes out and the transferee comes in. It connotes that the whole business is transferred; it also implies that substantially the identity and the continuity of the business are preserved.

The expression "succession" has acquired a somewhat artificial meaning. The Supreme Court, in CIT vs. Chambers (KH) (1965) 55 ITR 674 (SC), held that the tests of change of ownership, integrity, identity and continuity of business have to be satisfied before it can be said that a person "succeeded" to the business of another.

Succession and discontinuance: Where a person is carrying on a business or profession, such business or profession may come to an end so far as he is concerned in one of the following ways:

(i) It may come to end by the business changing hands by way of sale, gift or any other kind of transfer so that the business, considered an integral whole, continues to be carried on, though by a different person. That situation is called "succession" dealt with by the present section.

(ii) It may come to end in the manner that there is no succession but the business or profession as such ceases to be carried on by the assessee or anyone else. This is called discontinuance. In this case, a charge would arise on the person concerned at the Assessing Officers discretion under the provisions of, and in accordance with the procedure laid down in section 176. Should the Assessing Officer choose not to take action under section 176, the charge would be levied in the assessment year following the previous year of discontinuance. The consequence of a finding of discontinuance would also involve that any business which is found to be carried on by the successor after the discontinuance would be a fresh and new business.

Point no. (ii) eventuality is not provided for in section 170.

Assessment on predecessor & successor [Section 170(1)]: Where a person carrying on any business or profession (such person hereinafter referred to as the predecessor) has been succeeded therein by any other person (hereinafter to as the successor) who continues to carry on that business or profession,—

(a) the predecessor shall be assessed in respect of the income of the previous year in which the succession took place up to the date of succession (including any gain accruing from the transfer of business as a result of succession);

(b) the successor shall be assessed in respect of the income of the previous year after the date of succession.

The effect of this section is that the predecessor in business is assessable in respect of the income of the year of succession upto the date of succession, while the successor is assessable in respect of the income of that year after the date of succession. The predecessor and the successor would each be liable to tax at the rate applicable to each. The income of the predecessor and the successor must be computed separately and each must be granted the deduction and allowances appropriate to his case. The assessment on each must be separate and distinct. The successor is not allowed to carry forward and set off the losses incurred by his predecessor. He has also no right to carry forward the unabsorbed depreciation allowance of the years prior to his succession to the business.

Assessment when predecessor cannot be found [Section 170(2)]: Notwithstanding anything contained in sub-section (1), when the predecessor cannot be found, the assessment of—

(a) the income of the previous year in which the succession took place up to the date of succession, and

(b) the previous year preceding the year of succession

shall be made on the successor in like manner and to the same extent as it would have been made on the predecessor, and all the provisions of this Act shall, so far as may be, apply accordingly.

Tax of predecessor can be recovered from successor [Section 170(3)]: When any sum payable under this section in respect of the income of such business or profession for the previous year, in which the succession took place, up to the date of succession or for the previous year preceding that year, assessed on the predecessor, cannot be recovered from him, the Assessing Officer shall record a finding to that effect and the sum payable by the predecessor shall thereafter be payable by and recoverable from the successor, and the successor shall be entitled to recover from the predecessor any sum so paid by him.

T Ltd. is succeeded by H Ltd. on 25.09.2013 and the tax cannot be recovered from T Ltd.. In this case the tax relating to previous year 1.4.2013 to 25.09.2013 and the preceding previous year i.e. 2012-13 can only be recovered from the successor provided the Assessing Officer records a finding to that effect. However H Ltd. shall be entitled to recover such income-tax from T Ltd.

Recovery of tax of a HUF on succession thereto [Section 170(4)]: Where business of a Hindu Undivided Family is succeeded, and there is a partition in the family either simultaneously with the succession or sometime later, the tax due by the HUF in respect of its income from the business or profession succeeded to, up to the date of the succession, shall be recoverable from the members of the divided family in accordance with the proportions of the property allotted to them on partition. The liability of such members is joint and several. In respect of such taxes owing by the divided members, the liability of the successor under sub-section (2) and (3) of section 170 would continue. Consequently, if any of the divided members cannot be found or the tax levied upon any of the divided members cannot be recovered from them, the same can be recovered from the successor, subject to the restrictions and qualifications discussed above.

Income of Predecessor includes capital gains by virtue of succession: The explanation to section 170, states that any capital gain accruing to the transferor from the transfer which has resulted in the succession is treated as a category of the predecessors income to which this provision is applicable. One consequence is that, if the predecessor cannot be found, the successor would be liable to pay the tax on the sum of the capital gains.

Section 41(1) provides that where an allowance or deduction has been made in the assessment for any year in respect of loss, expenditure or trading liability incurred by the assessee (hereinafter referred to as the first mentioned person) and subsequently during any previous year, the successor in business has obtained, whether in cash or in any other manner whatsoever, any amount in respect of which loss or expenditure was incurred by the first-mentioned person or some benefit in respect of the trading liability by way of remission or cessation thereof, the amount obtained by the successor in business or the value of benefit accruing to the successor in business shall be deemed to be profits and gains of the business or profession, and accordingly chargeable to income-tax as the income of that previous year.

20.1.6. Charge of tax in case of AOP/BOI [Section 167B]

The tax liability of AOP/BOI shall be determined on the basis of the following:

(1) Charge of tax where share of members in AOP/BOI are unknown;

(2) Charge of tax where share of members are known.

(1) Charge of tax where share of members in AOP/BOI are unknown [Section 167B(1)]: Where the individual share of members of AOP/BOI are indeterminate or unknown, tax shall be charged on the Total Income of the AOP/BOI at the maximum marginal rate i.e. 30%. However, if the total income of any member of AOP/BOI is chargeable at a rate higher than 30%, the tax will be charged on the Total Income of the AOP/BOI also at such higher rale.

Thus, although the maximum tax rate in case of AOP is 30.9% (30% + education cess + SHEC) if the total income does not exceed ₹1 crore and 33.99% (30% + 10% surcharge + education cess + SHEC) if the total income exceeds ₹1 crore but in case a company happens to be a member of AOP/BOI, the rate of tax may be higher. In case of a foreign company which is a member of AOP/BOI, the tax rate will be 41.2% if total income of the foreign company does not exceed ₹1 crore. Where it exceeds ₹1 crore but does not exceed ₹10 crore it will be taxable @ 40% + 2% surcharge + education cess @ 2% + SHEC @ 1% and where it exceeds ₹10 crore, it will be taxable @ 40% + 5% surcharge + education cess @ 2% + SHEC @ 1%.

For the purposes of this section, the individual shares of the members of an association of persons or body of individuals in the whole or any part of the income of such association or body shall be deemed to be indeterminate or unknown, if such shares (in relation to the whole or any part of such income) are indeterminate or unknown on the date of formation of such association or body or at any time thereafter.

(2) Charge of tax where share of members are known [Section 167B(2)]:

(a) Where one of the members has total income exceeding maximum exemption limit: Where the total income of any member of AOP/BOI, without including his income from AOP/BOI exceeds the maximum amount which is not chargeable to tax, then AOP/BOI will be charged tax at maximum rate of 30% + 10% surcharge (in case total income exceeds ₹1 crore) + education cess + SHEC as applicable on its Total Income. However, in this case, if the total income of one or more member of AOP/BOI is chargeable at a rate more than 30%, tax shall be charged on that portion of income of AOP/BOI which is relatable to the share of such member at such higher rate and the balance of the income is taxable at the maximum marginal rate of tax.

(b) Where none of the members has total income exceeding maximum exemption limit:

(i) Where any member of AOP has total income exceeding neither maximum exemption limit nor any member is taxable at a rate more than maximum marginal rate, the AOP will pay income-tax on its total income at the rates which are applicable to individuals.

(ii) Where none of the member has total income exceeding the maximum exemption limit, but one or more member is liable to tax rate of more than the maximum limit (i.e. taxable at a rate higher than 30%), then on that portion of income of AOP which is relatable to that member, the tax rate applicable shall be rate of income-tax which is applicable to such member and the balance total income of AOP shall be charged at the maximum marginal rate.

20.1.7. Liability of partners of Limited Liability Partnership in liquidation [Section 167C) [Inserted by the Finance (No. 2) Act, w.e.f. Assessment Year 2010-11]

Notwithstanding anything contained in the Limited Liability Partnership Act, 2008, where any tax due from a Limited Liability Partnership in respect of any income of any previous year or from any other person in respect of any income of any previous year during which such other person was a Limited Liability Partnership cannot be recovered, in such case, every person who was a partner of the Limited Liability Partnership at any time during the relevant previous year, shall be jointly and severally liable for the payment of such tax unless he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the Limited Liability Partnership.

20.1.8. Liability of members after partition of Hindu Undivided Family [Section 171]

In case total partition took place during the previous year the total income of the joint family in respect of the period upto the date of partition shall be assessed as if so far no partition had taken place; and each member or group of members shall, in addition to any tax for which he or it may be separately liable and notwithstanding anything contained in Clause (2) of section 10, be jointly and severally liable for the tax on the income so assessed and in case total partition took place after the expiry of the previous year, the total income of the previous year of the joint family shall be assessed as if no partition had taken place; and each member or the group of members shall be jointly and severally liable for the tax on the income so assessed.

In case of partial partition taken place after the 31st December, 1978, the HUF shall continue to be liable to be assessed under this Act as if no such partial partition had taken place and each member or group of members of such HUF immediately before such partial partition and the HUF shall be jointly and severally liable for any tax, penalty, interest, fine or other sum payable under this Act by the HUF in respect of any period, whether before or after such partial partition. The several liability of any member or group of members aforesaid shall be computed according to the portion of the HUF property allotted to him or it at such partial partition.

Some doubt has been expressed on the proposition that where the individual coparcener getting his share on partition is entitled to be treated as Hindu Joint Family when he has wife and minor daughter. This issue need not have arisen at all after the decision of the Supreme Court in N. V. Narendranath vs. CWT (1969) 74 ITR 190 (SC) which had held that even asset received on partition would continue to have joint family character in the hands of each erstwhile coparcener, who had taken his share of the joint family property.

In CIT vs. Harshvadan Mangaldas (1992) 194 ITR 136 (Guj.) it was held, that the coparcener having a minor daughter on partition could be treated as holding property so acquired as joint family property. The Gujarat High Court has taken the same view in a later decision also CIT vs. Parmanandas Mahanlal (1994) 208 ITR 35 (Guj.). However, Andhra Pradesh High Court in Seth Tulsidas Bolumal vs. CIT (1988) 170 ITR 1 (AP) and Rajasthan High Court in Sohan Lal Kukar vs. CWT (1995) 211 ITR 1001 (Raj.) would take a contrary view holding that it would be individual property. Andhra Pradesh High Court in Ashok Kumar Ratanchand vs. CIT (1990) 186 ITR 475 (AP), however, had occasion to reconsider its earlier view and reviewed the earlier precedents exhaustively and came to the conclusion that the decision which it had taken earlier that it would continue to be individual property had overlooked the right or interest of a Hindu wife for maintenance as an obligation attaching to the property. In fact, such a view was taken even in the context of the facts of the case that assessee in this case was not married at the time of partition, so that both the issues as to the concept of "potential family" and the concept of a Hindu joint family with a single coparcener were not considered in this case.

In CIT vs. Harbhagwan (1999) 236 ITR 620 (P&H), the High Court dealt with a case, where a member threw his property purchased by him into the common hotchpotch of HUF only to partition the same shortly thereafter before the property was compulsorily acquired, so that the question of computing capital gains in respect of each member of the family entitled to a share in the property came up for consideration. It can be a matter of dispute because of the difficulty in determining the cost, which could be either: (i) the amount paid by the individual before he converted the same as joint family property; (ii) the market value as on the date of conversion; and (iii) nil value since HUF did not pay for it. There is scope for all the three views from the available judgments and interpretation. The High Court reviewed these possible views in this case and pointed out that Explanation-1 to sub-section (1) of section 49 required that where an asset is received on succession, inheritance or devolution or such other circumstances as prescribed therein, the cost will be that of the previous owner. It therefore did not approve the adoption of nil cost by the Bombay High Court in CIT vs. Kanubhai R. Shah (HUF) (1993) 201 ITR 1050 (Bom) but held, that cost to individual should be taken, so that what it adopted was the cost of the predecessor's predecessor on the inference that both the devolutions in law should be ignored both for period of holding under section 2(42A) of the Act and for ascertaining the relevant date for cost.

The decisions do raise a controversial legal issue, which may have to be resolved by the Supreme Court because of conflicting decisions. It is clear that conversion of individual property to joint family property and partition should be treated as passing of property on devolution under the Hindu Law as well as Tax Law. Incidentally, in respect of shares it should be taken as transmission and not transfer within the meaning of Company Law on the same logic.

When co-sharers hold property of the deceased as tenants in common liability for capital gains can arise only on each co-sharer separately and not in the hands of the HUF.

20.1.9. Discontinued Business [Section 176]

The cessation of the business of the assessee may occur in 2 ways —

(a) Where the business is no longer in existence i.e. there is complete closing down of the business or profession and a cessor of all the operations immediately. This would amount to "discontinuance" used in that context under this section.

(b) Where the business is in existence but has been transferred by the assessee as a going concern to another entity. In this case, there is a mere change in the ownership or change in the constitution of firm. A change in ownership may amount to succession and this does not mean the discontinuance of the business. Similarly, there is no discontinuance when a partner of a firm ceases to be a partner.

As succession and discontinuance are two mutually exclusive concepts there cannot be a discontinuance in cases where there is a succession. Further, if a part of the business of an assessee is dropped owing to non-profitable nature, either permanently or temporarily it will not imply that the business has been discontinued.

In the case of dissolutions of a firm or the liquidation of a company, sometimes the trade may be carried on even after such dissolution or liquidation.

Other cases of discontinuance of business are as follows:

(a) Amalgamation of two separate and independent businesses belonging to distinct owners may result in the discontinuance of those businesses.

(b) Partition of a joint family business and the business is divided amongst the members. In this case, there will be a discontinuance of the old business even if some or all the members carry on their business in the same premises and take the advantage of the old business connections.

(c) In case a firm is split up into two different firms and the old business is also divided amongst the different firms, the original firm shall be deemed to have discontinued. [Sait Nagjiu Purushotam and Co. vs. CIT (1969) 51 ITR 849 (SC)].

(d) If a professional person ceases to excise his profession a vocation then there would be a discontinuance. The question whether a professional person discontinued his profession depends upon the state of his mind at the time of cessation. Merely because he takes to the profession once again it cannot be said that there is no discontinuance at the time of cessation.

Section 176(1) provides that notwithstanding anything contained in section 4, where any business or profession is discontinued in any assessment year, the income of the period from the expiry of the previous year for that assessment year up to the date of such discontinuance may at the discretion of the Assessing Officer be charged to tax in that assessment year, that is to say, the pace of assessment may be accelerated. Now this period may cover either a fraction of an accounting year (a broken period, to coin a phrase) or completed accounting year plus a broken period. Thus if the accounting year of an assessee be the financial year and the business is discontinued on, say, the 29.10.2013, i.e., during the assessment year 2014-15, the income of the period between the 1.4.2013 and 29.10.2013 will be income of a broken period. The income of the period contemplated by sub-section (1) of section 176 is that of the entire period between 1.4.2012 to 29.10.2013 being the date of discontinuance. This, as would be seen, includes a completed accounting-year commencing from 1.4.2012 and ending with 31.3.2013 and in addition a broken period being 1.4.2013 to 29.10.2013.

Section 176(2) states as to how the incomes of these two periods should be dealt with. According to this sub-section separate assessments shall be made, one with reference to the income of the completed accounting year, and another with reference to the total income of the broken period. Applying the aforesaid principles to the above example, there shall have to be two separate computations of income for the two periods, viz., 1.4.2012 to 31.3.2013 and 1.4.2013 to 29.10.2013. Further such separate income shall be chargeable to tax at the rate or rates in force in that assessment year.

In order to enable the Assessing Officer to make the accelerated assessment, sub-section (3) provides that the assessee discontinuing the business or profession should give to the Assessing Officer notice of the discontinuance within 15 days thereof.

Sub-section (3A) of section 176 provides that where any business is discontinued in any year, any sum received after the discontinuance shall be deemed to be the income of the recipient and charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the person who carried on the business had such sum been received before such discontinuance.

Sub-section (4) of section 176 provides that where any profession is discontinued in any year on account of the cessation of the profession by, or the retirement or death of, the person carrying on the profession, any sum received after the discontinuance shall be deemed to be the income of the recipient and charged to tax accordingly in the year of receipt, if such sum would have been included in the total income of the aforesaid person had it been received before such discontinuance. However, section 176(4) applies only to a profession and not to a business discontinued.

Fees earned by a professional person which are collected after his death by the executor are part of the estate and not the income of the estate within section 168, therefore such fees cannot be taxed in the hands of the executor under section 168 or be clubbed with the income of the estate, but the executor may be separately taxed in respect of such fees as the recipient thereof within section 176(4). [CIT vs. Estate of Late A.V. Viswanatha Sastri (1980) 121 ITR 270 (Mad)].

Sub-section (5) of this section enacts that the Assessing Officer may, where he decides to complete an accelerated assessment, serve, on the person whose income is to be assessed, or in the case of a firm, on any of its partners at the time of its discontinuance, or in the case of a company, on the principal officer thereof, a notice calling for the return of the income of the assessee for the completed previous year and/or broken period.

The above procedure in relation to charge of income for a completed previous year or for a broken period is left to the discretion of the Assessing Officer. If the Assessing Officer opts to take action under this section, the sum of the tax would be ascertained and levied under this section. If he does not so opt, the assessment will be made in the normal course under section 4, when the relevant assessment year arrives. The above procedure applies where an assessee has several kinds of business or profession and he discontinues one or more of them and not all. The accelerated assessment would then apply only to the particular business or businesses or profession or professions discontinued.

Sub-section (6) of this section clarifies that the tax chargeable under this section shall be in addition to the tax, if any, chargeable under any other provisions of this Act.

Sub-section (7) of section 176 provides that where the Assessing Officer proceeds to assess the income of the completed previous year and/or the broken period in the year of discontinuance itself, any notice that he issues to the assessee calling for a return either for a regular assessment, or for an escaped assessment or for representative assessment on the assessee, need not grant the normal time of thirty days from the date of service, as specified in section 142(1)(i) or 148, but, it can fix a shorter time of seven days or more as the Assessing Officer may think proper.

20.1.10. Liability of an Association dissolved or business discontinued [Section 177]

This section covers discontinuance of the business of AOP as well as dissolution of AOP.

Where any business or profession carried on by an association of persons has been discontinued or is dissolved, the Assessing Officer shall make an assessment of the total income of the association of persons as if no such discontinuance or dissolution had taken place, and all the provisions of this Act, including the provisions relating to the levy of a penalty or any other sum chargeable under any provision of this Act shall apply, so far as may be, to such assessment.

Without prejudice to the generality of the above provisions, if the Assessing Officer or the Commissioner (Appeals) in the course of any proceedings under this Act in respect of such association of persons is satisfied that the AOP was guilty of any acts specified in Chapter XXI (relating to penalty), he may impose or direct the imposition of a penalty in accordance to provisions of that Chapter.

Every person who was at the time of such discontinuance or dissolution a member of the association of persons, and the legal representative of any such person who is deceased, shall be jointly and severally liable for the amount of tax, penalty or other sum payable, and all the provisions of this Act, so far as may be, shall apply to any such assessment or imposition of penalty or other sum.

Where such discontinuance or dissolution takes place after any proceedings in respect of an assessment year have commenced, the proceedings may be continued against the persons referred above from the stage at which the proceedings stood at the time of such discontinuance or dissolution, and all the provisions of this Act shall, so far as may be, apply accordingly.

A society registered under the Societies Registration Act is a legal entity. Its members are not personally liable for the tax levied on the society as an association of persons, so long as the society is not dissolved and its business is not discontinued. [Swami Satchitanand and Others vs. Second Addl. ITO (1964) 53 ITR 533 (Ker)].

20.1.11. Liability of liquidator/receiver of a company in liquidation [Section 178]

A company in liquidation is still a Company within the meaning of the charging provisions of the Act and the liquidator/receiver is merely an agent of the Company to administer the property of the company for purpose prescribed by the statute. Thus the liquidator/receiver (hereinafter called as liquidator) would have to act in regard to the submission of the return, etc. after the company goes into liquidation, whether under the orders of a court or otherwise.

According to Section 178(1) of the Income-tax Act 1961 provides that it is a duty of the liquidator/receiver to give notice of his appointment to the Assessing Officer who is entitled to assess the income of the company within 30 days of his appointment.

According to section 178(2) the Assessing Officer shall, after making such enquiries or calling for such information as he may deem fit, notify to the liquidator within three months from the date on which he receives notice of the appointment of the liquidator the amount which, in the opinion of the Assessing Officer, would be sufficient to provide for any tax which is then, or is likely thereafter to become, payable by the company.

According to section 178(3) the liquidator—

(a) shall not, without the leave of the Chief Commissioner or Commissioner, part with any of the assets of the company or the properties in his hands until he has been notified by the Assessing Officer under sub-section (2); and

(b) on being so notified, shall set aside an amount equal to the amount notified and, until he so sets aside such amount, shall not part with any of the assets of the company or the properties in his hands.

Provided nothing contained in this sub-section shall debar the liquidator from parting with such assets or properties for the purpose of the payment of the tax payable by the company or for making any payment to secured creditors whose debts are entitled under law to priority of payment over debts due to Government on the date of liquidation or for meeting such costs and expenses of the winding up of the company as are in the opinion of the Chief Commissioner or Commissioner reasonable.

According to section 178(4) if the liquidator fails to give the notice in accordance with section 178(1) or fails to set aside the amount as required by section 178(3) or parts with any of the assets of the company or the properties in his hands in contravention of the provisions of that subsection, he shall be personally liable for the payment of the tax which the company would be liable to pay.

Provided if the amount of any tax payable by the company is notified under sub-section (2), the personal liability of the liquidator under this sub-section shall be to the extent of such amount.

Where there are more than one liquidator, the obligations and liabilities attached to the liquidator under this section shall attach to all the liquidators jointly and severally.

The provisions of this section shall have effect notwithstanding anything to the contrary contained in any other law for the time being in force.

Case Law

The scope of section 327 of the Companies Act, 2013, is different from that of section 178 of the Income-tax Act. Under section 327 of the Companies Act, all taxes which have "become due and payable" alone are entitled to preferential payment. The amount should have crystallised into a liability. Under section 178(2) read with section 178(3) of the Income-tax Act, provision should be made for any tax which is then or is likely thereafter to become payable. Even the amounts which have not crystallised into a liability, but which are "likely to become due thereafter" should be taken note of. Moreover, there is a non-obstante clause in section 178(6). On a total view of the relevant statutory provisions, the Income-tax Department is treated as a "secured creditor" [Imperial Chit Funds (P) Lid. vs. ITO (1996) 219 ITR 498 (SC)].

20.1.12. Liability of directors of private company in liquidation [Section 179]

Notwithstanding anything contained in the Companies Act, 2013 where any tax due from a private company in respect of any income of any previous year or from any other company in respect of any income of any previous year during which such other company was a private company cannot be recovered, then, every person who was a director of the private company at any time during the relevant previous year shall be jointly and severally liable for the payment of such tax unless he proves that the non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part in relation to the affairs of the company.

As per section 179 of the Income-tax Act, 1961, every person who was a director of the private company during the relevant year can be made jointly and severally liable to pay the arrears of tax provided the Income-tax Department is unable to realise the arrears from the company. In the absence of any reasons recorded by the Assessing Officer to the effect that the arrears could not be recovered from the company, recovery cannot be made from the directors. [Dipak Dutta vs. Union of India (2004) 268 ITR 302 (Cal). Also see Indu Bhai T. Vasa (HUF) vs. ITO (2006) 282 ITR 120 (Guj)].

Section 179 allows recovery of tax due from a company from the director only when revenue is able to establish that it had taken appropriate step for recovery from the company as the expression used in section 179 is that tax cannot be recovered from the company. Where the revenue has failed to establish the same, the proceedings u/s 179 would not be valid. [Amit Suresh Bhatnagar vs. ITO (2009) 308 ITR 113 (Guj)].

For invoking section 179 it is not necessary that all three ingredients, viz, gross neglect, misfeasance and breach of duty are satisfied; it is sufficient if it is held that there is a gross neglect or misfeasance or breach of duty on part of directors in relation to affairs of company. Thus where a company did not file its return of income for more than 10 year and was not in a position to pay tax demanded, it could be said that there was a gross neglect on part of directors of company and, hence, all ingredients of section 179 were satisfied. [H. Ebrahim vs. DCIT (2009) 185 Taxman 11 (Kar)].

The phrase 'tax' as contemplated under section 179 does not include penalty and interest in so far as directors of company are concerned. [H. Ebrahim vs. DCIT (2009) 185 Taxman 185 (Kar)].

For the purposes of section 179 "Tax" does not include penalty, therefore, directors of the company cannot be called upon to pay penalty of the company under section 179. Order passed by the Assessing Officer under section 179 without examining the question as to whether the non recovery of tax from the assessee company was or not a result of gross neglect, misfeasance or breach of duty on the part of the assessee in relation to affairs of the company, Assessing Officer was directed to pass fresh order after giving a reasonable opportunity to the assessee. [Dineslt T. Tailor vs. Tax Recovery Officer (2010) 326 ITR 85/41 DTR 6/192 Taxman 152 (Bom)]

While deciding, if the nomenclature 'tax' would include other components such as penalty as well as interest, the High Court placed reliance on the judgment in the case of Soma Sundarams Ltd. vs. CIT 116 ITR 620, which had held that the Court has decidedly stated that the component 'income tax' does not include payment of penalty as well as interest. [H. Ebrahim and Others vs. DCIT (2011) 332 ITR 122 (Karn)].

Study Note - 21

WEALTH TAX

Levy of Wealth Tax under the Wealth Tax Act has been abolished with effect from the Assessment Year 2016-2017

Study Note - 22

TAXATION OF INTERNATIONAL TRANSACTIONS

This Study Note includes

22. 1 INTERNATIONAL TAXATION AND TRANSFER PRICING – INTRODUCTION

The source rule/statutory provision relating to levy and collection of tax liability on international transactions or specified domestic transactions is empowered through Sec.92 to 92F of the Income Tax Act, 1961. These provisions were inserted by the Finance Act, 1976. With the opening up of global economy, apart from goods, there has been transfer or transaction relating to rendering of services cross-border. There is a magnanimous increase in the volume of cross-border transactions, which calls for attracting the provisions of Indirect Taxes in India. There arises the necessity and therefore leads to computation of reasonable, fair and equitable profit and tax in India are not being eroded of Indian tax revenue. Any income arising from an international transaction or specified domestic transactions shall have to be computed having regard to arm's length price.

22.2 INTERNATIONAL TRANSACTION

As per Sec. 92B of the Income Tax Act, 1961

(1) For the purposes of this section and sections 92, 92C, 92D and 92E, "international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises.

(2) A transaction entered into by an enterprise with a person other than an associated enterprise shall, for the purposes of sub-section (1), be deemed to be an international transaction entered into between two associated enterprises, if there exists a prior agreement in relation to the relevant transaction between such other person and the associated enterprise, or the terms of the relevant transaction where the enterprise or the associated enterprise or both of them are non-residents irrespective of whether such other person is a non-resident or not.

Meaning and scope of international transaction widened [Explanation to section 92B] [W.r.e.f. A.Y. 2002-03] [Inserted by Finance Act, 2012]

An Explanation has been inserted in section 92B to clarify the expression "international transaction" and "intangible property".

The expression "international transaction" shall include-

(a) the purchase, sale, transfer, lease or use of tangible property including building, transportation vehicle, machinery, equipment, tools, plant, furniture, commodity or any other article, product or thing;

(b) the purchase, sale, transfer, lease or use of intangible property, including the transfer of ownership or the provision of use of rights regarding land use, copyrights, patents trademarks, licences, franchises, customer list, marketing channel, brand, commercial secret, know-how, industrial property right, exterior design or practical and new design or any other business or commercial rights of similar nature;

(c) capital financing, including any type of long-term or short-term borrowing, lending or guarantee, purchase or sale of marketable securities or any type of advance, payments or deferred payment or receivable or any other debt arising during the course of business;

(d) provision of services, including provision of market research, market development, marketing management, administration, technical service, repairs, design, consultation, agency, scientific research, legal or accounting service;

(e) a transaction of business restructuring or reorganisation, entered into by an enterprise with an associated enterprise, irrespective of the f act that it has bearing on the profit, income, losses or assets of such enterprises at the time of the transaction or at any future date;

The expression "intangible property" shall include-

(a) marketing related intangible assets, such as, trademarks, trade names, brand names, logos;

(b) technology related intangible assets, such as, process patents, patent applications, technical documentation such as laboratory notebooks, technical know-how;

(c) artistic related intangible assets, such as, literary works and copyrights, musical compositions, copyrights, maps, engravings;

(d) data processing related intangible assets, such as, proprietary computer software, software copyrights, automated databases, and integrated circuit masks and masters;

(e) engineering related intangible assets, such as, industrial design, product patents, trade secrets, engineering drawing and schematics, blueprints, proprietary documentation;

(f) customer related intangible assets, such as, customer lists, customer contracts, customer relationship, open purchase orders;

(g) contract related intangible assets, such as, favourable supplier, contracts, licence agreements, franchise agreements, non-compete agreements:

(h) human capital related intangible assets, such as, trained and organised work force, employment agreements, union contracts;

(i) location related intangible assets, such as, leasehold interest, mineral exploitation rights, easements, air rights, water rights;

(j) goodwill related intangible assets, such as, institutional goodwill, professional practice goodwill, personal goodwill or professional, celebrity goodwill, general business going concern value;

(k) methods, programmes, systems, procedures, campaigns, surveys, studies, forecasts, estimates, customer lists, or technical data;

(l) any other similar item that derives its value from its intellectual content rather than its physical attributes.

Meaning of Specified Domestic Transaction [Sec 92BA]

For the purposes of this section and sections 92, 92C, 92D and 92E, "specified domestic transaction" in case of an assessee means any of the following transactions, not being an international transaction, namely:

(i) any expenditure in respect of which payment has been made or is to be made to a person referred to in clause (b) of sub-section (2) of section 40A;

(ii) any transaction referred to in section 80A;

(iii) any transfer of goods or services referred to in sub-section (8) of section 80-IA;

(iv) any business transacted between the assessee and other person as referred to in sub-section (10) of section 80-IA;

(v) any transaction, referred to in any other section under Chapter VI-A or section 10AA, to which provisions of sub-section (8) or sub-section (10) of section 80-IA are applicable; or

(vi) any other transaction as may be prescribed,

and where the aggregate of such transactions entered into by the assessee in the previous year exceeds a sum of ₹ 5 crore upto 31.3.2016 or ₹ 20 crore w.e.f. 1.4.2016 onwards.

With the insertion of section 92BA for such specified domestic transactions, the following sections, which are applicable to international transactions, have also been made applicable to such specified domestic transaction.

22.3 ARM'S LENGTH PRINCIPLE

The arm's length principle seeks to ensure that transfer prices between members of an MNE ("controlled transactions"), which are the effect of special relationships between the enterprises, are either eliminated or reduced to a large extent. It requires that, for tax purposes, the transfer prices of controlled transactions should be similar to those of comparable transactions between independent parties in comparable circumstances ("uncontrolled transactions"). In other words, the arm's length principle is based on the concept that prices in uncontrolled transactions are determined by market forces and, therefore, these are, by definition, at arm's length. In practice, the "arm's-length price" is also called "market price". Consequently, it provides a benchmark against which the controlled transaction can be compared.

The Arm's Length Principle is currently the most widely accepted guiding principle in arriving at an acceptable transfer price. As circulated in 1995 OECD guidelines, it requires that a transaction between two related parties is priced just as it would have been if they were unrelated. The need for such a condition arises from the premise that intra-group transactions are not governed by the market forces like those between two unrelated entities. The principle simply attempts to place uncontrolled and controlled transactions on an equal footing.

22.2.1 Why Arm's Length Pricing?

The basic object of determining Arm's Length Price is to find out whether any addition to income is warranted or not, if the following situations arises:

(a) Selling Price of the Goods < Arm's Length Price

(b) Purchase Price > Arm's Length Price

Total Income as disclosed by an Assessee	XXXX
Add: Understatement of profit due to overstatement of purchase price	XXX
Add: Understatement of profit due to understatement of selling price	XXX
Total Income after Assessment	XXXX

22.2.2 Role of market forces in determining the "Arm's Length Price"

In case of transactions between Independent enterprises, the conditions of their commercial and financial relations (eg. The price of goods transferred or services provided and the conditions of the transfer or provision) are, ordinarily, determined by the market force.

Whereas,

In case of transactions between MNEs (Multinational Enterprises), their commercial and financial relations may not be affected by the external forces in the same way, although associated enterprises often seek to replicate the dynamics of the market forces in their dealings with each other.

22.2.3 Difficulties in applying the arm's length principle

The arm's length principle, although survives upon the international consensus, does not necessarily mean that it is perfect. There are difficulties in applying this principle in a number of situations.

(a) The most serious problem is the need to find transactions between independent parties which can be said to be exact compared to the controlled transaction.

(b) It is important to appreciate that in an MNE system, a group first identifies the goal and then goes on to create the associated enterprise and finally, the transactions entered into. This procedure obviously does not apply to independent enterprises. Due to these facts, there may be transactions within an MNE group which may not be between independent enterprises.

(c) Further, the reductionist approach of splitting an MNE group into its component parts before evaluating transfer pricing may mean that the benefits of economies of scale, or integration between the parties, is not appropriately allocated between the MNE group.

(d) The application of the arm's length principle also imposes a burden on business, as it may require the MNE to do things that it would otherwise not do (i.e. searching for comparable transactions, documenting transactions in detail, etc).

(e) Arm's length principle involves a lot of cost to the group.

22.4 TRANSFER PRICING – CLASSIFICATION OF METHODS

In order to ensure that a transfer price meets the arm's length standard, the OECD (Organization for Economic Co-operation and Development) guidelines have indicated five transfer pricing methods that can be used. These methods fall in two categories:

(1) Traditional Transaction Methods;

(2) Transactional Profit Methods.

As per Sec.92C of the Income Tax Act, 1961, the methods for determining Arm's Length Price may be represented as under:

(1) Comparable Uncontrolled Price Method,

(2) Resale Price Method,

(3) Cost plus Method,

(4) Profit Split Method,

(5) Transactional Net Margin Method,

(6) Such other method as may be prescribed by the Board.

TRANSACTION BASED METHODS

COMPARABLE UNCONTROLLED PRICE METHOD
RESALE PRICE METHOD
COST PLUS METHOD

PROFIT BASED METHODS

PROFIT SPLIT METHOD
TRANSACTION NET MARGIN METHOD

Amendment made by the Finance (No. 2) Act, 2014 [Section 92C] [W.e.f. A.Y. 2015-16]

Section 92C(2) provides that the most appropriate method referred to in section 92C(1) shall be applied for determination of arm's length price in the manner as may be prescribed.

However, where more than one price is determined by the most appropriate method, the arm's length price shall be taken to be the arithmetical mean of such prices. [Proviso to section 92C(2)].

Further, if the variation between: (a) the arm's length price so determined, and (b) price at which international transaction has been actually undertaken, does not exceed such percentage not exceeding 3% of the latter (i.e. price at which international transaction has been actually undertaken) **as may be notified by the Central Government in the Official Gazette in this behalf**, then the price at which international transaction has actually been undertaken shall be deemed to be the arm's length price and no adjustment is required to be made. [Proviso 2 to section 92C(2)].

The following third proviso has been inserted in section 92C(2):

Provided also that where more than one price is determined by the most appropriate method, the arm's length price in relation to an international transaction or specified domestic transaction undertaken on or after 1-04-2014, shall be computed in such manner as may be prescribed and accordingly the first and second proviso shall not apply.

In other words, for any international transaction or specified domestic transaction undertaken on or after 01-04-2014, third proviso shall be applicable instead of proviso first and second.

22.5 STEPS IN THE PROCESS OF COMPUTING ARM'S LENGTH PRICE – TRANSFER PRICING (TP) STUDY

Transfer Pricing Study (TP Study) is the prime document which is used during transfer pricing assessment. The statement of particulars to be furnished in the Annexure to Form No.3CEB for the Income Tax Act, 1961 assessment, has thirteen clauses.

The following are the steps to be followed:-

Step 1	Selection of comparable companies
Step 2	Use of different filters
Step 3	Screening of comparables based on FAR
Step 4	Use of Power under Indirect Tax laws [special reference to Sec.133(6) of the Income Tax Act,1961]
Step 5	Adjustments
Step 6	5% Safe Harbour

The steps may be enumerated as follows:

Step 1: Selection of Comparable Companies

The first step for doing this study is to select comparable companies. This can be selected in the following four ways:-

(a) Industry-wise selection

(b) Product-wise selection

(c) NIC Code-wise selection

(d) Segment-wise selection

The data relating to the financial year in which the international transaction or specified domestic transactions has been entered into must be used in analyzing the comparability of an uncontrolled transaction with an international transaction or specified domestic transactions.

Step 2: Use of different filters

Once there is a selection of comparable companies, the next step is to filter these companies with the use of quantitative and qualitative filters. The following filters are also used sometimes:

(a) Companies whose data is not available for the relevant year

(b) Companies for which sufficient financial data is not available to undertake analysis

(c) Different financial year filter

(d) Turnover filter

(e) Service Income filter

(f) Export filter

(g) Diminishing Loss filter

(h) Related party filter

(i) Companies that had exceptional year/(s) of operation

(j) Employee cost filter

(k) Onsite and offsite filter

(l) Fixed Asset filter

(m) Research & Development Expense filter

(n) Income Tax filter

Step 3: Screening of comparables based on FAR

Comparability of an international transaction or specified domestic transactions with an uncontrolled transaction shall have to be judged with relevance to the following factors:

(a) The specific characteristics of the property transferred or services provided in either transaction;

(b) FAR Analysis- the (F) functions performed, taking into account (A)assets employed or to be employed or the (R) risks assumed by the respective parties to the transactions;

(c) The contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions;

(d) Conditions prevailing in the markets in which the respective parties to the transactions operate, including the geographical location and size of the markets, overall economic development and level of competition and whether the markets are wholesale or retail.

There may arise situation, where it requires further analysis of the following factors:-

(i) Is there a public issue in the relevant year or previous year?

(ii) Are the entity's profits exempted from tax?

(iii) Is there any merger/de-merger, etc., during the relevant time?

(iv) Is the depreciation policy different?

(v) Is there a wide difference between various segments' profitability?

(vi) Is the area of operation, i.e. geography different?

(vii) Is the volume of operation different?

Step 4: Use of power under Indirect Tax Laws

This power is usually used by the Revenue Department/Authorities, with a special reference to Sec.133(6) of the Income Tax Act,1961. The authorities may exercise such powers for getting details which are generally not available in the annual reports of the companies. This power is used more in the earlier years.

Step 5: Adjustments

Based on specific characteristics of the property transferred or the services rendered in either transaction and the contractual terms (whether or not such terms are formal or in writing) of the transactions which lay down explicitly or implicitly how the responsibilities, risks and benefits are to be divided between the respective parties to the transactions. The following enterprise level and transaction level adjustments are suggested:

(a) Functional differences

(b) Asset differences

(c) Risk differences

(d) Geographical location

(e) Size of the market

(f) Wholesale or retail market

(g) The laws and governmental orders in force

(h) Cost of labour

(i) Cost of capital in the markets

(j) Overall economic development

(k) Level of competition

(l) Accounting practices

However, in practice the following adjustments are provided:

(i) Working capital adjustment

(ii) Risk adjustment

(iii) Volume/geographical/depreciation/idle capacity/first year operation, etc.

Step 6: Safe Harbour Rules

Power of Board to make Safe Harbour Rules [Section 92CB]

The determination of arm's length price under section 92C or section 92CA shall be subject to safe harbor rules.

Further as per section 92CB(2), the Board may, for the purposes of section 92CB(1), make rules for safe harbor.

Explanation.— For the purposes of this section, "safe harbour" means circumstances in which the income-tax authorities shall accept the transfer price declared by the assessee.

Safe hourbour rules for international transactions have since been notified by the CBDT by Notification No. 73/2013, dated 18-9-2013 which contain rules 10TA to 10TG.

Prescribing upper ceiling of 3% tolerance range for determination of Arm's Length Price [Section 92C(2)] [W.e.f. A.Y. 2013-14]

Section 92C (1) prescribes the methods of computation of Arm's Length Price (ALP). Section 92C(2) provides that if the appropriate method results in more than one price then the arithmetic mean of these prices would be the ALP. The proviso to section 92C(2) which was amended by Finance Act, 2011 provides that the Central Government may notify a percentage and if variation between the ALP so determined and the transaction price is within the notified percentage (of transaction price), no adjustment shall be made to the transaction price.

Therefore, second proviso to section 92C(2) of the Act has been amended, so as to provide an upper ceiling of 3% in respect of power of Central Government to notify the tolerance range for determination of arms length price.

Further Explanation to section 92C(2) provides that the second proviso to section 92C relating to variation between the arm's length price so determined by the arithmetical mean and price at which the international transaction has actually been undertaken shall also be applicable to all proceedings which were pending as on 01.10.2009. [The date of coming in force of second proviso inserted by Finance (No. 2) Act, 2009].

Tolerant variation between the arithmetic mean of ALP and actual transaction price [Section 92C(2A) and 2(B)] [W.r.e.f. A.Y. 2002-03]

Sub-section (2A) and (2B) have been inserted in section 92C to provide clarity with retrospective effect in respect of first proviso to section 92C(2) as it stood before its substitution by Finance Act (No.2), 2009.

As per section 92C(2A) where the first proviso to section 92C(2) as it stood before its amendment by the Finance 50 (No. 2) Act, 2009, is applicable in respect of an international transaction for an assessment year and the variation between the arithmetical mean referred to in the said proviso and the price at which such transaction has actually been undertaken exceeds 5% of the arithmetical mean, then, the assessee shall not be entitled to exercise the option as referred to in the said proviso.

As per section 92C(2B) nothing contained in section 92C(2A) shall empower the Assessing Officer either to assess or reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154 for any assessment year the proceedings of which have been completed before 1.10.2009.

22.6 TRANSFER PRICING ISSUES

In the content of International Transactions or specified domestic transactions and ascertainment of arm's length price, the following issues are surfaced. These needs to be further examined in the light of applicable statutory provisions of Indirect Tax laws in India.

22.6.1 Key current and emerging TP Audit issues in India

Indian transfer pricing administration over the past 10 years has witnessed several challenges in administration of transfer pricing law. In the above backdrop, this chapter highlights some of the emerging transfer pricing issues and difficulties in implementation of arm's length principle.

22.6.2 Key Issues for consideration

(a) Challenges in the comparability analysis - Increased market volatility and increased complexity in international transaction have thrown open serious challenges to comparability analysis and determination of arm's length price.

(b) Issue relating to risks - A comparison of functions performed, assets employed and risks assumed is basic to any comparability analysis. India believes that the risk of a MNE is a by-product of performance of functions and ownership, exploitation or use of assets employed over a period of time. Accordingly, risk is not an independent element but is similar in nature to functions and assets. In this context, India believes that it is unfair to give undue importance to risk in determination of arm's length price in comparison to functions performed and assets employed.

(c) Arm's length range - Application of most appropriate method may set up comparable data which may result in computation of more than one arm's length price. Where there may be more than one arm's length price, mean of such prices is considered. Indian transfer pricing regulations provide that in such a case the arithmetic mean of the prices should be adopted as arm's length price. If the variation between the arithmetic mean of uncontrolled prices and price of international transactions or specified domestic transactions does not exceed 3% or notified percentage of such transfer pricing, then transfer price will be considered to be at arm's length. In case transfer price crosses the tolerance limit, the adjustment is made from the central point determined on the basis of arithmetic mean. Indian transfer pricing regulation do not mandate use of inter quartile range.

(d) Comparability adjustment - Like many other countries, Indian transfer pricing regulations provide for "reasonably accurate comparability adjustments". The onus to prove "reasonably accurate comparability adjustment" is on the taxpayer. The experience of Indian transfer pricing administration indicates that it is possible to address the issue of accounting difference and difference in capacity utilization and intensities of working capital by making comparability adjustments. However, Indian transfer pricing administration finds it extremely difficult to make risk adjustments in absence of any reliable and robust and internationally agreed methodology to provide risk adjustment. In some cases taxpayers have used Capital Asset Pricing Method (CAPM).

(e) Location Savings - It is view of the Indian transfer pricing administration that the concept of "location savings" which refer to cost savings in a low cost jurisdiction like India – should be one of the major aspects to be considered while carrying out comparability analysis during transfer pricing audits. Location savings has a much broader meaning; it goes beyond the issue of relocating a business from a 'high cost' location to a 'low cost' location and relates to any cost advantage. MNEs continuously search options to lower their costs in order to increase profits. India provides operational advantages to the MNEs such as labour or skill employee cost, raw material cost, transaction costs, rent, training cost, infrastructure cost, tax incentive etc.

(i) Highly specialized skilled manpower and knowledge

(ii) Access and proximity to growing local/regional market

(iii) Large customer base with increased spending capacity

(iv) Superior information network

(v) Superior distribution network

(vi) Incentives

(vii) Market premium

The incremental profit from LSAs is known as "location rents". The main issue in transfer pricing is the quantification and allocation of location savings and location rents among the associated enterprises.

Under arm's length pricing, allocation of location savings and rents between associated enterprises should be made by reference to what independent parties would have agreed in comparable circumstances.

The Indian transfer pricing administration believes it is possible to use the profit split method to determine arm's length allocation of location savings and rents in cases where comparable uncontrolled transactions are not available. In these circumstances, it is considered that the functional analysis of the parties to the transaction (functions performed, assets owned and risks assumed), **and** the bargaining power of the parties (which at arm's length would be determined by the competitiveness of the market availability of substitutes, cost structure etc) should both be considered appropriate factors.

(f) Intangibles - Transfer pricing of intangibles is well known as a difficult area of taxation practice. However, the pace of growth of the intangible economy has opened new challenges to the arm's length principle. Seventy five percent of all private R&D expenditure worldwide is accounted for by MNEs.

The transactions involving intangible assets are difficult to evaluate because of the following reasons:

(i) Intangibles are seldom traded in the external market and it is very difficult to find comparables in the public domain.

(ii) Intangibles are often transferred bundled along with tangible assets.

(iii) They are difficult to be detected.

A number of difficulties arise while dealing with intangibles. Some of the key issues revolve around determination of arm's length price of rate of royalties, allocation of cost of development of market and brand in a new country, remuneration for development of marketing, Research and Development intangibles and their use, transfer pricing of cobranding etc.

(g) R&D activities - Several global MNEs have established subsidiaries in India for research and development activities on contract basis to take advantage of the large pool of skilled manpower which are available at a lower cost. These Indian subsidiaries are generally compensated on the basis of routine and low cost plus mark up. The parent MNE of these R&D centres justify low cost plus markup on the ground that they control all the risk and their subsidiaries or related parties are risk free or limited risk bearing entities.

The claim of parent MNEs that they control the risk and are entitled for major part of profit from R&D activities is based on following contentions:

(i) Parent MNE designs and monitors all the research programmes of the subsidiary.

(ii) Parent MNE provides fund needed for R&D activities.

(iii) Parent MNE controls the annual budget of the subsidiary for R&D activities.

(iv) Parent MNE controls and takes all the strategic decisions with regards to core functions of R&D activities of the subsidiary.

(v) Parent MNE bears the risk of unsuccessful R&D activities.

The Indian transfer pricing administration always undertakes a detailed enquiry in cases of contract R&D centres. Such an enquiry seeks to ascertain correctness of the functional profile of subsidiary and parent MNE on the basis of transfer pricing report filed by the taxpayers, as well as information available in the public domain and commercial databases. After conducting detailed enquiries, the Indian tax administration often reaches the following conclusions:

(i) Most parent MNEs were not able to file relevant documents to justify their claim of controlling risk of core functions of R&D activities and asset (including intangible assets) which are located in the country of subsidiary or related party.

(ii) Contrary to the above, it was found that day to day strategic decisions and monitoring of R&D activities were carried out by personnel of subsidiary who were engaged in actual R&D activities and bore relevant operational risks.

(h) Marketing Intangibles

Marketing related intangible assets are used primarily in the marketing or promotion of products or services.

This includes: Trademarks; Trade names; Service marks; Collective marks; Certification marks; Trade dress; Newspaper mastheads; Internet domain names; Non-competitive agreements

(i) Customer-related intangible assets – are generated through inter-action with various parties such as customers, entities in complimentary business, suppliers, etc. these can either be purchased from outside or generated internally.

(i) Contractual basis: customer contracts and customer relationships; order or production backlog

(ii) Non-contractual basis:- customer lists; non-contractual customer relationships;

(j) Artistic-related intangible assets – are rights granted by Government or other authorized bodies to the owners or creators to reproduce or sell artistic or published work. These are on a contractual basis. These includes: Plays, opera and ballets; Books, magazines, newspapers and other literary works; Musical works; Picture and photographs; Video and audio-video material.

(k) Intra-group Services - Globalization and the drive to achieve efficiencies within MNE groups have encouraged sharing of resources to provides support between one or more location by way of shared services. Since these intra group services are the main component of "tax efficient supply chain management" within an MNE group, the Indian transfer pricing authorities attach high priority to this aspect of transfer pricing.

The tax administration has noticed that some of the services are relatively straight forward in nature like marketing, advertisement, trading, management consulting etc. However, other services may be more complex and can often be provided on stand alone basis or to be provided as part of the package and is linked one way or another to supply of goods or intangible assets. An example can be agency sale technical support which obligates the licensor to assist the licensee in setting up of manufacturing facilities, including training of staff.

The Indian transfer pricing administration generally considers following questions in order to identify intra group services requiring arm's length remuneration:

(i) Whether Indian subsidiaries have received any related party services i.e., intra group services?

(ii) Nature and detail of services including quantum of services received by the related party.

(iii) Whether services have been provided in order to meet specific need of recipient of the services?

(iv) What are the economic and commercial benefits derived by the recipient of intra group services?

(v) Whether in comparable circumstances an independent enterprise would be willing to pay the price for such services?

(vi) Whether an independent third party would be willing and able to provide such services?

The answers to above questions enable the Indian tax administration to determine if the Indian subsidiary has received or provided intra group services which requires arms' length remuneration. Determination of the arm's length price of intra group services normally involve following steps:

(i) Identification of the cost incurred by the group entity in providing intra group services to the related party.

(ii) Understanding the basis for allocation of cost to various related parties i.e., nature of allocation keys.

(iii) Whether intra group services will require reimbursement of expenditure along with markup.

(iv) Identification of arm's length price of markup for rendering of services.

(I) Financial Transactions

Intercompany loans and guarantees are becoming common international transactions or specified domestic transactions between related parties due to management of cross border funding within group entities of a MNE group. Transfer pricing of inte company loans and guarantees are increasingly being considered some of the most complex transfer pricing issues in India. The Indian transfer pricing administration has followed a quite sophisticated methodology for pricing inter company loans which revolves around:

(i) comparison of terms and conditions of loan agreement;

(ii) determination of credit rating of lender and borrower;

(iii) Identification of comparables third party loan agreement;

(iv) suitable adjustments to enhance comparability.

Transfer pricing administration is more than a decade old in India. However disputes are increasing with each transfer pricing audit cycle, due to the following factors:

(i) Cross border transactions have increased exponentially in the last one decade.

(ii) Lack of international consensus on taxation of certain group cross border transactions like intangible, financial transactions, intra group services etc.

(iii) Difficulty in applying the arm's length principle to complex transactions like business restructuring.

(iv) Taxpayers in India can postpone payment of tax liability by resorting to litigation.

(v) Availability of multiple channels to resolve disputes in India.

22.7 CROSS-BORDER TRANSACTIONS

Cross Border Transaction services means services related to transaction which involve two or more countries. In India there are two Acts which primarily seems to show concern when a person (Indian Resident or foreign Resident) undertakes cross border transactions viz.

(i) Foreign Exchange Management Act,1999

(ii) Income Tax Act,1961

Therefore it is imperative that a person needs to deal with both the above mentioned Acts to enter into a cross-border transaction.

22.7.1. Relevant provisions and the structure

In terms of the provisions of Sec.5 (2) of the Income Tax Act,1961, non-residents are also liable to tax in India on the income received or deemed to be received in India.

22.7.1.1. Major charging provision

The major charging provision is Sec.5(2) of the Income Tax Act,1961. Two major and specific tests are required to determine the incidence of tax and tax liability thereafter. The tests are related to determining:-

(i) Whether Income Accruing or Arising in India or not;

(ii) Whether the Source of Income is India or not.

22.7.1.2. Deeming provisions

The major provisions laying down the source rule are contained in sections 9(1)(vii), 44D,44DA and 115A of the Income Tax Act,1961. There are some specific provisions also related to imposing tax liability on cross-border services, which are, Sections 44B, 44BB, 44BBA, 44BBB.

Section	Deals with	
9(1)(vii)	Fees for technical services paid by the Government or a resident is deemed to accrue or arise in India unless such services are utilized by a resident for business or profession carried on outside India or for the purpose of earning income from any source outside India.	
	Fees for technical services paid by a non-resident is deemed to accrue in India only if such services are utilized in a business carried on in India by the non-resident or are utilized for the purpose of earning income from any source in India.	
44D	Restriction on the right of foreign company to claim deduction for expenses from income in the nature of royalties or fees for technical services received from the Government or an Indian concern as follows:	
	Date of Signature of Agreement	restriction on deduction for expenses
	Before April 1,1976	deduction allowed upto 20% of gross amount of fees for technical services
	After 31st March,1976 but before April 1, 2003	No deduction allowed.
	This section is applicable to foreign companies only and not to any other non-residents.	
44DA	Specific provisions dealing with royalties/fees for technical services – after 31st March,2003 Provisions laid down in this section emphasizes to harmonise the provisions relating to income from royalty or fees for technical services attributable to a fixed place of profession or permanent establishment in India with similar provisions in various tax treaties. In terms of the provisions of this section, deduction is available for expenses from royalty or fees for technical services to a non-resident if : (i) Royalties or FTS are received from Government or an Indian concern (ii) Agreement is made after 31st March,2003 (iii) Business is carried on in India through a permanent establishment (iv) Professional services are provided from fixed place of profession (v) Right, property or contract for which royalty/fees for technical services arises is effectively connected with the permanent establishment or fixed place of profession. "Permanent Establishment is defined in Sec.92F (iiia),which includes a fixed place of business through which the business of the enterprise is wholly or partly carried on". There are three types of Permanent Establishments (PEs): (i) Basic rule PE – a fixed place of business, office, branch, installation, etc (ii) Service PE – presence of employees (iii) Agency PE – presence of dependent agent	
44C	The provision starts with a 'non-obstante clause', i.e. "Notwithstanding anything to the contrary contained in section 28 to 43A…..". This section overrides Sections 28 to 43A and accordingly the words "computation under the head profits and gains of business or profession in accordance with the provisions of ITA" would mean that deduction of head office expenses would be allowed subject to restrictions contained in Section 44C.	
44DA	This section is inserted "with a view to harmonize the provisions relating to the income from royalty or fees for technical services attributable to a fixed place of profession or a permanent establishment in India with a similar provisions in various DTAAs'.	

22.7.1.3. Income accruing or arising

A non-resident is subject to tax in India, if the income is:

(i) Received in India, or

(ii) Deemed to be received in India, or

(iii) Accrues or arises in India, or

(iv) Deemed to be accruing or arising in India

Income from services is subject to tax in India for the non-resident, if such income/fees are received in India or are deemed to be received in India or such fees accrue or arise in India, or are deemed to be accruing or arising in India.

The dictionary meaning of the word "accrue" is to "arise or spring as a natural growth or result"; "to come by way of an increase". "Arising" means "coming into existence or notice or presenting itself".

The word "accrue" and "arise" do not mean actual receipt of the income, profits or gains; and they may be interpreted as conveying the idea of a present enforceable right to receive the income, profits or gains. It is something unclear but is being enforced or converted into money by actual receipt. The words denote a point of time anterior to the actual receipt".

22.7.1.4. Source of Income

The term source is used in the context of income, deduction or collection of tax, and for certain purposes. A source of income in simple terms is a source from which income gets generated or arises. The word source means a place from which something is obtained. The source in relation to an income has been construed to be where the transaction of sale takes place and not where the item of value, which was the subject of the transaction, was acquired.

"Source means not a legal concept but something which a practical man would regard as a real source of income; the ascertaining of the actual source is a practical hard matter of fact".

Example:

A Tax Association proposes to organize its Annual Congress in Country X. For this purpose, the Association branch in Country X has hired an event management company (EMC). The EMC has finalized a five-star hotel as a venue for the Annual Congress. The delegates would also stay in the same hotels. EMC would also coordinate hotel reservations for the delegates coming from the respective countries. The delegate would do the hotel booking through EMC, although the payment would be made directly to the hotel.

For the hotel, the source of income can be said to be :

(i) Tax Association's branch in Country X

(ii) The EMC

(iii) The delegates who actually pay room rent to the hotel

(iv) The event

Different sources of income:

Considering the above analysis/example, the following may be considered as categories of source of income:

(i) Person paying income – the person from whom the income is received and earned. Accordingly, income is said to be originating from him and the payer as such becomes the source of income.

(ii) Economic activity – these ultimately result in revenue for the organization and hence such economic activities can be treated as source of income.

(iii) Business unit/industrial undertaking – these unit would produce/generate income, and hence can be referred as a "source of income".

(iv) Contractual arrangement between the parties – the relationships, rights, obligations and the income flow from such contracts, and hence such contractual arrangement can be viewed as a source of income.

(v) An Asset – tangible or intangible – income may be seen as originating from various types of assets. If an asset generating income is situated/located in a particular country, then it can be treated as a source of income in that country.

(vi) An event/ an act – there are situations, when an event or an act is considered to be a source of income.

(vii) Law/regulations/court decree - in some situations, the income may be originating from the law itself and in such cases, the law itself is treated as the source of income.

22.7.1.5. Place of utilization of services

With reference to terms of Sec.9(1)(vii)(b) of the Income Tax Act,1961, the issue which comes up is, what are the parameters to decide the place where the services are utilized? This correspondingly leads to the issue – whether to avail the exemption under the said provision, whether the services should necessarily be utilized outside India?

22.7.1.5.1. Rendition of services – some broad categories

There may be various forms of rendition of services, some of which are as follows:

(i) Services could be rendered by actually deploying people on a project, say repairing a machine, installing a machine at the location of the person availing services (onsite services).

(ii) Services can be rendered at the location of the services provider by actually deploying people for say repairing a machine, etc

(iii) Services can be rendered by preparing at the location of service provider a written report or an advice

(iv) Services can be rendered by giving advice in a physical meeting

(v) Services can be rendered by giving advice through video-conferencing

(vi) Services can be rendered by giving advice on a telephone

22.7.1.5.2. Place where services are immediately implemented/rendered as a place of utilization of services (immediate location)

The place where the services are immediately implemented or rendered or utilized can be said to be place of utilization of services.

Say,

Situation	Place of utilization of services
(i) Engineer of a service provider repair a machine at the location of the client	such location of the client
(ii) If a machine is repaired at the location of the service provider	location of the person availing services where the machine is put to use
(iii) Services rendered in the form of a written report	place where the report is read and implemented
(iv) Advice through electronic media or a physical meeting	place where the advice is implemented

Some more common examples could be as:-

(a) While you are busy in your office, sitting in a place in India, you are eager to know the results of an ongoing cricket match between India and Australia, which is held in Melbourne Cricket Ground. You have typed “CRI” (i.e. cricket) and sent it to “8888” from your cell phone.

(b) Within a few seconds, the reply/information/data comes back to your hand-set. The services are said to be utilized in India.

(c) While relaxing during your busy schedule, you have logged in to say 'FACEBOOK' or search engine 'Google'. The request is sent from your Cell-phone/Laptop/I-pad/Note-pad/any other electronic device, which is located with you, somewhere in India. The server of 'FACEBOOK' or 'Google' is in a place outside India. You are receiving the required information/data while you are physically present within India. Hence, the place of utilization would be India.

(d) X Ltd. has factories in four different locations A,B,C and D. The Head office of X Ltd is in Location E. Certain functions are centralized in location E. For example, if there are any technical problems in any machines in the factories, then such machines are brought at Location E. Engineers of external service providers visit Location E and repair the machines. The repaired machines are sent back to the respective locations, i.e. A,B,C or D.

(e) In this case, the machines are repaired by external service provider at location E, but the repaired machines are actually utilized in locations A,B,C and D. The immediate location of utilization of services is E but the actual and ultimate utilization of services happens at locations A,B,C and D, i.e. the ultimate locations.

(f) A & Co. is a firm of Cost Accountants. It has branches in four locations, X,Y.Z and P. the staff strength in each location is fifty professionals. A & Co. also hires an external services provider to conduct soft skill training to its professional staff. The training is given at a conference conducted in location X. The staff from the other locations also travelled to location X to avail this training.

(g) The immediate location of services is location X but the ultimate location are all X,Y,Z and P. This is because the professional staff availing the training could actually apply the skills learned in the respective locations.

22.8 CLASSIFICATION OF "CROSS BORDER SERVICES"

(a) Advance Ruling Representative Services

The term 'advance ruling' means (a) the determination of a question of law or fact in relation to a transaction which has been undertaken or is proposed to be undertaken by a non-resident applicant and also includes the determination of the tax liability of a non-resident arising out of such transaction with a resident applicant; (b) the determination or a decision on a question of law or fact relating to the computation of total income which is pending before any Income-tax authority or the Appellate Tribunal.

(b) Branch office set up of a Foreign Company

Permission to set up a branch office is granted by the Reserve Bank of India. A Branch office of a foreign company upon approval from the RBI must be compulsorily registered under the (Indian) Companies Act, 2013.

Upon registration under the Companies Act, 2013 the branch office can carry on its business activities in the same way as a domestic company. Unlike a liaison office a branch office can generate revenue from the sales in the local market and repatriate the profits to the foreign parent company.

A branch office so approved and registered can carry on the following activities :–

(a) Export/Import of goods

(b) Rendering professional or consultancy services

(c) Carrying out research work, in which the parent company is engaged

(d) Promoting technical or financial collaborations between Indian companies and parent or overseas group company

(e) Representing the parent company in India and acting as buying selling agents in India

(f) Rendering services in Information Technology and development of software in India

(c) Business set up services

Consultancy services rendered to Non-residents and entrepreneurs in starting, growing, expanding, diversifying and in case required, closing businesses in India. The services may also include preparation of project reports, feasibility report, Market survey, Project Planning & many more.

(d) FEMARBI Compliance

The transaction involving foreign exchange is regulated by Foreign Exchange Management Act, 1999 in India. The main thrust from liberalization of economy has been on promotion of foreign exchange rather than control of foreign exchange. All transaction involving foreign exchange is regulated by FEMA and the provisions of FEMA have to comply with wherever applicable. The preamble of the act says that it is an Act to consolidate and amend the law relating to foreign exchange with the objective of facilitating external trade and payments and for promoting the orderly development and maintenance of foreign exchange market in India.

(e) Foreign company incorporation

In India, incorporation of a company involving foreign investment is primarily governed by two laws i.e. Companies Act, 2013 and Foreign Exchange Management Act, 1999 (FEMA). Companies Act is principally concerned with compliance with requirements and guidelines prescribed by registrar of companies whereas FEMA mandates compliances with guidelines prescribed by Reserve Bank of India in relation to Foreign Direct Investment in India. It is imperative from above that our scope of service emanate in form of consultancy services for ensuring compliance with both the above laws i.e. Companies Act, 2013 and FEMA, 1999 and liaisoning with respective authorities.

<u>Cases for reference</u>:

1. B Ltd., having 200 employees, engaged in manufacturing concern. The tax laws requires that the company should deduct taxes should deduct taxes from the salaries paid to its employees. To comply with the requirement, the company has recruited a pay roll manager whole role, besides other things, is to determine the taxes required to be deducted from the salaries of the employees. Similarly, payroll manager also takes care of the leave balances of the employees. The work performed by the payroll manager can be said to be managerial services.

   AZ and Co., a firm of service providers, have developed payroll software which takes care of various payroll related functions of the organizations. The firm approaches to offer the services of managing payroll of B Ltd. through this software. As per revised arrangement, the employees of B Ltd. would interact with the website of AZ and Co. as against the payroll manager of B Ltd.

2. If a service provider provides services of managing canteen of an organization, it would be an ongoing process which will continue throughout the year. As against this, if a company organizes events celebrating completion of its 25th year, the service provider who manages such celebration event (i.e. event manager) would be doing a onetime assignment.

   Apparently, there is no difference between the two. In both the cases, the service provider uses his managerial skills and manages various functions. Merely because the celebration event happens only, once in a year the fact that the services provided are managerial in nature cannot be denied. Further, neither the definition of "fees for technical services" contained in Explanation 2 nor Sec.9(1)(vii) suggests that the managerial services cannot be for one off transaction.

3. Indirect Taxes on Soft ware

   "Software is the set of instructions that allows physical hardware to function and perform computations in a particular manner, be it a word processor, web browser or the computer's operating system.

These expressions are in contrast with the concept of hardware which are the physical components of a computer system, and data, which is information that performs no computation and gives no enabling instructions to computer hardware but is ready for processing by the computer software" – LML Ltd. vs. Commissioner of Customs 2010 (258) ELT 321(SC).

Also held that CD-ROM containing images of drawings and designs of engineering goods are not classifiable as computer software.

In 2004, the Supreme Court pronounced a landmark judgement in case of Tata Consultancy Services vs. State of Andhra Pradesh(2004) 141 Taxman 132(SC) – TCS Case. The judgement stated the parameters under which software would qualify as "goods". The relevant text of the judgement read " the text, to determine whether a property is 'goods', for the purposes of sales tax (now VAT), is not whether the property is tangible or intangible or incorporeal. The test is whether the concerned item is capable of abstraction, consumption and use and whether it can be transmitted, transferred, delivered, stored, possessed, etc. Admittedly in the case of software, both canned and uncanned, all of these are possible.'

While the Supreme Court firmly concluded that sale of branded/canned software is liable to sales tax law (now VAT), the view expressed on unbranded software was with caveat stating that 'even unbranded software, when it is marketed/sold, may be goods. We, however, are not dealing with this aspect and express no opinion thereon because in case of unbranded software other questions like situs of contract of sale and/or whether the contract is a service contract may arise'.

In the light of Tax Treaty Provisions

1. A Ltd. is a tax resident in Country A and has a branch in Country B. The branch in Country B pays fees to technical services to C Ltd which is a tax resident of Country C. There is a tax treaty between Country B and Country C.

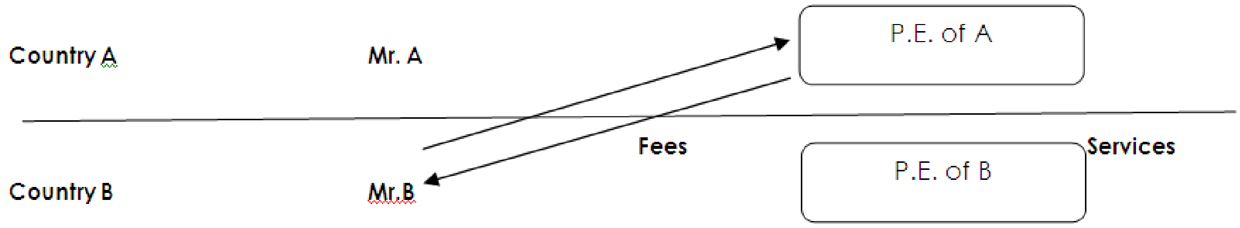
As per Para 5 of Article 12 of the tax treaty, the fees are "deemed to arise" in Country B as it is paid and borne by the branch. As per the domestic law of country A, the fees arise in Country A. Further, Article 12 shall be applicable to such fees i.e. as per Para 1, fees arising in Country B and paid to a resident of Country C may be taxed in Country C.

While interpreting Para 2 of Article 12, the same question needs to be analysed i.e. whether the term "arising" in Para 2 shall also include "deemed to arise".

As per Para 1 of Article 12, income (deemed to) arising in Country B and paid to the resident of Country C may be taxed in Country C.

Such fees may also be taxed in the country in which it arises i.e. Country B. This is on the basis that once the fees are deemed to arise in Country B, all the implications shall follow as if the income would have arouse in Country B.

2. A and B are tax residents of Country A and Country B respectively. A has an office in Country A which is its permanent establishment. B renders services to A in relation to the permanent establishment and the fees are borne by the permanent establishment.



In this example, the fees would be deemed to arise in Country A as per the second sentence of Para 5 of Article 12. However, the fees would be deemed to arise in Country A even by virtue of the first sentence of Para 5 of Article 12, this is because A is a tax resident of Country A. Further, generally a permanent establishment is generally contemplated in a country other than the country in which the head office exists i.e. the country in which the person is a resident.

Thus, although the second sentence of Para 5 of Article 12 uses the words " is a resident of a contracting state or not" , it probably does not contemplate a situation described in this example i.e. a person having a permanent establishment in the country in which it is resident.

3. A, B and C are residents of countries A,B and C respectively. C has a permanent establishment in Country B and the fees are borne by it. C pays fee to A.

In this case, the payer (C) is not a resident of country B where the permanent establishment is situated. Although the payer is not a resident of country B, it has a permanent establishment in that country.

4. Credit Rating Services

X Ltd. an Indian Company availed credit rating services from B Ltd. an Australian Company, for which the Indian Company had paid the annual surveillance fee to B Ltd. Is this taxable?

In terms of tax treaty provision between India and Australia, the payment was held to be "royalty" considering the provisions of clauses (c) & (d) of Article 12(3), which are worded as follows:

"(c) the supply of scientific, technical, industrial or commercial knowledge or information;

(d) the rendering of any technical or consultancy services (including those of technical or other personnel) which are ancilliary and subsidiary to the application or enjoyment of any such property or right as is mention in sub-paragraph(a) any such equipment as mentioned in sub-paragraph(b) or any such knowledge or information as is mentioned in sub-paragraph(c)".

Credit rating was treated as "commercial information" and fees received was falling under "Royalty".

[Essar Oil Limited (Essar) and Standard & Poor's (Australia) Pty. Ltd (S&P)].

5. Procurement charges for goods

An Indian Company availed services of a German entity for the purpose of procurement of goods from outside India. As a consideration, the Indian company paid 4% of the total purchase price as fees to the German entity.

If this service is subject to tax as "fees for technical services"?

The Mumbai Bench of the Tribunal had examined this issue in the case of Linde A.G. vs ITO., where the CIT(A) held the case as "fees for technical services" in terms of Indo-German treaty. The relevant definition read as follows:

" the payment of any kind to any person other than payments to an employee of the person making the payments in consideration for services of a managerial ,technical or consultancy nature, including the provision of services of technical or other personnel".

The Tribunal held that the entire fees were in the nature of commercial profits and cannot be subject to tax in India in the absence of permanent establishment of the German Company in India.

6. Inspection fees

A German company sold certain equipment to an Indian Company. The equipment was damaged in transit. The German company sent two of its technicians and charged "inspection fees". The tax authorities taxed such fees as "fees for technical services". The German company claimed that such fees cannot be taxed as "fees for technical services".

The Tribunal held that the technician could not have been sent unless they were equipped with "technical knowledge". Accordingly, the fees were held to be 'fees for technical services" in terms of the provisions of Article 12 of the Indo-German treaty.

7. Services linked to purchase of machinery

The Indian party importing large machinery and equipment from foreign suppliers also require their assistance in installation/commissioning of such machinery, etc. At times, the foreign supplier would send his technicians to India for this purpose. The foreign supplier may also charge separate consideration for such services.

On a standalone basis, the services provided by the foreign supplier may be in the nature of technical services. However, the court has taken a view that such services are to be treated as incidental to the purchase of machinery and also inextricably linked to it. On the basis, the consideration for such services is not treated as fees for technical services, but is given the same treatment which is given to the sales consideration. Hence, it is to be considered as "make available" and not fees for technical services.

8. Dividend Income

(a) "Forming part of the Assets"

(i) A UK-based company has established a banking branch in India. The branch has also invested its funds in shares of Indian Companies. The shares of Indian companies could be said to be forming part of the assets of the permanent establishment. The branch is the economic owner of the shares

(ii) A US-based conglomerate company has a permanent establishment in India. The company has different types of business including cement, steel, etc. The Indian branch is in the business of steel. The US-based company also owns certain shares of an Indian cement company. The Indian branch, which is involved in steel business, has nothing to do with the cement business. However, it has the custody of the share certificates of the shares owned by the head office. These shares are not shown in the balance sheet of the Indian branch.

Are the shares forming part of assets of the permanent establishment? The answer seems to be 'no'. The permanent establishment is just holding the shares physically and it may be possible to say that such shares do not form part of the assets of the permanent establishment. The permanent establishment is not the economic owner of the shares, as it does not enjoy the risk and rewards of the shares.

(b) What is 'otherwise effectively connected'?

(i) A non-resident company has a subsidiary company in India. Such company, however, becomes permanent establishment of the non-resident company by virtue of provisions of Article 5(4) – dependent agent. This subsidiary company declares dividend to the parent company.

Are the shares effectively connected with the permanent establishment? The answer seems to be 'yes'. This is because the subsidiary is a permanent establishment of the foreign company and the shares are of such subsidiary.

However, considering the new guidance available in the OECD commentary, the permanent establishment may not be said to be the "economic owner" of the shares.

(ii) The Indian permanent establishment has played effective role in purchasing the shares of an Indian company on behalf of its head office outside India. In such situation, it may be difficult to say that the shares are effectively connected with the Indian permanent establishment, as it is no way connected with the shares except that it played a major role in acquisition of the shares for the head office.

9. Service PEs

An enterprise can carry on business in other country in different manners. This may be broadly divided in the following three categories:

(i) Business activities carried on in a branch, an office, etc

(ii) Business activities through a dependent agent

(iii) Business activities through employees.

Service PE is defined in clause (b) of Article 5(3) of the UN Model, as follows:

"The furnishing of services, including consultancy services,

by an enterprise through employees or other personnel engaged by the enterprise for such purpose, ut only if activities of that nature continues (for the same or a connected project) within the country for a period of periods *aggregating more than six months within any twelve month period*."

(a) Presence of person availing services

If the person availing the services is present in the country in which the services are rendered, the service PE would be formed. This can be explained on the basis of the following example:

X Ltd a company based in Country X, specializes in rendering machine maintenance services. This service requires actual testing, cleaning, etc of the machine.

Z Ltd. a company in Country Z, wants maintenance services for the machines purchased by it . Z Ltd. engages X ltd for this purpose. The employees of X Ltd visit Country Z and carry out the maintenance for the machines.

In this case, X Ltd is furnishing services in Country Z through its employees. Service PE is created if the employees of X ltd provide services for a period exceeding 90 days.

(b) Absence of person availing services in the country –direct utilization / consumption of services

It is possible that the person availing services may not be present in the country in which services are rendered, but such services may be consumed in the same country in which the service are rendered.

The issue is whether it is necessary that the person availing services should be present in the same country in which the services are rendered. As such the language of Article 5(3)(b) does not require that the person availing services should be present in the same country. What it requires is that the services should be rendered within the country. This can be explained on the basis of the following example:

X Ltd a company based at Country X, specializes in rendering machine maintenance services. The service requires actual testing, claiming, etc of the machine.

Y ltd, a company situated in Country Y, wants maintenance services for the machines sold by it to its customers in Country Z. Y ltd. engages X Ltd for this purpose. The employees of X Ltd visit country Z and carry out maintenance for the machines sold by Y ltd.

The following issues may arise in this structure:

(i) The employees of X Ltd are rendering services to whom? To the customers in Country Z or to Y Ltd based in Country Y?

(ii) If the services are rendered to Y Ltd,. then can it be said that the services are not furnished in Country Z as the beneficiary (Y Ltd) is situated in Country Y. Does presence of employees result in service PE of X ltd in country Z?

The answer to the first querry is that the employees of X Ltd are rendering services to X Ltd only, as there is a contract of employment between them. There is no contract between employees of X Ltd and Y Ltd or the customers of Y Ltd.

The second issue is whether it can be claimed that services are furnished within Country Z as the beneficiary (Y Ltd) is not present in country Z.

The services are undoubtedly furnished in Country Z as the employees are present and render such services in Country Z. Further, Article 5(3)(b) does not suggest that the person availing such services should also be present in the same country in which the services are rendered.

(c) Absence of person availing services in the country – indirect utilization of services

It may happen that the person availing services is not present in the country where the employees carry out activities. However, the services may ultimately be utilized in the same country.

Example:

X Ltd. is based in Country X, specializes in real estate related issues. Y ltd is situated in Country Y, wants to enter into real estate sector in Country Z. Y Ltd. engages X Ltd for the purpose of studying the real estate market in Country Z. The employees of X Ltd visit Country Z and carry out the market research activities. The employees of X Ltd carry out various activities in Country Z for 130 days and at the end of the assignment the employees go back to Country X, prepare the final report and sent it to Y Ltd. Y Ltd. uses such report for the purpose of future investments in Country Z.

The issue to be answered is whether X Ltd. can be considered as rendering services within Country Z? Whether the presence of such employees results in X Ltd having a service PE in Country Z?

In this example, the residence country is country X. however, the determination of the source country leads to some confusion. Should Country Y be considered as 'source country' on the basis that X Ltd earns income from the resident of country Y. Alternatively, should country Z be considered as a source country on the basis that the source of revenue for X Ltd is the activities carried out in Country Z.

Even in a situation, where the services are considered as not rendered in Country Z, the fact that the economic activities are carried out on the soil of Country Z cannot be denied. Accordingly, country Z may want to tax such activities. Country Z may have the right to tax the employees of X Ltd for the services rendered and X Ltd. However, such right can be exercised only if the provisions of DTAA permit.

22.9 ASSOCIATED ENTERPRISE

The term 'associated enterprise' has been defined in a broad manner. Based on the same, the following illustrates the definition when Enterprise X ("X") would be the associated enterprise of Enterprise Y ("Y") :

- X participates, directly or indirectly, or through one or more intermediaries, in the management, control4 or capital of Y and one or more of the requisites enlisted below are fulfilled; or
- The same persons participate in the management, control or capital of X, as also that of Y and one or more of the requisites enlisted below are fulfilled.
- X and Y would be deemed to be associated enterprises if at any time during the previous year :
- X holds directly or indirectly shares carrying at least 26% voting power in Y or vice versa;
- Any person holds directly or indirectly shares carrying at least 26% voting power in both X and Y;
- A loan advanced by X to Y amounts to atleast 51% of book value of the total assets of Y or vice versa;
- X guarantees at least 10% of the total borrowings of Y or vice versa;
- More than half of the directors or members of the governing board, or one or more of the executive directors or executive members of the governing board of X are appointed by Y or vice versa;
- More than half of the directors or members of the governing board, or one or more of the executive directors or members of the governing board of X and Y are appointed by the same person(s);
- The manufacture / processing of goods/articles by, or business of, X, is wholly dependent on use of intangibles or any other commercial rights of similar nature, or any data, documentation or drawing etc., owned by Y or for which Y has exclusive rights; or
- Atleast 90% of raw materials for the manufacture or processing of goods or articles required by X are supplied by Y or persons specified by Y under commercial terms influenced by Y or;
- Goods / articles manufactured / processed by X are sold to Y or persons specified by Y, and Y influences the commercial terms relating to the sale or;
- X is controlled by Mr. A and Y is controlled by Mr. A or relative of Mr. A either individually or jointly;
- X is controlled by a Hindu Undivided Family, and Y is controlled by a member of such Hindu Undivided Family or by a relative of a member of such Hindu Undivided Family, or jointly by such member and his relative; or
- X is a firm, association of persons or body of individuals, and Y holds atleast 10% interest in such firm, association of persons or body of individuals; or
- There exists, between X and Y, any relationship of mutual interest, as may be prescribed (no such relationship has yet been prescribed).

Explanatory Notes & Illustrations on the different Methods of determination of Arms Length Price u/s 92C of the Income Tax Act,1961

Method 1: Computation of Arm's Length Price:

COMPARABLE UNCONTROLLED PRICE METHOD (CUP)

An uncontrolled price is the price agreed between unconnected parties for the transfer of goods and services. If this transfer is in all material respects comparable to transfers between associates, then that price becomes a comparable uncontrolled price.

Under this method, the price at which a controlled transaction is carried out is compared to the price obtained in a comparable uncontrolled transaction.

Rule 10B (1) (a) of the Income Tax Rules read with sub-section (2) of Section 92C, the CUP method is described as under:

(i) The price charged or paid for property transferred or services provided in a comparable uncontrolled transaction, or a number of such transactions, is identified;

(ii) Such price is adjusted to account for differences, if any, between the international transaction or specified domestic transaction and the comparable uncontrolled transactions or between the enterprises entering into such transactions, which could materially affect the price in the open market;

(iii) The adjusted price arrived at sub-clause(ii) is taken to be an ALP in respect of the property transferred or services provided in the international transaction or specified domestic transaction.[1]

Terms used:

(1) Transaction: As per Sec.92F(v) the term "transaction" which is defined to include an arrangement, understanding or action in concert, whether or not such arrangement, understanding or action is formal or in writing or whether or not it is intended to be enforceable by legal proceeding.

"Transaction" includes a number of closely linked transactions.

(2) "Uncontrolled Transaction": a transaction between enterprises other than associated enterprises, whether resident or non-resident.

(3) "Comparable Transaction": The OECD guidelines further states that an uncontrolled transaction is comparable to a controlled transaction (i.e. it is a comparable uncontrolled transaction) for purposes of the CUP method if one of the two conditions is met:

(i) None of the differences(if any) between the transactions being compared or between the enterprises undertaking those transactions could materially affect the price in the open market;

(ii) Reasonably accurate adjustments can be made to eliminate the material effects of such differences.

(4) International transaction : Sub-section (1) of Sec.92B defines the term as follows:

"For the purposes of this section and sections 92,92C,92D and 92E, "international transaction" means

1 Definition of CUP as per OECD Guidelines:

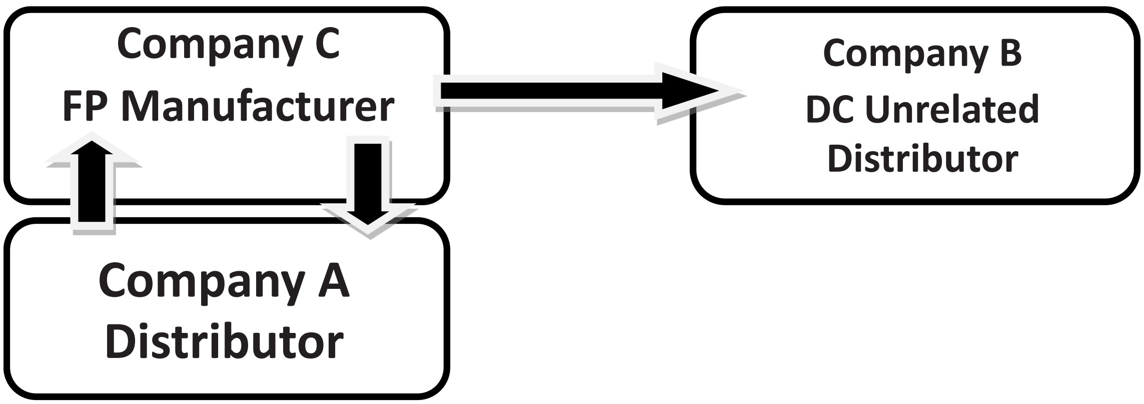
"The CUP method compares the price charged for property or services transferred in a controlled transaction to the price charged for property or services transferred in a comparable uncontrolled transaction in comparable circumstances. If there is any difference between the two parties, this may indicate that the conditions of the commercial and financial relations of the associated enterprises are not at arm's length , and that the price in the uncontrolled transaction may need to be substituted for the price in the controlled transaction".

a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises."

(5) **"Property"** includes goods, articles or things and intangible property.

(6) **"Services"** include financial services.

Scope:



Company C sells toaster ovens to its subsidiary A and to unrelated distributor C. Toaster ovens sold to A and B are identical and there are no material differences between the C to A and C to B transactions. CUP is the most reliable (best) method.

(1) Interest rate charged on a loan;

(2) Royalty payment;

(3) Industries where CUPs are more prevalent, for example, software development where products are often licensed to a third party;

(4) The price charged for the transfer of a homogeneous item, such as traded commodity

(5) Extracted raw materials;

(6) Harvested crops;

(7) Animal products;

(8) Fungible chemicals;

(9) Other fungible goods i.e. pen, pencil, clips, computer disk, etc.;

(10) Transactions which are dependent on publicly available market quotations

Methods of CUP:

The CUP method provides the best evidence of an arm's length price.

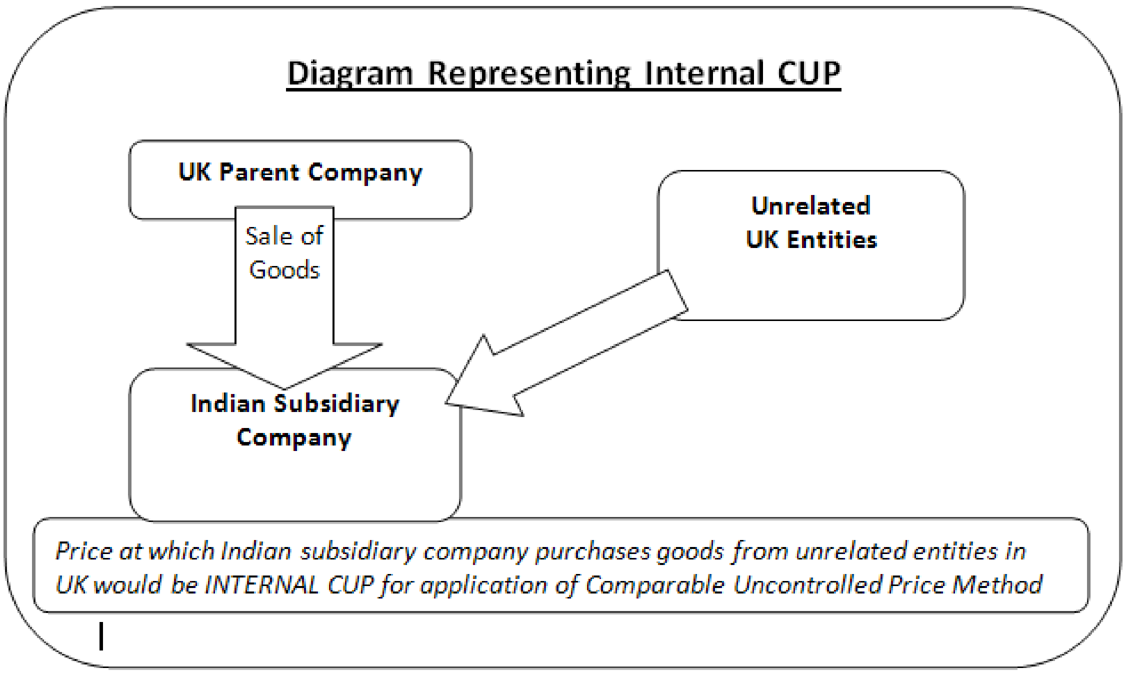
CUP can be either of the following:

(1) Internal CUP: this would be available if the taxpayer (or one of its group entities) enters into a comparable transaction with an unrelated party where the goods or services under consideration are same or similar.

Situations where Internal CUP may be applicable:

(a) The tax payer or any other member of the group **sells** similar goods in similar quantities and under similar terms to an independent enterprise in a similar market.

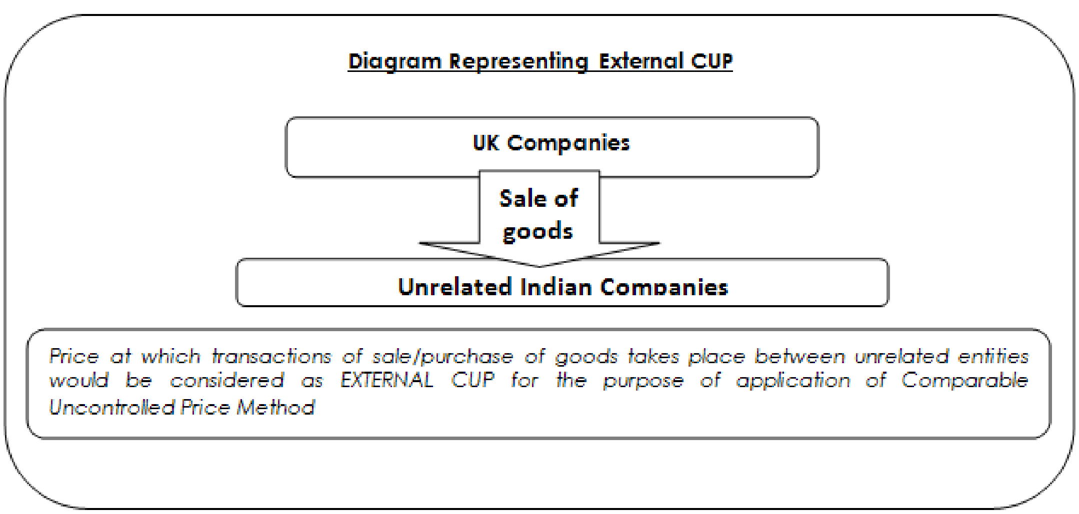
(b) The tax payer or another member of the group **buys** similar goods in similar quantities and under similar terms from an independent enterprise in a similar market (an internal comparable).



(2) **External CUP**: this would be applicable if a transaction between two independent enterprises involves comparable goods or services under comparable conditions.

(a) An independent enterprise **sells** the particular product in similar quantities and under similar terms to another independent enterprise in a similar market;

(b) An independent enterprise **buys** similar goods in similar quantities and under similar terms from another independent enterprise in a similar market.



Adjustments to CUP:

There will be no comparable transactions to the ones under review and there will be a real doubt over how independent parties would have behaved. It is possible to adjust a potential comparable to take account of factors such as differences in volumes sold, markets traded in, terms of trade,etc.

If there are differences between the controlled and uncontrolled transactions that would affect price, adjustments should be made to the price of the uncontrolled transaction according to the comparability provisions.

The tax payer must provide sufficient proof by way of concrete documentation that the adjustments made were correct.

(1) FAR Analysis;

(2) Quality of the product or service;

(3) Characteristics of the Property;

(4) Contractual terms;

(5) Level of the market;

(6) Geographic market in which the transaction takes place;

(7) Date of the transaction;

(8) Intangible property associated with the sale; and

(9) Foreign currency risks.

Other important factors affecting CUP

(1) Time of the transaction and multiple year data

(2) Data and assumptions

(3) Indirect CUP

(4) Use of quotation medium

(5) Extra ordinary market conditions

Conditions for application of Comparable Uncontrolled Price Method:

"Where an assessee, being an associated enterprise as per Sec. 92A of the Act had entered into a transaction as per Sec. 92B of the Act, involving transfer of goods or rendering of services as per Sec.92F (v) of the Act, and where such a transaction is uncontrolled in nature, having classified to be a comparable transaction, the Assessing officer shall for the purpose of determining the Arm's Length price, being satisfied that the transactions could materially affect the price in the open market and hence comparable; then reasonable adjustments shall be made to eliminate the material effects arising from such differences, for the purpose of determining the Arm's Length Price. The adjustments for differences shall be made for:

(i) FAR Analysis;

(ii) Quality of the product or service;

(iii) Characteristics of the Property;

(iv) Contractual terms;

(v) Level of the market;

(vi) Geographic market in which the transaction takes place;

(vii) Date of the transaction;

(viii) Intangible property associated with the sale;

(ix) Foreign currency risks;

(x) Time of the transaction and multiple year data;

(xi) Data and assumptions;

(xii) Indirect CUP;

(xiii) Use of quotation medium; and

(xiv) Extra ordinary market conditions."

Accountant's Report:

The arm's length price as computed under this method shall be audited and certified in Form No. 3CEB vide Rule 10E.

Steps in Computation of Arm's Length Price using CUP Method:

Step I: Identify the price charged/ paid for property transferred or services provided in a **comparable uncontrolled transaction(s).**

Step II: Adjust the price derived in Step I above **for differences**, if any, which could materially affect the price in the open market.

(a) between the international transaction or specified domestic transaction and the comparable uncontrolled transactions, or

(b) between the enterprises entering into such transactions.

Step III: Arm's Length Price = Step I **Add/Less**: Step II

Computation of Arm's Length Price as per Comparable Uncontrolled Price Method

No.	Particulars	Amount (₹)
1	Price charged or paid for property transferred or services rendered in a comparable uncontrolled transaction	XXXXX
2	Add/Less: Adjustments for differences, having material affect on the price in the open market:	
	i) Adjustments for FAR Analysis	XXXX
	ii) Quality of the product or service	XXXX
	iii) Characteristics of the Property	XXXX
	iv) Contractual terms	XXXX
	v) Level of the market	XXXX
	vi) Geographic market in which the transaction takes place	XXXX
	vii) Date of the transaction	XXXX
	viii) Intangible property associated with the sale	XXXX
	ix) Foreign currency risks	XXXX
	x) Time of the transaction and multiple year data	XXXX
	xi) Data and assumptions	XXXX
	xii) Indirect CUP	XXXX
	xiii) Use of quotation medium	XXXX
	xiv) Extra ordinary market conditions	XXXX
3	Arm's Length Price for the purpose of Sec.92C (1 -2)	XXXX

Illustrations on COMPARABLE UNCONTROLLED PRICE METHOD

Illustration 1: J Inc. of Korea and CD Ltd, an Indian Company are associated enterprises. CD Ltd manufactures Cell Phones and sells them to J.K. & F Inc., a Company based at Nepal. During the year CD Ltd. supplied 2,50,000 Cellular Phones to J Inc. Korea at a price of ₹3,000 per unit and 35,000 units to JK & F Inc. at a price of ₹5,800 per unit. The transactions of CD Ltd with JK & F Inc. are comparable subject to the following considerations -

Sales to J Inc. are on FOB basis, sales to JK &F Inc. are CIF basis. The freight and insurance paid by J Inc. for each unit @ ₹700. Sales to JK &F Inc. are under a free warranty for Two Years whereas sales to J Inc. are without any such warranty. The estimated cost of executing such warranty is ₹500. Since J Inc.'s order was huge in volume, quantity discount of ₹200 per unit was offered to it.

Compute the Arm's Length Price and the subsequent amount of increase in the Total Income of CD Ltd, if any.

(a) Computation of Arm's Length Price of Products sold to J Inc. Korea by CD Ltd

Particulars	₹	₹
Price per Unit in a Comparable Uncontrolled Transaction		5,800
Less: Adjustment for Differences -		
(a) Freight and Insurance Charges	700	
(b) Estimated Warranty Costs	500	
(c) Discount for Voluminous Purchase	200	(1,400)
Arms's Length Price for Cellular Phone sold to J Inc. Korea		4,400

(b) Computation of Increase in Total Income of CD Ltd

Particulars	₹
Arm's Length Price per Unit	4,400
Less: Price at which actually sold to J Inc. Korea	(3,000)
Increase in Price per Unit	**1,400**
No. of Units sold to J Inc. Korea	2,50,000
Increase in Total Income of CD Ltd (2,50,000 x ₹1,400)	**₹ 35 Crores.**

Illustration 2: — Comparable sales of same product

DSM, a manufacturer, sells the same product to both controlled and uncontrolled distributor. The circumstances surrounding the controlled and uncontrolled transactions are substantially the same, except that the controlled sales price is a delivered price to the buyer and the uncontrolled sales are made F.O.B. DSM's factory. Differences in the contractual terms of transportation and insurance generally have a definite and reasonably ascertainable effect on price, and adjustments are made to the results of the uncontrolled transaction to account for such differences. In this case the transactions are comparable and internal CUP can be applied by comparing the prices of both, the controlled and uncontrolled transactions, albeit after subtracting the costs of transportation and insurance of the controlled transaction.

Illustration 3: — Effect of geographic differences

FM, a foreign specialty radio manufacturer, also exports its radios to a controlled U.S. distributor, AM, which serves the United States. FM also exports its radios to uncontrolled distributors to serve in South America. The product in the controlled and uncontrolled transactions is the same, and all other circumstances surrounding the controlled and uncontrolled transactions are substantially the same, other than the geographic differences. The geographic differences e.g. differences in purchasing power, levels of economic development, etc, in two different geographies, are likely to have a material effect on price, for which accurate adjustments cannot be made and hence the transactions are not comparable. Thus, CUP method cannot be applied.

Illustration 4: — External Commercial Borrowing

Pharma Ltd, an Indian company has borrowed funds from its parent company at LIBOR plus 150 basis points. The LIBOR prevalent at the time of borrowing is 4% for US$, thus its cost of borrowings is 5.50%. The borrowings allowed under the External Commercial Borrowings guidelines issued under FEMA, for example, say is LIBOR plus 250 basis points, then it can be said that Pharma's borrowing at 5.50% is less than 6.50% and thus at arm's length.

In this connection, one may rely on Rule 10B (2) (d) which specifies that the comparability of an international transaction with an uncontrolled transaction shall be judged with reference to the laws and government orders in force.

Method 2: Computation of Arm's Length Price:

RESALE PRICE METHOD (RPM)

The RPM is a direct method which comprises the gross margins (i.e. gross profit over sales) earned in transactions between related and unrelated parties for the determination of the arm's-length price. The RPM method requires high level of functional comparability and is mainly applicable where the controlled party is a distributor.

Rule 10B (1) (b) of the Income Tax Rules read with sub-section (2) of Section 92C, the RPM method is described as under:

(i) The price at which property purchased or services obtained by the enterprises from an associated enterprise is resold or are provided to an unrelated enterprise, is identified;

(ii) Such resale price is reduced by the amount of a normal gross profit margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from obtaining and providing the same or similar services, in a comparable uncontrolled transaction, or a number of such transactions;

(iii) The price so arrived at is further reduced by the expenses incurred by the enterprise in connection with the purchase of property or obtaining of services;

(iv) The price so arrived at is adjusted to take into account the functional and other differences including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market;

(v) The adjusted price arrived at under sub-clause (iv) is taken to be an arm's length price in respect of the purchase of the property or obtaining of the services by the enterprise from the associated enterprise. [2]

Terms used:

1) Transaction: As per Sec.92F(v) the term "transaction" which is defined to include an arrangement, understanding or action in concert, whether or not such arrangement, understanding or action is formal or in writing or whether or not it is intended to be enforceable by legal proceeding.

2 *Definition of RPM as per OECD Guidelines :*

" a transfer pricing method based on the price at which a product that has been purchased from an associated enterprise is resold to an independent enterprise. The resale price is reduced by resale price margin. What is left after subtracting the resale price margin can be regarded, after adjustment for other costs associated with the purchase of the product (i.e. custom duties) as an ALP of the original transfer of property between the associated enterprises".

For the above purposes, the OECD Guidelines define Resale Price Margin as: "a margin representing the amount out of which a reseller would seek to cover its selling and other operating expenses and, in the light of the functions performed (taking into account assets used and risks assumed), make an appropriate profit."

"Transaction" includes a number of closely linked transactions.

2) **"Uncontrolled Transaction":** a transaction between enterprises other than associated enterprises, whether resident or non-resident.

3) **"Comparable Transaction":** The OECD guidelines further states that an uncontrolled transaction is comparable to a controlled transaction (i.e. it is a comparable uncontrolled transaction) for purposes of the CUP method if one of the two conditions is met:

   i) None of the differences(if any) between the transactions being compared or between the enterprises undertaking those transactions could materially affect the price in the open market;

   ii) Reasonably accurate adjustments can be made to eliminate the material effects of such differences.

4) **International transaction** : Sub-section (1) of Sec.92B defines the term as follows:

   "For the purposes of this section and sections 92,92C,92D and 92E, "international transaction" means a transaction between two or more associated enterprises, either or both of whom are non-residents, in the nature of purchase, sale or lease of tangible or intangible property, or provision of services, or lending or borrowing money, or any other transaction having a bearing on the profits, income, losses or assets of such enterprises, and shall include a mutual agreement or arrangement between two or more associated enterprises for the allocation or apportionment of, or any contribution to, any cost or expense incurred or to be incurred in connection with a benefit, service or facility provided or to be provided to any one or more of such enterprises."

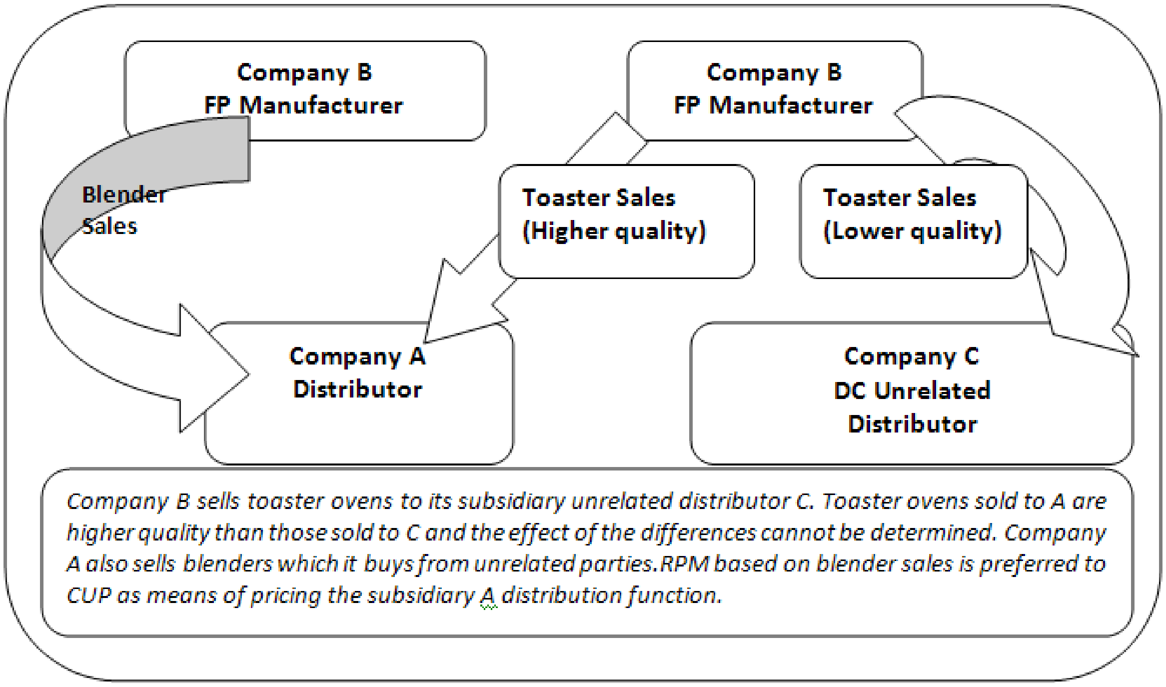
5) **"Property"** includes goods, articles or things and intangible property.

6) **"Services"** include financial services.

7) **Controlled party**:

8) **Gross margin**: Gross margin is calculated as a percentage on sales, earned in transactions between related and unrelated parties for the determination of the arm's length price.

9) **Tested Party**: As per the OECD guidelines, the tested party is ought to be the enterprise that offers a higher degree of comparability or would require lesser adjustment with uncontrolled companies. Consequently, the enterprise that requires the least amount of adjustments as compared to potentially comparable companies should be the tested party. Hence, in most cases, the tested party will be the least complex of the controlled tax payers and will not own valuable intangible property or unique assets that distinguish it from potential uncontrolled comparables.



Applicability of RPM:

This method is ideally suited to measure the value of the services performed by a buyer or seller of goods who generally acts as a distributor and does not add a significant value to goods sold. It is applicable even with differences in products, as long as the functions performed are similar. However, it is less useful where goods are further processed or in nature of raw material.

RPM is applied in a backward process. From the sale price to an unrelated third party, appropriate adjustments to the gross margin is made by comparing the transaction to other, third party transactions.

(1) This method can be applied when there are no comparable uncontrolled sales and an applicable resale price is available within a reasonable time before or after the controlled sale.

(2) Where the reseller does not add substantial value to the goods through physical modification. Limited enhancements such as packaging, repackaging, labeling or minor assembly ordinarily do not generally affect the use of RPM. Hence, RPM may not be applicable if the reseller performs value added functions.

(3) RPM is more accurate where it is realized within a short time of the reseller's purchase of goods.

(4) RPM is ordinarily used when the controlled reseller does not use intangible property to add substantial value to the products.

(5) RPM is applied when the reseller does not alter the physical characteristics of the product.

(6) Where the reseller has the exclusive right to resell the goods, the gross margin would be affected by factors like size of market, existence of substitute goods, and level of activity undertaken by the reseller.

Adjustments to RPM:

Where it is not possible to compare the transactions even by comparing with the transactions entered by the third party and that the differences have a material effect on price, necessary adjustments shall have to be made to eliminate the effect of such differences.

(1) Inventory adjustment: An adjustment to operating income for ratios other than the ROA is necessary if a comparable company has a different relative level of inventory holding than the tested party. The inventory adjustment thus estimates the implicit capital cost of holding inventory ("AVGINV").

(2) Accounts payable adjustment: This adjustment eliminates the implicit interest in the price of goods purchased on other than a cash basis from supplie₹ The purpose of this adjustment is to identify and eliminate from profit comparisons the effect of companies' decisions on how to finance purchases.

(3) Accounts receivable adjustment: This adjustment eliminates the implicit interest in the price of goods or services sold on other tan cash basis to custome₹ The purpose of this adjustment is to identify and eliminate the profit related to finance decisions of the seller. A company selling on cash basis would receive a lower price than a company selling the goods on terms, because selling on terms subjects the seller to a capital cost that will be reflected in the price.

(4) Contractual terms: where the contractual terms includes the provisions like warranties, terms of credit, facilities for transportation and transshipment of goods, facilities related to quantity of purchase or sale of goods.

(5) The level of the market: The adjustments also considers the level of the market, i.e. wholesale, retail, etc.

(6) Foreign currency adjustments: In case of an export transaction, the foreign exchange loss because of depreciation of the USD is disadvantageous to the exporter and it results in lower margin. The comparable companies having domestic sale transactions will be having higher margin. If the tested party imports raw material from foreign company, being an associated enterprise, it will be exposed to foreign exchange risk. The comparable companies using raw material procured from India will not be exposed from this risk. If the comparable companies hedge, the forex risk using financial instruments adjustment for the same is required for the tested party which does not perform the hedging.

Conditions for application of Resale Price Method:

"Where an assessee, being an associated enterprise as per Sec. 92A of the Act had entered into a transaction as per Sec. 92B of the Act, involving transfer of goods or rendering of services as per Sec.92F (v) of the Act, and where it is not possible to compare the transactions even by comparing with the transactions entered by the third party and that the differences have a material effect on price, the Assessing officer shall for the purpose of determining the Arm's Length price having satisfied that the transactions could materially affect the price in the open market and hence comparable; then reasonable adjustments shall be made for such comparable to eliminate the material effects of such differences for the purpose of determining the Arm's Length Price. The adjustments for differences shall be made for:

i) FAR Analysis;

ii) Quality of the product or service;

iii) Contractual terms;

iv) Level of the market;

v) Inventory turnover;

vi) Intangible property associated with the sale;

vii) Foreign currency risks;

viii) Transport costs;

ix) Data and assumptions;

x) Extra ordinary market conditions; and

xi) Other measurable difference."

Accountant's Report:

The arm's length price as computed under this method shall be audited and certified Form No. 3CEB vide Rule 10E.

Steps in Computation of Arm's Length Price as per Resale Price Method:

Step I: Identify the price at which property purchased or services obtained by the enterprise from an associated enterprise are resold or are provided to an **unrelated enterprise.**

Step II: Reduce the normal GP margin accruing to the enterprise or to an unrelated enterprise from the purchase and resale of the same or similar property or from (II) obtaining and providing the same or similar services, in a comparable uncontrolled transaction/(s).

Step III: Reduce expenses incurred by the enterprise in connection with the purchase of property or obtaining of services.

Step IV: Adjust for functional and other differences, including differences in accounting practices, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of gross profit margin in the open market.

Step V: Arm's Length Price = Step I

Less: Step II & III

Add / Less: Step IV.

Computation of Arm's Length Price as per Resale Price Method

No.	Particulars	Amount (₹)
1	Price at which property purchased or services obtained by the enterprise from an associated enterprise are resold or are provided to an **unrelated enterprise.**	XXXX
2	**Add/Less: Adjustments for differences, having material affect on the price in the open market:**	
	i) Adjustments for FAR Analysis	**XXXX**
	ii) Quality of the product or service	**XXXX**
	iii) Characteristics of the Property	**XXXX**
	iv) Contractual terms	**XXXX**
	v) Level of the market	**XXXX**
	vi) Inventory turnover	**XXXX**
	vii) Intangible property associated with the sale	**XXXX**
	viii) Foreign currency risks	**XXXX**
	ix) Data and assumptions	**XXXX**
	x) Extra ordinary market conditions	**XXXX**
3	Arm's Length Price for the purpose of Sec.92C (1 -2)	XXXX

Illustrations on RESALE PRICE METHOD

Illustration 5: Megabyte Inc. of France and R Ltd. of India are associated enterprises. R Ltd. imports 3,000 compressors for Air Conditioners from Megabyte Inc. at ₹7,500 per unit and these are sold to Pleasure Cooling Solutions Ltd at a price of ₹11,000 per unit. R Ltd. had also imported similar products from Cold Inc. Poland and sold outside at a Gross Profit of 20% on Sales.

Megabyte Inc. offered a quantity discount of ₹1,500 per unit. Cold Inc. could offer only ₹500 per unit as Quantity Discount. The freight and customs duty paid for imports from Cold Inc. Poland had cost R Ltd. ₹ 1,200 per piece. In respect of purchase from Cold Inc., R Ltd. had to pay ₹200 only as freight charges.

Determine the Arm's Length Price and the amount of increase in Total Income of R Ltd.

(a) Computation of Arm's Length Price of Products bought from Megabyte Inc., France by R Ltd, India

Particulars	**Amount (₹)**
Resale Price of Goods Purchased from Megabyte Inc.	11,000
Less: Adjustment for Differences –	
a) Normal Gross Profit Margin at 20% of Sale Price [20% x ₹11,000]	2,200
b) Incremental Quantity Discount by Megabyte Inc. [₹1,500 - ₹500]	1,000
c) Difference in Purchase related Expenses [₹ 1,200 - ₹200]	1,000
Arms Length Price	6,800

(b)Computation of Increase in Total Income of R Ltd

Particulars	**Amount (₹)**
Price at which actually bought from Megabyte Inc. of France	7,500
Less: Arms Length Price per unit under Resale Price Method	(6,800)
Decrease in Purchase Price per unit	700
No. of units purchased from Megabyte Inc.	3,000 units
Increase in Total Income (3,000 units x ₹700)	₹21,00,000

Illustration 6:

A Ltd. an Indian company purchases microwave ovens from its parent company situated in US. The same are sold to third party customers in India. The price of the microwave oven set is ₹ 9,000 and the same is sold for ₹ 12,000. A Ltd. also purchases washing machines from another company in UK who is not a related party for ₹ 10,000. The washing machines are sold to customers in India for ₹ 12,000. A Ltd. performs the same functions in case of both purchases of microwave oven and washing machines, that is reselling the goods to the Indian customer. Both the products are sold in the same market and in the same conditions.

Analysis

In this case A Ltd. has transactions with the US Company and the UK Company. The transactions with the US Company are controlled transactions and those with the UK Company are uncontrolled transactions. However, the functions performed in case of both type of transactions are same/similar, that is distributing the same to the third party customers in India without adding any value. Further, the product purchased from US Company and from UK Company are both consumer durables. Though the products need not be similar but the functions are similar and both products broadly fall within the same industry (the white goods industry segment).

Hence, for the purpose of RPM, these transactions can be taken as the basis of comparison. The RPM for this product would be calculated as under:

Particulars	Microwave Oven (₹)	Washing Machine (₹)
Sale Value	12,000	12,000
Cost of Goods Sold	9,000	10,000
Other Expenses	1,500	1,000
Gross Profit (GP)	1,500	1,000
Gross Profit Margin (%)	12.5	8.33

In this case the gross profit margin in case of purchases made from related party is higher as compared to the margin in respect of purchases made from the unrelated party. Hence the controlled transactions are at Arm's Length.

Method 3: Computation of Arm's Length Price:

COST PLUS METHOD (CPM)

The cost plus method determines an arm's length price by adding an appropriate gross profit margin to an associated entity's costs of producing products or services. The gross profit margin should reflect the functions performed by an entity and should include a return for capital used and risks accepted by the entity. The gross profit margin for a controlled transaction is calculated by reference to the gross profit margins made in comparative uncontrolled transactions.

Rule 10B (1) (c) of the Income Tax Rules read with sub-section (2) of Section 92C, the Cost Plus Method (CPM) method is described as under:

(i) the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an AE, are determined;

(ii) the amount of a normal gross profit mark-up to such costs (computed according to the same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction, or a number of such transactions, determined;

(iii) the normal gross profit mark-up referred to in sub-clause (ii) is adjusted to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market;

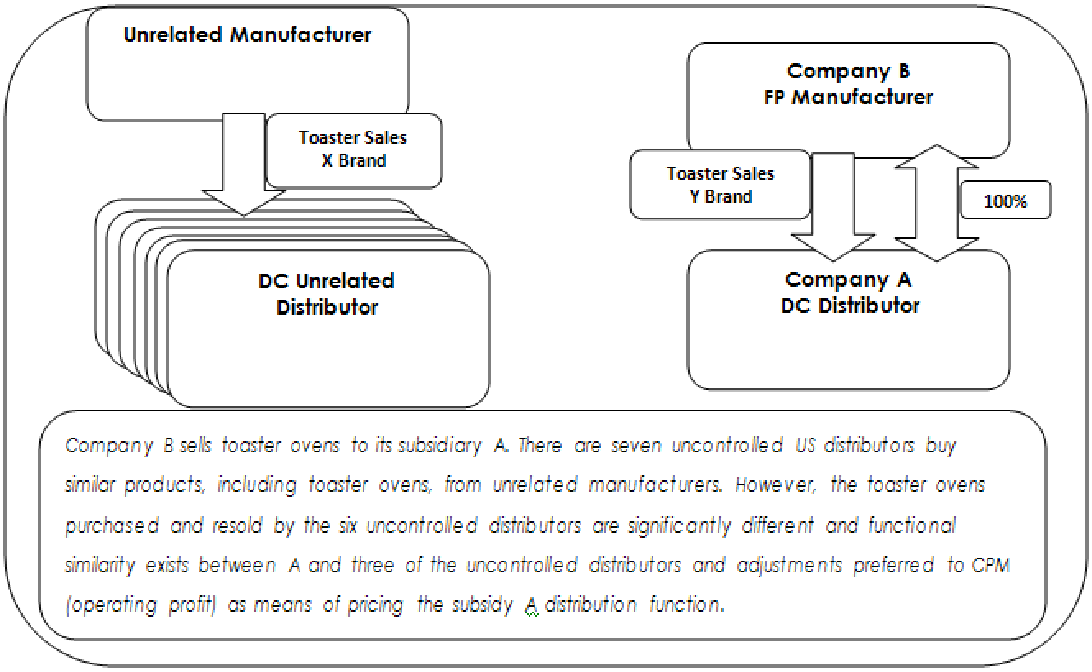
(iv) the cost referred to in sub-clause (i) are increased by the adjusted profit mark-up arrived at under sub-clause (iii);

(v) the sum so arrived at is taken to be an ALP in relation to the supply of the property or provision of services by the enterprise.[3]

3 *Definition of CPM as per OECD Guidelines:*

"A transfer pricing method using the costs incurred by the supplier of property (or services) in a controlled transaction. An appropriate cost plus mark up is added to this cost, to make an appropriate profit in light of the functions performed (taking into account assets used and risks assumed) and the market conditions. What is arrived at after adding the cost plus mark up to the above costs may be regarded as an ALP of the original controlled transaction."

Scope:



Application of CPM:

1) The CPM is ordinarily used where:

2) Semi finished goods are sold between related parties;

3) Contract/Toll Manufacturing arrangements;

4) Long-term buy — and supply arrangements have been entered; and

5) Services are provided.

Special consideration while applying the CPM:

1) The third party comparable mark-up on a comparable cost. For example, if the supplier to which reference is made in applying the cost plus method in carrying out its activities uses leased business assets, the cost basis may not be comparable without adjustment if the supplier in the controlled transaction owns its business assets.

2) The differences in the level and type of expenses should also be considered while applying the CPM.

3) The assets employed and functions performed by the parties have also to be taken into account while applying the CPM.

4) Appropriate adjustments should be made to ensure that there is accounting consistency between the controlled and uncontrolled transactions.

5) The mark-ups must be measured consistently between the associated enterprises and the independent enterprises.

6) If the tested party employs valuable and unique assets, it would be difficult to apply this method, as comparables may not be available.

Degree of Reliability:

The application of CPM is less likely to be reliable if material differences exist between the controlled and uncontrolled transactions with respect to:

1) intangibles;

2) cost structure;

3) business experience;

4) management efficiency;

5) functions performed; and

6) products.

Adjustments to CPM:

Some of the factors in respect of which adjustments may be required for application of CPM are:

1) Complexity of manufacturing or assembling;

2) Manufacturing, production and process engineering;

3) Procurement, purchasing, and inventory control activities;

4) Testing functions;

5) Selling, general and administrative expenses;

6) Accounting treatment of costs between controlled and uncontrolled transactions

7) Foreign currency risks; and

8) Contractual terms for example scope and terms of warranties provided, sales or purchase volume, credit terms, transport terms

Issues to be considered while applying the CPM

In this method, the direct and indirect costs of production are to be identified. The terms "direct" or "indirect" costs are however not defined. A reference may therefore be made to the industry practice.

In identifying and adopting the direct and indirect costs, the following factors would also have to be borne in mind:

(a) utilisation of the plant; for example, if the plant has been under-utilised;

(b) method of absorbing costs; absorption costing method is normally to be preferred;

(c) in abnormal situations, marginal-costing principles may have to be applied; for example, use of incremental costing or marginal costing can be applied.

Under the Indian Companies Act, there is no requirement to report distinctly the gross profits of companies. Thus, there is no consistency in the accountancy practices across the industry. The non-availability of gross margins of comparable companies from public databases makes the application of this method rare, and hence in practice this method is rarely used for testing the controlled transactions.

Conditions for application of Cost Plus Method:

"Where an assessee, being an associated enterprise as per Sec. 92A of the Act had entered into a transaction as per Sec. 92B of the Act, involving transfer of goods or rendering of services as per Sec.92F (v) of the Act, and where

(i) Semi-finished goods are sold between related parties;

(ii) Contract/toll manufacturing arrangements;

(iii) Long-term buy- and supply arrangements have been entered; and

(iv) Services are provided;

the Assessing officer, for the purpose of determining the Arm's Length price, to eliminate the effect on valuation, shall cause to make appropriate adjustments to ensure accounting consistency between the controlled and uncontrolled transactions, considering the third party comparable mark-up on a comparable cost.

The adjustments for differences shall be made for:

i) FAR Analysis;

ii) Complexity of manufacturing or assembling;

iii) Characteristics of the Property;

iv) Manufacturing, production and process engineering;;

v) Procurement, purchasing and inventory control activities;

vi) Testing functions;

vii) Selling, general and administrative expenses;

viii) Accounting treatment of costs between controlled and uncontrolled transactions;

ix) Intangible property associated with the sale;

x) Foreign currency risks;

xi) Contractual terms"

Accountant's Report:

The arm's length price as computed under this method shall be audited and certified in Form No. 3CEB vide Rule 10E.

Steps in Computation of Arm's Length Price using Cost Plus Method

Step I: Determine the direct and indirect costs of production incurred by the enterprise in respect of property transferred or services provided to an associated enterprise.

Step II: Determine the normal GP mark-up to such costs (computed under same accounting norms) arising from the transfer or provision of the same or similar property or services by the enterprise, or by an unrelated enterprise, in a comparable uncontrolled transaction(s).

Step III: Adjust the normal gross profit mark-up referred to in Step II to take into account the functional and other differences, if any, between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect such profit mark-up in the open market.

Step IV: Arm's Length Price = Step I **Add** Step III

Computation of Arm's Length Price as per Cost Plus Method

No.	Particulars	Amount (₹)
1	Price at which property purchased or services obtained by the enterprise from an associated enterprise are resold or are provided to an **unrelated enterprise.**	XXXX
2	**Add/Less: Adjustments for differences, having material affect on the price in the open market:**	
	i) Adjustments for FAR Analysis	**XXXX**
	ii) Quality of the product or service	**XXXX**
	iii) Characteristics of the Property	**XXXX**
	iv) Contractual terms	**XXXX**
	v) Level of the market	**XXXX**
	vi) Inventory turnover	**XXXX**
	vii) Intangible property associated with the sale	**XXXX**
	viii) Foreign currency risks	**XXXX**
	ix) Data and assumptions	**XXXX**
	x) Extra ordinary market conditions	**XXXX**
3	Arm's Length Price for the purpose of Sec.92C (1 -2)	XXXX

Illustrations on COST PLUS METHOD

Illustration 7: Branco Inc., French Company, holds 45% of Equity in the Indian Company Chirag Technologies Ltd (CTL). CTL is engaged in development of software and maintenance of the same for customers across the globe. Its clientele includes Branco Inc. During the year, CTL had spent 2,400 Man Hours for developing and maintaining software for Branco Inc, with each hour being billed at ₹1,300. Costs incurred by CTL for executing work for Branco Inc. amount to ₹ 20,00,000.

CTL had also undertaken developing software for Harsha Industries Ltd for which CTL had billed at ₹2,700 per Man Hour. The persons working for Harsha Industries Ltd. and Branco Inc. were part of the same team and were of matching credentials and caliber. CTL had made a Gross Profit of 60% on the Harsha Industries work.

CTL's transactions with Branco Inc. are comparable to the transactions with Harsha Industries, subject to the following differences:

a) Branco Inc. gives technical know-how support to CTL which can be valued at 8% of the normal gross profit. Harsha Industries does not provide any such support.

b) Since the work for Branco involved huge number of man hours, a quantity discount of 14% of Normal Gross Profits was given.

c) CTL had offered 90 Days credit to Branco the cost of which is measured at 2% of the Normal Billing Rate, No such discount was offered to Harsha Industries Ltd.

Compute ALP and the amount of increase in Total Income of Chirag Technologies Ltd.

(a) Computation of Arms Length Gross Profit Mark Up

Particulars	**%**	**%**
Normal Gross Profit Mark Up		**60.00**
Less: Adjustment for differences:(which had the effect of reducing the profit of CTL)		
(i)Technical support from Branco Inc. (8% of Normal Gross Profit 60%)	4.80	
(ii)Quantity Discount @ 14% of Normal Gross Profit (14% of 60%)	8.40	**13.20**
Normal Gross Profit Rate of CTL, had the transaction been unrelated and there been no technical support or quantity discount		46.80
Add: Cost of Credit to Branco Inc. @2% of Normal Gross Profit (2% of Gross Profit 60%) [since this had effect of reducing the gross profit of CTL]		1.20
Arms Length Gross Profit Mark-up		48.00

(b) Computation of Increase in Total Income of CTL for services to Branco Inc.

Particulars	**Amount (₹)**
Cost of Services provided to Branco	20,00,000
Billed Value at Arm's Length [Cost / (100 – Arm's Length Mark) = [₹20,00,000/ (100% -48%]	38,46,154
Less: Actual Billing to Branch Inc. [2,400 x 1,300]	31,20,000
Increase in Total Income of Branco Inc.	7,26,154

Illustration 8:

Indco, an Indian company, manufactures specialized stamping equipment for uncontrolled companies in the manufacturing industry using designs supplied to them by the arm's length parties. Indco realizes its costs plus a mark-up of 8% on this custom manufacturing. Under the arm's length agreements, costs are defined as the sum of direct costs (i.e., labour and materials) plus 50% of the direct costs. The additional 50% of direct costs is intended to approximate indirect costs, including overhead. Indco also manufactures stamping machines for its Chinese subsidiary, Chco, using designs supplied by Chco. Under the Chco agreement, costs are defined as the sum of the direct costs plus the indirect costs, including overhead is also computed at 50% of direct costs, and the mark-up earned is 10% of the direct and indirect costs.

The cost plus mark up is calculated as follows:

Calculation of mark-up under the uncontrolled transaction

Particulars	Amount(₹)
Direct costs	1,000
Indirect costs(50% * 1,000)	500
Total costs	1,500
Mark-up 8%	120

Calculation of mark-up under the controlled transaction

Particulars	Amount(₹)
Direct costs	3,000
Indirect costs (50% * 1,000)	1,500
Total costs	4,500
Mark-up earned on controlled transactions at 10%	450

Calculation of arm's length cost mark up

Cost plus markup from uncontrolled transactions 8%

Cost plus mark up from controlled transactions 10%

Thus the controlled transactions are at Arm's Length.

However, in practice, globally it is found that it is not feasible to apply this method.

Illustration 9: Happy Ltd. , an Indian Company is a wholly-owned subsidiary of Happy Inc. Happy Ltd. is engaged in provision of software development services to its associated enterprise Happy Inc. The following is the income statement if Happy Ltd. for the year ended 31.3.2016

Happy Ltd.	**All figures in Rupees '000**
Revenue from associated enterprises	
- Total operating income	95,000
Costs	
- Pay roll	40,000
- Rent	16,500
- Depreciation	9,500
- General administration expenses	8,200
- Other operating expenses	11,800
Total operating expenses	86,000
Operating profit	9,000

Net Cost plus mark-up (%) [Operating profit /total operating expenses] 10.46%

Conclusion: *For the financial year ended 31st March, 2016, Happy Ltd has earned a Net Cost Plus mark-up of 10.46% from its associated enterprises. Accordingly, it is reasonable to conclude that Happy Ltd's international transactions with Happy Inc., relating to the provision of software services, appears to be consistent with the arm's length standard from the Indian transfer pricing perspective.*

Use of multi-year data

As per Rule 10B (4), *the use of the data relating to the financial year in which such international transaction has been entered into, must be considered. Data for earlier years may also be used, if such data reveals facts, which could have an influence on the determination of transfer prices in relation to the transactions being compared.*

The purpose of using multiple-year data is to ensure that the outcomes for the relevant year

Implications of tested party earning lower than arm's length mark-up

If Happy Ltd's actual mark-up is less than the arm's length mark-up benchmark of 11.77%, it would need further examination as to whether it is compliant with the arm's length standard from an Indian Transfer pricing perspective. We may have two different scenarios:

Scenario 1: where Happy Ltd's margin is below the arm's length mark-up but within the range permissible under the proviso to Sec.92C (2)

Scenario 2: Where Happy Ltd's margin falls below the lower limit of the range of permissible under the proviso.

The calculation of range of permissible margins applying the proviso is shown in Table A. The arithmetic mean of 11.77% is applied to the costs of the tested party (₹86,000) to derive the arm's length price of the international transaction (refer col.2 –figure indicated as ALP ₹ 96,122) is a balancing figure and refers to the arm's length price of the international transaction.

The adjustment of (+/-) 3 percent as permitted by Safe Harbour Rules is applied to the ALP to give the range of values that would be considered at arm's length. Further, as the international transactions consists of export of services, the lower end of the range is 97% of ALP ₹93,238 *(Col.4) representing the lowest possible transaction value that would be considered compliant with the arm's length principle.*

Table A

Calculation of Range of outcomes that would meet the arm's length standard applying the proviso to Section 92C (2)

Profit & Loss Account for the year ended 31st March, 2016 [All figures in Rupees '000]

Particulars	Col. 1	Col. 2			Col.3		Col.4	
	Actual	At ALP	Refer Note No.		At ALP (+) 3% of ALP		At ALP (-)3% of ALP	
(a) Revenue								
-From associated enterprises (international transaction)	95,000	96,122	2	ALP	1,00,928	ALP (+)3%	93,238	ALP (-) 3%
Total Operating Income	95,000	96,122			1,00,928		93,238	
(b)Costs (all unrelated, no international <u>transactions)</u>								
Pay roll	40,000	40,000			40,000		40,000	
Rent	16,500	16,500			16,500		16,500	
Depreciation	9,500	9,500			9,500		9,500	
General administration exp.	8,200	8,200			8,200		8,200	
Other operating expenses	11,800	11,800			11,800		11,800	
Total Operating expenses	**86,000**	**86,000**			**86,000**		**86,000**	
(c)**Operating Profit**[=(a) – (b)]	9,000	10,122	1		14,928		7,238	
Net Cost Mark-up (%)	10.46%							
Arm's length mark-up [i.e. arithmetical mean of the Net Cost Plus mark-up(%) of broadly comparable independent companies]		11.77%						
Range of net cost plus mark-ups that would be considered compliant with the arm's length standard applying the +/- 3% variation permitted by proviso to Sec.92C(2) [= Operating Profit / Operating expenses]					17.36%		8.42%	

Notes:

1. Operating profit in Col.2 is a derived figure by applying mark-up of 11.77% to the tested party's total operating expenses of ₹86,000
2. (a) Revenue from associated enterprises (international transaction) in Col.2 is the balancing figure considering operating profit derived in Col.1 above and the total operating expenses remaining unchanged at ₹86,000. This revenue figure is the Arm's Length Price (ALP).
   (b) Revenue from associated enterprises (international transaction) in Col.3 represents the upper limit of the range permissible under the proviso the Section 92C(2)
   (c) Revenue from associated enterprises (international transaction) in Col.4 represents the lower limit of the range permissible under the proviso the Section 92C(2)
3. The Net Cost Plus Mark-up earned by the tested party (col.1) is higher than the arm's length mark-up (col.2), accordingly the international transaction complies with the arm's length principle.

Workings: Computation of Weighted Net Cost-plus mark-ups of broadly comparable independent companies. (on the basis of hypothetical data of 5 such companies for 5 years)

Comparable Company 1 (₹ In Crores)

Profit and Loss Account (Summary) year ended…..

Comparable 1	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	125	143	155	134	175	732
(3)Total Cost	118	129	140	128	159	674
(4)Net profit [=(2) – (3)]	7	14	15	6	16	58
(5)Net cost plus mark-up [=(4)/(3) *100]	5.93%	10.8%	10.71%	4.69%	10.06%	—
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	—	—	—	—	—	8.61%

Comparable Company 2 (₹ In Crores)

Profit and Loss Account (Summary) year ended…..

Comparable 2	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	152	134	155	143	157	741
(3)Total Cost	118	129	140	128	135	674
(4)Net profit [=(2) – (3)]	34	5	15	15	22	91
(5)Net cost plus mark-up [=(4)/(3) *100]	28.81%	3.88%	10.71%	11.72%	16.30%	—
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	—	—	—	—	—	13.50%

Comparable Company 3 (₹ In Crores)

Profit and Loss Account (Summary) year ended…..

Comparable 3	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	15	13	15	14	17	74
(3)Total Cost	13	12	14	12	15	66

(4)Net profit [=(2) – (3)]	2	1	1	2	2	8
(5)Net cost plus mark-up [=(4)/ (3) *100]	15.38%	8.33%	7.14%	16.67%	13.33.%	—
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	—	—	—	—	—	12.12%

Comparable Company 4 (₹ In Crores)

Profit and Loss Account (Summary) year ended…..

Comparable 4	**March 2012**	**March 2013**	**March 2014**	**March 20015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	215.38	183.68	176.85	244.73	267.57	1088.21
(3)Total Cost	191.21	162.55	169.29	212.11	223.34	958.50
(4)Net profit [=(2) – (3)]	24.17	21.13	7.56	32.62	44.23	129.71
(5)Net cost plus mark-up [=(4)/ (3) *100]	12.64%	13.00%	4.47%	15.38%	19.80%	—
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	—	—	—	—	—	13.53%

Comparable Company 5 (₹ In Crores)

Profit and Loss Account (Summary) year ended…..

Comparable 5	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	231.15	138.89	157.86	424.37	327.75	1280.02
(3)Total Cost	211.29	132.46	129.19	392.21	303.34	1168.49
(4)Net profit [=(2) – (3)]	19.86	6.43	28.67	32.16	24.41	129.71
(5)Net cost plus mark-up [=(4)/ (3) *100]	9.40%	4.85%	22.19%	8.20%	8.05%	----
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	----	----	----	----	----	11.10%

Summary of Net Cost plus Mark-ups of broadly comparable independent companies

Sl No.	**Company name**	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Weighted average**
1	Comparable 1	5.93%	10.8%	10.71%	4.69%	10.06%	8.61%
2	Comparable 2	28.81%	3.88%	10.71%	11.72%	16.30%	13.50%
3	Comparable 3	15.38%	8.33%	7.14%	16.67%	13.33.%	12.12%
4	Comparable 4	12.64%	13.00%	4.47%	15.38%	19.80%	13.53%
5	Comparable 5	9.40%	4.85%	22.19%	8.20%	8.05%	11.10%
	Arithmetic Mean	14.43%	8.17%	11.04%	11.33%	13.51%	11.77%

Conclusion: On the basis of the above, the Net Cost-plus mark-ups of broadly comparable independent companies range from 8.61% to 13.53% with an arithmetical mean of 11.77%.

Scenario 1: *where Happy Ltd's margin is below the arm's length mark-up but within the range permissible under the proviso to Sec.92C (2)*

Profit & Loss Account for the year ended 31st March, 2016 [All figures in Rupees '000]

Particulars	Col. 1	Col. 2			Col.3		Col.4	
	Actual	**At ALP**	**Refer Note No.**		**At ALP (+) 3% of ALP**		**At ALP (-) 3% of ALP**	
(a) Revenue								
-From associated enterprises (international transaction)	**93,500**	**96,122**	**2**	**ALP**	**1,00,928**	**ALP (+)3%**	**93,238**	**ALP (-) 3%**
Total Operating Income	**93,500**	**96,122**			**1,00,928**		**93,238**	
(b)Costs (all unrelated, no international <u>transactions)</u>								
Pay roll	40,000	40,000			40,000		40,000	
Rent	16,500	16,500			16,500		16,500	
Depreciation	9,500	9,500			9,500		9,500	
General administration exp.	8,200	8,200			8,200		8,200	
Other operating expenses	11,800	11,800			11,800		11,800	
Total Operating expenses	**86,000**	**86,000**			**86,000**		**86,000**	
(c)**Operating Profit**[=(a) – (b)]	**7,500**	**10,122**	**1**		**14,928**		**7,238**	
Net Cost Mark-up (%)	**8.72%**							
Arm's length mark-up [i.e. arithmetical mean of the Net Cost Plus mark-up(%) of broadly comparable independent companies]		**11.77%**						
Range of net cost plus mark-ups that would be considered compliant with the arm's length standard applying the +/- 3% variation permitted by proviso to Sec.92C(2) [= Operating Profit / Operating expenses]					**17.36%**		**6.42%**	

Notes:

1. Operating profit in Col.2 is a derived figure by applying mark-up of 11.77% to the tested party's total operating expenses of ₹86,000

2. (a) Revenue from associated enterprises (international transaction) in Col.2 is the balancing figure considering operating profit derived in Col.1 above and the total operating expenses remaining unchanged at ₹ 86,000. This revenue figure is the Arm's Length Price (ALP).

   (b) Revenue from associated enterprises (international transaction) in Col.3 represents the upper limit of the range permissible under the proviso the Section 92C(2)

   (c) Revenue from associated enterprises (international transaction) in Col.4 represents the lower limit of the range permissible under the proviso the Section 92C(2)

3. The Net Cost Plus Mark-up of 8.72% earned by the tested party (col.1) even though below the arm's length Net Cost plus mark-up (col.2), still falls within the range permissible under the proviso to Section 92C(2) [Col.(3) & (4)] . Hence no adjustment needs to be made.

Scenario 2: Where Happy Ltd's margin falls below the lower limit of the range of permissible under the proviso

Profit & Loss Account for the year ended 31st March, 2016 [All figures in Rupees '000]

Particulars	Col. 1	Col. 2			Col.3		Col.4	
	Actual	**At ALP**	**Refer Note No.**		**At ALP (+) 3% of ALP**		**At ALP (-) 3% of ALP**	
(a) Revenue								
-From associated enterprises (international transaction)	91,000	96,122	2	ALP	1,00,928	ALP (+) 3%	93,238	ALP (-) 3%
Total Operating Income	91,000	96,122			1,00,928		93,238	
(b)Costs (all unrelated, no international <u>transactions)</u>								
Pay roll	40,000	40,000			40,000		40,000	
Rent	16,500	16,500			16,500		16,500	
Depreciation	9,500	9,500			9,500		9,500	
General administration exp.	8,200	8,200			8,200		8,200	
Other operating expenses	11,800	11,800			11,800		11,800	
Total Operating expenses	**86,000**	**86,000**			**86,000**		**86,000**	
(c)**Operating Profit**[=(a) – (b)]	5,000	10,122	1		14,928		7,238	
Net Cost Mark-up (%)	5.82%							
Arm's length mark-up [i.e. arithmetical mean of the Net Cost Plus mark-up(%) of broadly comparable independent companies]		11.77%						
Range of net cost plus mark-ups that would be considered compliant with the arm's length standard applying the +/- 3% variation permitted by proviso to Sec.92C(2) [= Operating Profit / Operating expenses]					17.36%		8.42%	

Notes:

1. Operating profit in Col.2 is a derived figure by applying mark-up of 11.77% to the tested party's total operating expenses of ₹86,000
2. (a) Revenue from associated enterprises (international transaction) in Col.2 is the balancing figure considering operating profit derived in Col.1 above and the total operating expenses remaining unchanged at Rs 86,000. This revenue figure is the Arm's Length Price (ALP).

   (b) Revenue from associated enterprises (international transaction) in Col.3 represents the upper limit of the range permissible under the proviso the Section 92C (2)

(c) Revenue from associated enterprises (international transaction) in Col.4 represents the lower limit of the range permissible under the proviso the Section 92C (2)

3. The Net Cost Plus Mark-up earned by the tested party (col.1) falls below the lower limit of the range permissible under proviso 92C(2) [Col.(4)] . This situation may expose the tested party to an adjustment to the price charged by it in its international transaction. Such adjustment, if recommended to be made by the TPO to the AO should amount to ₹2,238 As explained hereunder.

4. Quantum of adjustment:

(i)	Value of the international transaction	91,000
(ii)	Arm's length price	96,122
(iii)	Arm's length price applying the proviso to Sec. 92C(2)	93,238
(iv)	Adjustment (iii) – (i)	2,238

Method 4: Computation of Arm's Length Price:

PROFIT SPLIT METHOD (PSM)

The PSM evaluates whether the allocation of the combined operating profit or loss attributable to one or more controlled transactions is arm's length with reference to the relative value of each controlled taxpayer's contribution to that combined operating profit or loss.

The combined operating profit or loss must be derived from the most narrowly identifiable business activity of the controlled taxpayers for which data is available that includes the controlled transactions.

Objective of PSM:

1) To determine the relative value of each controlled taxpayer's contribution;

2) To assess the impact of the controlled taxpayer's contribution on the success of the relevant business activity;

3) To identify and evaluate the impact of the controlled taxpayer's contribution that reflects the functions performed, risks assumed, and resources employed.

4) To eliminate the effect on profits of special conditions made or imposed in a controlled transaction (or in controlled transactions that are appropriate to aggregate) by determining the division of profits that independent enterprises would have expected to realize from engaging in the transaction or transactions.

5) To identify the profit to be split for the associated enterprises from the controlled transactions in which the associated enterprises are engaged.

6) To allocate the profits between the associated enterprises on an economically valid basis that approximates the division of profits that would have been anticipated and reflected in an agreement made at arm's length.

The Indian TPR regulations provide that PSM is mainly applicable to international transactions involving transfer of unique intangibles or in multiple international transactions which are so interrelated that they cannot be evaluated separately for the purpose of determining the arm's length price.

Rule 10B (1)(d) of the Income Tax Rules read with sub-section (2) of Section 92C, the Profit Split Method (PSM) method is described as under:

(i) the combined net profit of the AE arising from the international transaction in which they are engaged, is determined;

(ii) the relative contribution made by each of the AE to the earning of such combined net profit, is then evaluated on the basis of the functions performed, assets employed or to be employed and risks assumed by each enterprise and on the basis of reliable external market data which indicates how such contribution would be evaluated by unrelated enterprises performing comparable functions in the similar circumstances;

(iii) the combined net profit is then split amongst the enterprises in proportion to their relative contributions, as evaluated under sub-clause (ii);

(iv) the profit thus apportioned to the assessee is taken into account to arrive at an ALP in relation to the international transaction.[4]

Terms Used:

(1) Comparable Residual Profit: A comparable profit split is derived from the combined operating profit of the uncontrolled taxpayers whose transactions and activities are similar to those of the controlled taxpayers in the relevant business activity.

(2) Residual Profit Split: This is the residual profit which is apportioned to each party based on ownership of non-routine intangibles (i.e. network reach, efficiency of Sales & Marketing team, etc)

(3) Contribution Analysis: Under this approach, the combined profits, which are the total profits from the uncontrolled transactions under examination, would be divided between the AEs based upon the relative value of the functions performed by each of the AEs participating in the controlled transaction, supplemented as much as possible by external market data that indicate how independent enterprises would have divided the profits in similar circumstances.

Residual Analysis: Under this analysis, the combined profit from controlled transactions under examination in two stages. In the first stage, each participant is allocated sufficient profit to provide it with a basic return appropriate for the type of transactions in which it is engaged. In the second stage, any residual profit (or loss) remaining after the first stage division would be allocated among the parties based on an analysis of facts and circumstances that might indicate how this residual profit would have been divided between independent enterprises.

Applicability of PSM (Profit Split Method)

The Indian TPR affirms that the PSM may be applicable mainly in the following cases:

a) Transactions involving transfer of unique intangibles;

b) Multiple inter-related international transactions which cannot be evaluated separately for determining the ALP of any one transaction.

(i) The extent of economies of backward and forward integration, the existence of intangibles on both sides of the transaction, and complex functional and transactional structures may limit the use of standard approaches to economic analysis for transfer pricing purposes (i.e. performing comparable company searches to apply the TNMM). In those circumstances, the arm's length nature of transactions may be better evaluated by considering the transaction from an end-to-end perspective, and thus PSM can be applied.

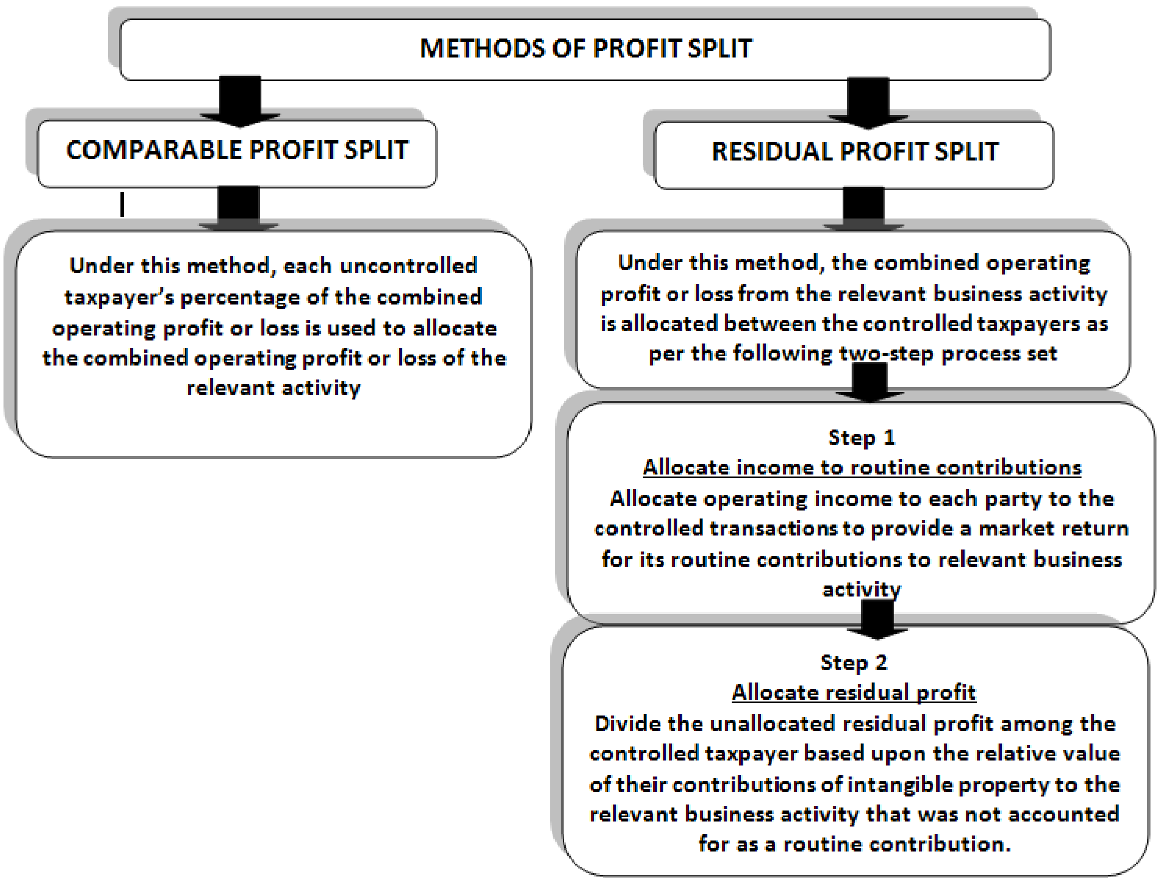
(ii) This method can be used in situations where economies of integration differentiate the tested party from the comparables, provided these are taken into account in the principle for

4 *Definition of PSM as per* ***OECD Guidelines:***
"A transactional profit method that identifies the combined profit to be split for the associated enterprises from a controlled transaction (or controlled transactions that is appropriate to aggregate) and then splits those profits between the associated enterprises based upon an economically valid basis that approximates the division of profit that would have been anticipated and reflected in an agreement made at arm's length."

allocating profits. The method enables accounting for valuable intangibles being developed on both sides of the transaction.

(iii) The allocation of profit can be calculated based on principles that take into account the contribution of intangibles in the industry's or the group's value creation process.

(iv) This method is also well suited to complex transactions where several entities are involved in the same functions and it is not possible to define precisely the scope of functions and responsibilities. While this method has not been widely used, it has been somewhat popular in the financial services industry.



Conditions for application of Profit Split Method (PSM):

"Where an assessee, being an associated enterprise as per Sec. 92A of the Act had entered into a transaction as per Sec. 92B of the Act, involving transfer of goods or rendering of services as per Sec.92F (v) of the Act, and where it is not possible to compare the transactions even by comparing with the transactions entered by the third party and that the differences have a material effect on price, the Assessing officer shall for the purpose of determining the Arm's Length price having satisfied that the transactions could materially affect the price in the open market and hence comparable; then reasonable adjustments shall be made for such comparable to eliminate the material effects of such differences for the purpose of determining the Arm's Length Price. The adjustments for differences shall be made for:

i) FAR Analysis;

ii) Quality of the product or service;

iii) Contractual terms;

iv) Level of the market;

v) External Data and Internal Data;

vi) Estimation of projected profits;

vii) Contribution Analysis;

viii) Residual Analysis."

Accountant's Report:

The arm's length price as computed under this method shall be audited and certified in Form No. 3CEB vide Rule 10E.

Steps in computation of Arm's Length Price using Profit Split Method:

This method is mainly applicable in international transactions involving transfer of unique intangibles or in multiple international transactions which are so inter-related that they cannot be evaluated separately for the purpose of determining the Arm's Length Price of any one transaction.

Step I: Determine the combined net profit of the associated enterprises arising from the international transaction in which they are engaged.

Step II: Determine the relative contribution made by each of the associated enterprises to the earning of such combined net profit. This is determined on the basis of the **FAR** Analysis:

(a) **F**unctions performed;

(b) **A**ssets employed;

(c) **R**isks assumed by each enterprise;

(d) on the basis of reliable external market data which indicates how such contribution would be determined by unrelated enterprises performing comparable functions in similar circumstances.

Step III: Split the combined net profit amongst the enterprises on the basis of reasonable returns and in proportion to their relative contributions, as determined in Step II. (**See note below**)

Step IV: Arm's Length Price **-** Profit apportioned to the assessee under Step III.

NOTE: Combined Net Profit shall be split as under:

III.A. First Split = Reasonable Return: Allocate an amount to each enterprise so as to provide it with a basic return appropriate for the type of international transaction with reference to market returns achieved in similar types of transactions by independent enterprises.

III.B. Second Split = Contribution Ratio: Allocate the residual net profit amongst the enterprises in proportion to their relative contribution.

III.C. Total Profit: Share of profit of each enterprise = **Step III.A + III.B**

Computation of Arm's Length Price as per Profit Split Method (PSM)

No.	Particulars	Amount (₹)
1	Price at which property purchased or services obtained by the enterprise from an associated enterprise are resold or are provided to an **unrelated enterprise.**	XXXX
2	Add/Less: Adjustments for differences, having material affect on the price in the open market:	
	i) Adjustments for FAR Analysis	**XXXX**
	ii) Quality of the product or service	**XXXX**
	iii) Contractual terms	**XXXX**
	iv) Level of the market	**XXXX**
	v) External data and internal data	**XXXX**
	vi) Estimation of projected profits	**XXXX**
	vii) Contribution Analysis	**XXXX**
	viii) Residual Analysis	**XXXX**
3	Arm's Length Price for the purpose of Sec.92C (1 -2)	XXXX

Illustrations on PROFIT SPLIT METHOD

Illustration 10: NBR Medical Equipments Inc. (NBR) of Canada has received an order from a leading UK based Hospital for development of a hi-tech medical equipment which will integrate the best of software and latest medical examination tool to meet varied requirements. The order was for 3,00,000 Euros. To execute the order, NBR joined hands with its subsidiary Precision Components Inc. (PCI) of USA and Bioinformatics India Ltd (BIL), an Indian Company. PCI holds 30% of BIL. NBR paid to PCI and BIL Euro 90,000 and Euro 1,00,000 respectively and kept the balance for itself. In the entire transaction, a profit of Euro 1,00,000 is earned. Bioinformatics India Ltd incurred a Total Cost of Euro 80,000 in execution of its work in the above contract. The relative contribution of NBR, PCI and BIL may be taken at 30%, 30% and 40% respectively. Compute the Arm's Length Price and the incremental Total Income of Bioinformatics India Ltd, if any due to adopting Arms Length Price determined here under.

A	Share of each of the Associates in the Value of the Order	**3,00,000**
	Share of BIL [Given]	**1,00,000**
	Share of PCI [Given]	90,000
	Share of NBR [Amount Retained = 3,00,000 – 1,00,000 - 90,000]	1,10,000
B	**Share of each of the Associates in the Profit of the Order**	
	Combined Total Profits	**1,00,000**
	Share of BIL [Contribution of 40% x Total Profit € 1,00,000]	40,000
	Share of PCI [Contribution of 30% x Total Profit € 1,00,000]	30,000
	Share of NBR [Contribution of 30% x Total Profit € 1,00,000]	30,000
C	**Computation of Incremental Total Income of BIL**	
	Total Cost to BIL Ltd	80,000
	Add: Share in the Profit to BIL (from B above)	40,000
	Revenue of BIL on the basis of Arm's Length Price	**1,20,000**
	Less: Revenue Actually received by BIL	(1,00,000)
	Increase in Total Income of BIL	**20,000**

Illustration 11:

Indco, an Indian company, has developed and manufactures a robot to be used for multiple industrial applications. The robot is considered to be an innovative technological advance. Chco, a Chinese subsidiary of Indco, has developed and manufactures a software programme which incorporates the new programme in the robot and makes it more effective. The success of the robot is attributable to both companies for the design of the robot and the software programme.

Indco manufactures and supplies Chco with the robot for installing of the new software programme for assembly and manufacture of the robot. Chco manufactures the robot and sells to an arm's length distributor.

In light of the innovative nature of the robot and software, the group was unable to find comparables with similar intangible assets. Because they were unable to establish a reliable degree of comparability, the group was unable to apply the traditional transaction methods or the TNMM.

However, reliable data are available on robot and software manufacturers without innovative intangible property, and they earn a return of 10% on their manufacturing costs.

The total profits attributable to manufacture of robots are calculated as follows:

Particulars	**Amount (₹)**	**Amount (₹)**
Sales to the arm's length distributor		1,000
Deduct:		
Indco's manufacturing costs	200	
Chco's manufacturing costs	300	
Total manufacturing costs for the group		500
Gross Margin		500
Deduct:		
Indco's development costs	100	
Chco's development costs	50	
Indco's operating costs	50	
Chco's operating costs	100	300
Net profit		200
Indco's return to manufacturing (200 * 10%)		20
Chco's return to manufacturing (300 * 10%)		30
Residual profit attributable to development		150

The split of the residual profit has been considered on the basis of the development cost considering the significance of technology in the manufacturing process.

Based on proportionate development costs

Particulars	(₹)
Indco's share of residual profit [100/)100+50)] * 150	100
Chco's share of residual profit [50/(100+50)] * 150	50

Indco's transfer price is calculated as follows:

Particulars	Amount (₹)
Manufacturing costs	200
Development costs	100
Operating costs	50
Routine 10% return on manufacturing costs	20
Share of residual profit	100
Transfer price	470

Method 5: Computation of Arm's Length Price:

TRANSACTION NET MARGIN METHOD (TNMM)

Under the Transaction Net Margin Method (TNMM), an arm's length price is determined by comparing the operating profit of the "tested party" with the operating profit of an uncontrolled party engaged in comparable transactions. The tested party is the least complex of the controlled tax payers and does not own valuable intangibles that contribute to the resulting profits from its operations. [5]

Objectives of TNMM:

(1) Computation of net profit margin realized y an AE from an international transaction to be made in relation to a particular factor such as costs incurred, sales, assets utilized, etc.

(2) Aggregate the relevant controlled transactions to test whether the controlled transactions earn a reasonable margin as compared to uncontrolled transactions.

(3) Benchmarking the dealings between the tested party and its associated enterprises on the basis of the margins earned by comparable uncontrolled companies.

Rule 10B (1)(e) of the Income Tax Rules read with sub-section (2) of Section 92C, the Transaction Net Margin Method (TNMM) is described as under:

(i) the net profit margin realised by the enterprise from an international transaction entered into with an AE is computed in relation to costs incurred or sales effected or assets employed or to be employed by the enterprise or having regard to any other relevant base;

(ii) the net profit margin realised by the enterprise or by an unrelated enterprise from a comparable uncontrolled transaction or a number of such transactions is computed having regard to the same base;

(iii) the net profit margin referred to in sub-clause (ii) arising in comparable uncontrolled transactions is adjusted to take into account the differences, if any, between the international transactions and the comparable uncontrolled transactions, or between the enterprises entering into such transactions, which could materially affect the amount of net profit margin in the open market;

(iv) the net profit margin realised by the enterprise and referred to in sub-clause (i) is established to be the same as the net profit margin referred to in sub-clause (iii);

5 The OECD Guidelines states that TNMM may be particularly sensitive to differences in business structure or management effectiveness between the controlled entities and the tested party, as these factors are likely to impact the operating profits generated across different entities.

(v) the net profit margin thus established is then taken into account to arrive at an ALP in relation to the international transaction."[6]

Application of the TNMM

i) An analysis under the TNMM considers the profits of the associated enterprise that are attributable to the company as a whole or to similar functional activities, e.g., manufacturing, trading, etc. TNMM requires establishing comparability at a broad functional level, for example trading function, manufacturing activities, etc.

ii) Only one party to the controlled transaction is analysed in applying TNMM. The party to the international transaction whose profitability is examined is known as the tested party.

iii) The choice of the tested party depends upon the availability of the data. In general, TNMM is applied to the least complex of the entity involved in the controlled transaction. There are usually more comparable data available in respect of the least complex entities, and fewer adjustments would be required to account for the differences in the functions and risk between the controlled and uncontrolled transactions.

iv) TNMM requires comparison between net margins derived from the operations of the uncontrolled parties and net margins derived by an AE from similar operations. Net margin is indicated by the rate of return on sales or cost or operating assets, and this forms the basis for TNMM.

v) A functional analysis of the tested party or the independent enterprise, as the case may be, is required to determine whether the transactions are comparable and the adjustments that are required to be made to obtain reliable results. The tested party would have to consider other factors, like cost of assets of comparable companies, etc. while applying the return on assets measure.

Steps in computation of Arm's Length Price using Transaction Net Margin Method

Step I: Compute the net profit margin realised by the enterprise from an international transaction entered into with an associated enterprise, in relation to costs incurred or sales effected or assets employed by enterprise or having regard to any other relevant base.

Step II: Compute the net profit margin realised by the enterprise or by an unrelated enterprise from a **comparable uncontrolled transaction (s),** having regard to the same base as in Step I.

Step III: Adjust the net profit margin as per Step II for differences, if any, which could materially affect amount of net profit margin in the open market:

(a) between the international transaction and the comparable uncontrolled transactions, or

(b) between the enterprises entering into such transactions.

Step IV: Net Profit Margin for uncontrolled transactions = Step II **Add/Less** Step III.

Step V: Arm's Length Price = Transaction Value x Net Profit Margin as per Step IV above.

Meaning of certain terms: For the computation of Arm's Length Price -

1. **"Transaction"** includes a number of closely linked transactions.
2. **"Uncontrolled Transaction"** means a transaction between unrelated enterprises, whether resident or non-resident.
3. **"Unrelated Enterprises":** Enterprises are said to be unrelated, if they are not associated or deemed to be associated u/s 92A.

6 *Definition of TNMM as per **OECD Guidelines:***

"a transactional profit method that examines the net profit margin relative to an appropriate base (e.g. costs, sales, assets) that a assessee realizes from a controlled transaction (or transactions that it is appropriate to aggregate)."

4. **"Uncontrolled conditions":** Conditions which are not controlled or suppressed or moulded for achievement of pre-determined results are said to be uncontrolled conditions.
5. **"Property"** includes goods, articles or things, and intangible property.
6. **"Services"** include financial services.

Computation of Arm's Length Price as per Transaction Net Margin Method

No.	Particulars	Amount (₹)
1	Price at which property purchased or services obtained by the enterprise from an associated enterprise are resold or are provided to an **unrelated enterprise.**	XXXX
2	Add/Less: Adjustments for differences, having material affect on the price in the open market:	
	i) Adjustments for FAR Analysis	**XXXX**
	ii) Quality of the product or service	**XXXX**
	iii) Characteristics of the Property	**XXXX**
	iv) Contractual terms	**XXXX**
	v) Level of the market	**XXXX**
	vi) Inventory turnover	**XXXX**
	vii) Intangible property associated with the sale	**XXXX**
	viii) Foreign currency risks	**XXXX**
	ix) Data and assumptions	**XXXX**
	x) Extra ordinary market conditions	**XXXX**
3	Arm's Length Price for the purpose of Sec.92C (1 -2)	XXXX

Use of Profit Level Indicator (PLI)

In trying to benchmark the results of the tested party with that of unrelated parties i.e. comparable companies, by applying the TNMM, it is important to use appropriate PLIs. The choice of PLI is dependent upon the following which also includes:

(a) the nature of the activities of the tested party,

(b) the reliability of the available financial data with respect to comparable companies,

(c) the extent to which a particular PLI is applicable to this data.

All PLIs not similar. The selection of the appropriate PLI depends on the structure and the business of the tested party. For example, Berry Ratio might be an apt PLI in case of the tax-payers that almost exclusively perform services and distribution activities. On the other hand, a manufacturing concern with an extensive capital investment in plant and equipment might require the application of the return on assets to determine the arm's length prices.

Use of Operating Margin

The operating margin (in this case the ratio of EBIT to Operating Revenue) is a profitability measure. EBIT is a measure of operating profit, which excludes the effect of company financing and taxation decisions as well as abnormal and extraordinary items.

The ratio is a useful indicator of comparative performance by showing the ability of a company to control its costs relative to its level of sales.

Illustrations on TRANSACTION NET MARGIN METHOD

Illustration 12: Fox Solutions Inc. a US Company, sells Laser Printer Cartridge Drums to its Indian Subsidiary Quality Printing Ltd at S 20 per drum. Doc Solutions Inc. has other takers in India for its Cartridge Drums, for whom the price is $ 30 per drum. During the year, Fox Solutions had supplied 12,000 Cartridge Drums to Quality Printing Ltd.

Determine the Arm's Length Price and taxable income of Quality Printing Ltd if its income after considering the above is ₹45,00,000. Compliance with TDS provisions may be assumed and Rate per USD is ₹45. Also determine income of Doc Solutions Inc.

(A) Computation of Total Income of Quality Printing Ltd

Particulars	Amount (₹)	Amount(₹)
Total Income before adjusting for differences due to Arm's Length Price		45,00,000
Add: Difference on Account of adopting Arm's Length Price [12,000 x $20 x ₹45]	1,08,00,000	
Less: Amount under Arm's Length Price[12,000 x $ 30 x ₹45]	1,62,00,000	
Incremental Cost on adopting ALP u/s 92(3), Taxable Income cannot be reduced on applying ALP. Therefore, difference on account of ALP is ignored.	**(54,00,000)**	
Total Income of Quality Printing Ltd.		45,00,000

(B) Computation of Total Income of Fox Solutions Inc.

The provisions relating to taxing income of Fox Solutions Inc., on applying Arm's Length Price for transactions entered into by a Foreign Company is given in Circular 23 dated 23.7.1969, which is as follows:

(I) **Transactions Not Taxable in India:** Transactions will not be subject tax in India if transactions are on principal-to-principal basis and are entered into at ALP, and the subsidiary also carries on business on its own.

(II) **Transactions Taxable in India** if the Indian Subsidiary does not carry on any business on its own. The following are the other considerations in this regard -

a) Adopting ALP does not affect the computation of taxable income of Fox Solutions Inc. if tax has been deducted at source or if tax is deductible.

b) Where ALP is adopted for taxing income of the Parent Company, income of the recipient Company (i.e. Quality Printing Ltd) will not be recomputed.

Illustration 13: Khazana Ltd is an Indian Company engaged in the business of developing and manufacturing Industrial components. Its Canadian Subsidiary Techpro Inc. supplies technical information and offers technical support to Khazana for manufacturing goods, for a consideration of Euro 1,00,000 per year. Income of Khazana Ltd is ₹90 Lakhs. Determine the Taxable Income of Khazana Ltd if Techpro charges Euro 1,30,000 per year to other entities in India. What will be the answer if Techpro charges Euro 60,000 per year to other entitles. (Rate per Euro may be taken at ₹50.)

Computation of Total Income of Khazana Ltd

Particulars	Amount	Amount
When price charged for Comparable Uncontrolled Transaction	€ 1,00,000	€ 50,000
Price actually paid by Khazana Ltd [€1,00,000 x ₹50] Less: Price charged in Rupees (under ALP) [€1,30,000 x ₹50] [€60,000 x ₹50]	50,00,000 65,00,000	50,00,000 30,00,000
Incremental Profit on adopting ALP (A)	(15,00,000)	20,00,000
Total Income before adjusting for differences due to Arm's Length Price Add: Difference on account of adopting Arms Length Price [if (A) is positive]	90,00,000 NIL	90,00,000 20,00,000
Total Income of Khazana Ltd.	90,00,000	1,10,00,000

Note: u/s 92(3), Taxable Income cannot be reduced on applying ALP. Therefore, difference on account of ALP which reduces the Taxable Income is ignored.

Illustration 14:

Designer Dolls Ltd. (DDI), located in United States, has a subsidiary in India. The Subsidiary manufactures designer dolls, using the unique technology developed by DDI. The Subsidiary has been able to locate from the public data base similar independent doll manufacturer. The Subsidiary pays Royalty to DDI @ 10% on sales, which is part of operating costs, which is the only international transaction that needs to be benchmarked.

The following is the profitability of the two companies:

Particulars	Subsidiary Co. (₹)	Independent Co. (₹)
Net Sales	2,50,000	7,00,000
Cost of goods sold	1,50,000	4,00,000
Operating Costs(including Royalty of ₹ 25,000)	50,000	2,00,000
Net Profit	50,000	1,00,000
Operating Margin: Net Profit/Net Sales *100	20%	14.28%

Thus, as the net profit margins earned by the subsidiary are more than the margin earned by the Independent Ca, the international transactions of the Subsidiary, i.e. Royalty paid of ₹ 25,000 is at arm's length.

Cost Cover Ratio

The cost coverage ratio measures the ability of a company to cover its operating expenses through operating revenue. Given the limitation of financial information publicly available, the operating expenses of a selected comparable company are the sum of its operating revenue less EBIT.

An example explaining the application of Operating margin is given below.

Illustration 15:

Indco, an Indian company produces a pen for itself and three foreign subsidiaries of its Swiss parent company. The foreign parent owns the rights to the product formulae for the pen. Although Indco has no internal comparable transactions, it has been able to locate data from a public data base, relating to a third party who manufactures similar pens. Indco has been able, after the appropriate functional analysis, to verify that the pen manufacturer is comparable. However, Indco cannot obtain the relevant information at the gross margin level. Therefore, it is unable to apply the CPM. The arm's length manufacturer realizes a net mark-up of 10% on the cost of manufacturing pens.

The following is the comparison of the net cost plus earned by IndCo, vis-à-vis the independent manufacturer is calculated as follows:

Particulars	Amount (₹)
Indco's cost of goods sold	1,000
Indco's operating expenses	300
Total costs	1,300
Sales Price earned by IndCo.	1,430
Markup earned (₹ 1430 – ₹ 1300)	130
Net Cost plus earned by IndCo (130/1300 * 100)	10%
Net Cost plus earned by Third Party Manufacturer	10%

Thus, IndCo's transactions are at arm's length.

Return on Assets Ratio

The return on assets ratio measures the amount of EBIT per rupee of asset invested. This is a profitability ratio measuring each company's operational efficiency, that is, how efficiently the assets have been deployed by the company.

Berry Ratio

Berry ratio is the ratio of gross profit to operating expenses. It measures the return on operating expenses. As the functions performed by the tax-payers are often reflected in the operating expenses, this ratio determines the relationship of the income earned in relation to the functions performed. This ratio helps in overcoming the difficulties in applying the RPM, which does not explain the creation of gross profit. This ratio is used in conducting an arm's length analysis of service-oriented industry such as limited risk distributor, advertising, marketing and engineering services. The Berry ratio may be used to test whether service providers have earned enough mark-up on their operating expenses. In essence, the Berry ratio implicity assumes that there is a relationship between the level of operating expenses and the level of gross profits earned by routine distributors and service providers. The use of Berry ratio is illustrated by way of the following example:

An example explaining the application of Operating margin is given below.

Illustration 16:

ABC Ltd. India acts as a limited risk distributor in respect of the goods manufactured by its parent company.

Dr. Profit and loss account of ABC Ltd India for the year ended March 31, 2016 Cr.

Particulars	Amount (₹)	Amount (₹)	Particulars	Amount (₹)	Amount (₹)
To Purchases		1,500	By Sales		2,500
To Gross profit		1,000			
Total		2,500	Total		2,500
To Employee Cost	250				
To Rent	200				
To Legal Charges	100				
To Depreciation	200				
ToTotal Operating Expenses		750			
Total		1,000	Total		1,000
To Interest Cost		15			

To Loss on sale of assets		2			
To Net Profit before tax		8			
Total		1,000	Total		1,000

In this case, ABC India purchases the goods from its AE only on receipt of orders received from third party domestic customers. Accordingly, it does not bear the risk of inventory.

In such a scenario, Berry Ratio would be an appropriate PLI as it represents a return on a company's value added functions and assumes that those functions are captured in its operating expenses. Thus, a Berry Ratio > 1 implies that the distributor earns enough to be able to recover its operating costs.

ABC India's Berry Ratio (Gross Profit/Operating Expenses) works out to be 1.33 (100/75).

Similarly, the mean of Berry Ratio of comparable companies is 1.17, which is illustrated as under:

Name of the Company	**Gross Profit** (₹)	**Operating Expenses** (₹)	**Berry Ratio (GP/Op.Exp)**
A Ltd.	50	40	1.25
B Ltd.	75	80	0.94
C Ltd.	120	80	1.50
D Ltd.	90	90	1.00
Mean			1.17

Since, the Berry Ratio of ABC India is higher than that of the mean of comparable companies the international transactions of ABC India regarding purchase of goods are at arm's length.

Documentation (Information and documents to be kept and maintained under section 92D)

Rule 10D. (1) Every person who has entered into an international transaction or specified domestic transaction shall keep and maintain the following information and documents, namely:—

Documents	**Details**
Ownership structure	(a)a description of the ownership structure of the assessee enterprise with details of shares or other ownership interest held therein by other enterprises;
Profile of MNC group	(b) a profile of the multinational group of which the assessee enterprise is a part along with the name, address, legal status and country of tax residence of each of the enterprises comprised in the group with whom international transactions or specified domestic transactions have been entered into by the assessee, and ownership linkages among them;
Description of business	(c) a broad description of the business of the assessee and the industry in which the assessee operates, and of the business of the associated enterprises with whom the assessee has transacted;
Nature and terms of international transactions	(d) the nature and terms (including prices) of international transactions entered into with each associated enterprise, details of property transferred or services provided and the quantum and the value of each such transaction or class of such transaction;
Description of FAR	(e) a description of the functions performed, risks assumed and assets employed or to be employed by the assessee and by the associated enterprises involved in the international transaction;

Record of economic and market analyses	(f) a record of the economic and market analyses, forecasts, budgets or any other financial estimates prepared by the assessee for the business as a whole and for each division or product separately, which may have a bearing on the international transactions entered into by the assessee;
Record of uncontrolled transactions for comparability	(g) a record of uncontrolled transactions taken into account for analysing their comparability with the international transactions entered into, including a record of the nature, terms and conditions relating to any uncontrolled transaction with third parties which may be of relevance to the pricing of the international transactions;
Record of analysis	(h) a record of the analysis performed to evaluate comparability of uncontrolled transactions with the relevant international transaction;
Description of the methods considered for determining ALP	(i) a description of the methods considered for determining the arm's length price in relation to each international transaction or class of transaction, the method selected as the most appropriate method along with explanations as to why such method was so selected, and how such method was applied in each case;
Record of actual working	(j) a record of the actual working carried out for determining the arm's length price, including details of the comparable data and financial information used in applying the most appropriate method, and adjustments, if any, which were made to account for differences between the international transaction and the comparable uncontrolled transactions, or between the enterprises entering into such transactions;
Assumptions, policies and price negotiations	(k) the assumptions, policies and price negotiations, if any, which have critically affected the determination of the arm's length price;
Details of adjustments	(l) details of the adjustments, if any, made to transfer prices to align them with arm's length prices determined under these rules and consequent adjustment made to the total income for tax purposes;
Any other information	(m) any other information, data or document, including information or data relating to the associated enterprise, which may be relevant for determination of the arm's length price.

Non-applicability:

Rule 10D(2): Nothing contained in sub-rule (1) shall apply in a case where the aggregate value, as recorded in the books of account, of international transactions entered into by the assessee does not exceed one crore rupees.

Provided that the assessee shall be required to substantiate, on the basis of material available with him, that income arising from international transactions entered into by him has been computed in accordance with section 92.

Rule 10D (3): The information specified in sub-rule (1) shall be supported by authentic documents, which may include the following:

(a) official publications, reports, studies and data bases from the Government of the country of residence of the associated enterprise, or of any other country;

(b) reports of market research studies carried out and technical publications brought out by institutions of national or international repute;

(c) price publications including stock exchange and commodity market quotations;

(d) published accounts and financial statements relating to the business affairs of the associated enterprises;

(e) agreements and contracts entered into with associated enterprises or with unrelated enterprises in respect of transactions similar to the international transactions;

(f) letters and other correspondence documenting any terms negotiated between the assessee and the associated enterprise;

(g) documents normally issued in connection with various transactions under the accounting practices followed.

Rule 10D (4): The information and documents specified under sub-rules (1) and (2), should, as far as possible, be contemporaneous and should exist latest by the specified date referred to in clause (iv) of section 92F:

Provided that where an international transaction continues to have effect over more than one previous year, fresh documentation need not be maintained separately in respect of each previous year, unless there is any significant change in the nature or terms of the international transaction, in the assumptions made, or in any other factor which could influence the transfer price, and in the case of such significant change, fresh documentation as may be necessary under sub-rules (1) and (2) shall be maintained bringing out the impact of the change on the pricing of the international transaction.

Rule 10D (5): The information and documents specified in sub-rules (1) and (2) shall be kept and maintained for a period of eight years from the end of the relevant assessment year.

Application of Berry Ratio under different propositions

Illustration 17:

ABC Ltd. An Indian Company, acts as a limited risk distributor in respect of the goods manufactured by its parent company.

Dr. Profit and loss account of ABC Ltd India for the year ended March 31, 2016 Cr.

Particulars	Amount (₹)	Amount (₹)	Particulars	Amount (₹)	Amount (₹)
To Purchases		1,500	By Sales		2,500
To Gross profit		1,000			
Total		2,500	Total		2,500
To Employee Cost	250		By Gross Profit		1,000
To Rent	200				
To Legal Charges	100				
To Depreciation	200				
Total Operating Expenses		750			
Total		1,000	Total		1,000
To Interest Cost		150			
To Loss on sale of assets		20			
To Net Profit before tax		80			
Total		1,000	Total		1,000

In this case, ABC Ltd. purchases the goods from its AE only on receipt of orders received from third party domestic customer. Accordingly, it does not bear the risk of inventory.

In such a scenario, Berry Ratio would be an appropriate PLI as it represents a return on a company's value added functions and assumes that those functions are captured in its operating expenses. Thus, a Berry Ratio > 1 implies that the distributor earns enough to be able to recover its operating costs.

ABC Ltd.'s Berry Ratio (Gross Profit/Operating Expenses) works out to be 1.33 (100/75).

Similarly, the mean of Berry Ratio of comparable companies is 1.17, which is illustrated as under:

Name of the Company	Gross Profit (₹)	Operating Expenses (₹)	Berry Ratio (GP/Op. Exp)	Purchase price in comparable transactions at same quantity by domestic companies from their AEs
A Ltd.	50	40	1.25	1,380
B Ltd.	75	80	0.94	1,390
C Ltd.	120	80	1.50	1,410
D Ltd.	90	90	1.00	1,370
Mean			1.17	1,387.5

Since, the ***Berry Ratio of ABC Ltd. is higher than that of the mean of comparable companies***, the international transactions of ABC Ltd. regarding purchase of goods are at arm's length.

Alternate Proposition I:

If Berry Ratio of ABC Ltd. Is 1.03 as compared to that of mean of comparable companies 1.17, is there any need to order for re-assessment of arm's length price?

Since, the ***Berry Ratio of ABC Ltd. is lower than that of the mean of comparable companies***, the international transactions of ABC Ltd. regarding purchase of goods are **not at arm's length.**

Impact on assessment of Arm's Length Price:

Particulars	Amount (₹)
Net Profit as per Profit & Loss Account before tax	80
Add : Adjustment for over-statement in Purchase Price on goods purchased from AE [= Purchase cost debited in Profit & Loss A/c (-) Average Purchase Price of Comparable Companies = ₹1,500 – 1,387.50]	112.50
Revised Net Profit after adjustment of over-statement in Purchase price but before tax	192.50

Alternate Proposition II:

Interest expense indicates only the extent to which the firm's assets are secured by debt and the amount of depreciation recorded on a firm's accounts is more likely to reflect the timing of that firm's acquisition of assets than the actual depletion of capital assets. What would be the impact on assessment if these both are excluded from Operating expenses for calculation of Berry Ratio?

Impact on assessment of Arm's Length Price:

Particulars	Amount (₹)
Net Profit as per Profit & Loss Account before tax	80
Add : Interest expense already excluded in computing operating expense, hence not considered further Add: Depreciation on assets added back	Nil 200
Revised Net Profit after adjustment of over-statement in Purchase price but before tax	380

Revised Operating Expenses = 750-200 =550

Revised Berry Ratio = (Gross Profit/Operating Expenses) works out to be 1.82 (1000/550).

Since, the ***Berry Ratio of ABC Ltd. is higher than that of the mean of comparable companies***, the international transactions of ABC Ltd. regarding purchase of goods are at arm's length.

Capacity Utilisation Adjustment

XYZ Ltd. An Indian Company, acts as a limited risk distributor in respect of the goods manufactured by its parent company.

Dr. Profit and loss account of ABC Ltd India for the year ended March 31, 2016 Cr.

Particulars	Amount (₹)	Amount (₹)	Particulars	Amount (₹)	Amount (₹)
To Purchases		1,500	By Sales		2,500
To Gross profit		1,000			
Total		2,500	Total		2,500
To Employee Cost	250		By Gross Profit		1,000
To Rent	200				
To Legal Charges	100				
To Depreciation	200				
Total Operating Expenses		750			
Total		1,000	Total		1,000
To Interest Cost		150			
To Loss on sale of assets		20			
To Net Profit before tax		80			
Total		1,000	Total		1,000

Installed capacity: 10,000 hours. Capacity Utilisation: 75%. Cost of Fixed Assets ₹10,000, Depreciation provided till date ₹8,000, rate of depreciation @ 10%. Also given that there are 40 labourers, 260 working days and 8 hours per day. Industry capacity utilization rate is 90%

What would be the adjustments required?

Solution:

(1) Depreciation related to "idle assets" should be adjusted from Profit & Loss Account.

Year Ended	INR'000
Total depreciation charged in Profit & Loss Account	200
Add: Proportionate depreciation in relation to "idle assets" to the extent of 30%, since utilized capacity is 75% =[200 x 25%]	50
Depreciation adjusted in line with capacity utilisation	150

(2) Adjustment in Profit & Loss Account

Year Ended	INR'000
Net Profit as per Profit & Loss Account	80
Add: Proportionate depreciation in relation to "idle assets" to the extent of 25%, since utilized capacity is 75% =[200 x 25%], now written back	50
Adjusted Net Profit	130

(3) Adjustment related to utilization of man-power

Steps	Year Ended	INR'000
(a)	Head counts	40
(b)	Maximum number of hours per employee (ie 260 days * 8 hrs per day)	2,080
(c)	Total available hours (c = a * b)	83,200
(d)	Utilisation rate	75%
(e)	Utilised hours (= c * d)	62,400

(f)	Unutilised hours (= c – e)	20,800
(g)	Unutilised hours after considering the industry unutilised rate of 10% (= f / 0.25*0.10)	8,320
(h)	Unutilised head counts (= g/2,080)	4
(i)	Employment related costs (i)	250
(j)	Adjustment to total employment related Cost (= i/a * h)	25

(4) Impact of capacity under-utilisation and its adjustment is shown as under:

Year Ended	**INR'000**
Sales (i)	2,500
Less: Total Cost (ii)	2,420
Operating profit (iii = i – ii)	80
Cost plus mark-up (iv = iii/ii * 100)	3.31%
Unutilised capacity cost adjustment –related to employee cost (v)	25
Unutilised capacity cost adjustment –related to depreciation "idle asset" (vi)	50
Adjusted operating profit (vii = iii + v + vi)	155
Adjusted cost plus mark-up (viii = vii/ii * 100)	6.40%
Net increase in cost plus mark-up (ix = iv – viii)	3.09%

Illustrations on Forex Adjustment

Illustration 18:

(a) An Indian software company receives an order from an European union country. The buyer will pay in four quarterly installments each of €0.5 million, starting from the end of the first quarter. The rates for euros in India is as follow :

Spot	3 month forward	6 month forward	9 month forward	1 year forward
₹ 52.80	₹ 52.70	₹ 52.55	₹ 52.50	₹ 52.48

If an Indian company hedges its foreign exchange rate risk in the forward market, how much revenue does it earn?

(b) Are arbitrage gains possible from the following set of information to the arbitrageur?

Spot rate: 47.88/$

3 month forward rate : ₹ 47.28/$

3 month interest rates :

₹ : 7% p.a.

$: 11% p.a.

Answer 18. (a)

Indian software company will have the following income streams :

Installment	**Euro income (€)**	**Rate (₹)**	**Revenue (₹)**
1st quarter-end	5,00,000	52.70/€	2,63,50,000
2nd quarter – end	5,00,000	52.55/€	2,62,75,000
3rd quarter-end	5,00,000	52.50/€	2,62,50,000
4th quarter-end	5,00,000	52.48/€	2,62,40,000
Total revenue income is		10,51,15,000	

Answer 18. (b)

3 month forward rate of the dollar is higher (at ₹48.28) than the spot rate (₹47.88). It implies that the dollar is at premium.

Premium (%) = (₹48.28 – ₹47.88)/47,88 x 12/3 x 100 = 3.34% per annum

Interest rate differential = 11% - 7% = 4% per annum

Since interest rate differential (4%) and premium % (3.34%) do not match, there are arbitrage gain possibilities. An arbitrageur can take the following steps in this regard :

(i) Arbitrageur borrows, say, ₹100 million at 7% for 3 months (he borrows in Indian currency as it carries lower interest rate).

(ii) He then converts ₹100 million in US $ at the spot rate of ₹47.88 in the spot market. He gets an amount of US $ 2,088,554.72 (₹100 million/ ₹47.88).

(iii) He invests US $ 2,088,554.72 in the money market at 11% interest per annum for 3 months. As a result of this investment, he obtains the interest of US $ 57,435.2548 ($ 2,088,554.72 × 3/12 × 11/100).

(iv) Total sum available with arbitrageur, 3 months from now is (US $ 2,088,554.72 amount invested + US $ 57,435.2548 interest) = US $ 2,145,989.974.

(v) Since he would get US $ 2,1451989.974 after 3 months, he sells forward US $ 2,145,989.974 at the rate of ₹48.28.

(vi) As a result of a forward deal, at the end of 3 months from now, he would get ₹103,608,395.90, i.e. ($ 2,1451989.974 × 48.28).

(vii) He refunds the Rs. 100 million borrowed, along with interest due on it. The refunded sum is ₹100 million + ₹1,750,000 i.e. (₹100 million × 3/12 × 7/100) = ₹101,750,000.

(viii) Net gain is ₹103,608,395.90 – ₹101,750,000 = ₹18,58,395.90.

Illustration 19:

The investment manager of a large Indian software company receives the following quotes from its foreign exchange broker.

US dollar spot rate : ₹47.75/ US $

US dollar option quotation

Strike price	Call			Put		
	September	December	March	September	December	March
45.0000	3.0	-	-	-	-	-
45.5000	2.6	2.9	-	-	-	-
46.0000	2.0	2.3	2.45	0.2	-	-
46.5000	1.85	1.95	2.15	0.25	-	-
47.0000	1.25	1.85	2.00	0.70	-	-
47.5000	0.85	1.15	1.45	1.00	1.25	1.75
48.0000	0.50	0.74	0.89	1.59	1.92	2.50
48.5000	0.30	0.52	0.68	1.70	2.20	-
49.0000	0.15	-	-	1.90	-	-
49.5000	0.10	-	-	2.00	-	-
50.0000	0.08	-	-	2.30	-	-

What calculation will the investment manager make for following questions?

(i) What is the intrinsic value for the December 47.5 call option?

(ii) What is the intrinsic value for the September 46 put option?

(iii) What is the break-even exchange rate for the March 46.5 call and the March 48 put?

(iv) If the March spot rate is expected to be ₹48.50/US $, which call option should be bought?

(v) The software company will receive its export income in March and the expected spot rate (in March) will be ₹46.5/US $, which put option should be bought?

Answer 19.

Intrinsic value of an option is the amount by which the option is in-the-money.

For a call option, intrinsic value = Maximum [(Spot rate – Strike rate), 0]

For a put option, intrinsic value = Maximum [(Strike rate – Spot rate), 0]

i. Intrinsic value for the December 47.5 call option

= Max [(₹47.75/US $ - ₹47.5/US $),0]

= Max [₹0.25/ US $, 0] = ₹0.25/ US $

ii. Intrinsic value for the September 46 put option

= Max [(₹46/ US $ - ₹47.75/US $), 0]

= Max [-(₹1.75/ US $), 0] = 0

iii. The break-even exchange rate for the March 46.5 call on settlement date is Re. X/US $

So, The premium paid = ₹2.15/US $

Profit from the call option = ₹(X – 46.5)/US $

At break even, ₹(X – 46.5)/US $ = ₹2.15/ US $

X = ₹48.65/ US $

The break even exchange rate for March 48 put is :

Premium paid= ₹2.50/US $

Profit from the put option = ₹(48 – X)/US $

At break-even, ₹(48 – X)/US $ = ₹2.50/US $

X = ₹45.5/US $

iv. For an expected spot rate of ₹48.50/US $, we need to find out profit from buying the March call option at various strike prices.

Gain from call option

= Max [(Settlement rate – Strike rate),0] – Premium

= value of option at expiration – Premium

Option	Strike price (₹)	Premium (A)	Option value at expiration (B) (₹)	Gain/ Loss [B – A] (₹)
March call	46.00/ US $	2.45/ US $	2.50 / US $	0.05/ US $
March call	46.50/ US $	2.15/ US $	2.00/ US $	- 0.15/ US $
March call	47.00/ US $	2.00/ US $	1.50/ US $	- 0.50/ US $
March call	47.50/ US $	1.45/ US $	1.00/ US $	- 0.45/ US $
March call	48.00/ US $	0.89/ US $	0.50/ US $	- 0.39/ US $
March call	48.50/ US $	0.68/ US $	0.00/ US $	- 0.68/ US $

So, for the expected March spot rate of ₹48.50/ US $, the March call option of strike price ₹46.00/ US $ should be bought.

v. Gain from purchasing the March put option of various strikes, for which quotes are available, for an expiration price of ₹46.50/ US $.

Option	Strike price	Premium (A)	Option value at expiration (B)	Gain/ Loss [B – A]
	(₹)	(₹)	(₹)	(₹)
March put	47.50/ US $	1.75/ US $	1.00 / US $	- 0.75/ US $
March put	48.00/ US $	2.50/ US $	1.50/ US $	- 1.00/ US $

As no gains accrue by purchasing the different March put available for the expected March expiration rate of ₹46.50/ US $, the software company should not hedge through the put options.

Illustration 20:

(a) XYZ Ltd. a US firm will need £ 3,00,000 in 180 days. In this connection, the following information is available :

Spot rate 1£ = $ 2.00

180 days forward rate of £ as of today = £ 1.96

Interest rates are as follows :

Particulars	U.K.	U.S.
80 days deposit rate	4.5%	5%
80 days borrowing rate	5%	5.5%

A call option on £ that expires in 180 days has an exercise price of $ 1.97 and a premium of $ 0.04.

XYZ Ltd. has forecasted the spot rates 180 days hence as below :

Future rate ($)	1.91	1.95	2.05
Probability	25%	60%	15%

Which of he following strategies would be most preferable to XYZ Ltd.?

(a) a forward contract

(b) a money market hedge

(c) an option contract

(d) no hedging

Show calculations in each case.

(b) For imports from UK, Philadelphia Ltd. of USA owes £ 6,50,000 to London Ltd., payable on May, 2010. It is now 12 February, 2010.

The following future contracts (contract size £ 62,500) are available on the Philadelphia exchange :

Expiry	Current futures rate
March	1.4900 $/£ 1
June	1.4960 $/£ 1

(i) Illustrate how Philadelphia Ltd. can use future contracts to reduce the transaction risk if, on 20 May the spot rate is 1.5030 $/£ 1 and June futures are trading at 1.5120 $/£. The spot rate on 12 February is 1.4850 $/£ 1.

(ii) Calculate the "hedge efficiency" and comment on it.

Answer 20. (a)

(a) **Taking a Forward Contract**

US $ needed on expiration of 180 days

= £ 3,00,000 × $ 1.96 = $ 5,88,000

(b) **Money Market Hedge Transaction**

Now :

Borrow in US dollars and invest in UK pounds on expiration of 180 days

On expiration of 180 days :

Repay in US $:

US $ needed to purchase UK £

= £ 2,87,081

US $ needed to convert into UK £

= £ 2,87,081 × $ 2 = $ 5,74,162

Principal and interest payable in US $ loan on expiry of 180 days

= $ 5,74,162 × $ 1.055 = $ 6,05,741

(c) **Entering into Option Market by taking Call Option**

Expected spot rate in 180 days	Premium per unit	Exercise option	Total price per unit	Total price for £ 3,00,000 (x)	Probability (p)	(px)
1.91	0.04	No	1.95	5,85,000	0.25	1,46,250
1.95	0.04	No	1.99	5,97,000	0.60	3,58,200
2.05	0.04	Yes	2.01	6,03,00	0.15	90,450
						5,94,900

Answer 20. (b)

(a) For Philadelphia Ltd. the appropriate futures contract will be the one that will expore soonest after the end of the exposure period i.e. the June contract.

Number of contracts needed

= £ 6,50,000/£ 62,500 = 10.4 (say 10 contracts)

P Ltd. will buy 10 June contracts now (12 Feb.) at $1.4960/£1 and sell 10 contracts on 20 May for $1.5120/£1, thus making a profit from the futures trading that will largely but not totally, netate the 'loss' from the spot market (since sterling has strengthened between 12 February and 20 May).

We now calculate the profit/loss from the futures contracts trade :

(i) The 'tick' movement is (1.5120 – 1.4960) = 0.0160 i.e., 160 ticks (for one tick = 0.00001)

(ii) 'Tick' value per contract = £ 62,500 × 0.00001 = $ 6.25

(iii) Profit = 10 contracts × 160 × $ 6.25 = $ 10,000

(iv) Overall cost on 20 May when P Ltd. will exchange $ for £ on the spot market :

(v) The net 'cost' to P Ltd.

= $ 9,76,950 – $ 10,000 = $ 9,66,950

(b) Hedge Efficiency

The spot on February 12 was 1.4850 $/£1. So £650.000 would have cost $ 9,65,250 and the los on the 'spot market' is $ (9,76,950 – 9,65,250) = $ 11,700.

The hedge efficiency is therefore the future contract profit divided by the spot market loss

The inefficiency is due to :

(i) rounding the contracts to 10 from 10.4, and

(ii) basis risk - the fact that the movement on the futures price has not exactly equalled the movement on the spot rate.

Illustration 21:

(a) The following quotes are avilable for 3-months options in respect of a share currently traded at Rs. 31 :

Strike price	₹30
Call option	₹3
Put option	₹2

An investor devises a strategy of buying a call and selling the share and a put option. Draw his profit/loss profile if it is given that the rate of interest is 10% per annum. What would be the position if the strategy adopted is selling a call and buying the put and the share?

(b) What is the difference between Forward and Futures contracts?

Answer 21. (a)

Strategy I : Buying a call and selling a put and a shre

Initial cash inflow (₹31 – ₹3 + ₹2) = ₹30

Interest rate = 10%

Amount grows in 3 months to $(30 \times e^{1 \times .25})$ = ₹30.76*

If the share price is greater than ₹30, he would exercise the call option and buy one share for ₹30 and his net profit is ₹0.76 (i.e. ₹30.76 – 30).

However, if the share price is less than ₹30, the counter-party would exercise the put option and the investor would buy one share at ₹30. The net profit to the investor is again ₹0.76.

Strategy II : Selling a calland buying a put and a share

In case, the investor has to arrange a loan @ 10% of ₹30 (i.e. ₹31 + ₹2 – ₹3).

This amount would be repaid after 3 months. Amount payable ($30 \times e^{1 \times .25}$) is ₹30.76.

After 3 months, if the market price is more than ₹30, the counter-party would exercise the call option and the investor would be required to sell the share at ₹30. The loss to the investor would be ₹0.76 (i.e. ₹30.76 – 30).

However, if the rate is less than ₹30, the investor would exercise the put option and would get ₹30 from the rate of share. The loss to be buyer would again be ₹0.76.

* Interest can also be calculated on simple interest basis instead of continuous compound interest.

Answer 21. (b)

Fundamentally, forward and futures contracts have the same function: both types of contracts allow people to buy or sell a specific type of asset at a specific time at a given price.

However, it is in the specific details that these contracts differ. First of all, futures contracts are exchange-traded and, therefore, are standardized contracts. Forward contracts, on the other hand, are private agreements between two parties and are not as rigid in their stated terms and conditions. Because forward contracts are private agreements, there is always a chance that a party may default on its side of the agreement. Futures contracts have clearing houses that guarantee the transactions, which drastically lowers the probability of default to almost never.

Secondly, the specific details concerning settlement and delivery are quite distinct. For forward contracts, settlement of the contract occurs at the end of the contract. Futures contracts are marked-to-market daily, which means that daily changes are settled day by day until the end of the contract. Furthermore, settlement for futures contracts can occur over a range of dates. Forward contracts, on the other hand, only possess one settlement date.

Lastly, because futures contracts are quite frequently employed by speculators, who bet on the direction in which an asset's price will move, they are usually closed out prior to maturity and delivery usually never happens. On the other hand, forward contracts are mostly used by hedgers that want to eliminate the volatility of an asset's price, and delivery of the asset or cash settlement will usually take place.

Illustration 22:

Hedging with Commodity Futures :

Bharat Oil Corporation (BOC) imports crude oil for its requirements on a regular basis. Its requirements are estimated at 100 tonnees per month.

Of late, there has been a surge in the prices of oil. The current price (month of June) of crude oil is ₹ 5,500 per barrel. The firm expects the price to rise in coming months to ₹5,800 by August. It wants to hedge against the rising prices for its requirements of the month of August.

Multi Commodity Exchange (MCX) in India offers a futures contract in crude oil. The contract size is 100 barrels and August contract is currently traded at ₹5,668 per ballel.

(a) How can BOC hedge its exposure against the rising price of crude oil?

(b) If Bharat Oil Corporation hede its exposure at MCX, how many contracts it must book?

(c) Analyse the position of BOC if in the month of August (i) the spot price is ₹5,750 and futures price is ₹5,788, (ii) the spot price is ₹5,417 and futures market were matched?

Ignore marking-to-the-market and initial margin on futures contracts.

Answer 22.

1 tonnes = 7.33 barrels

(a) Hedging strategy would be to take position in the futures market opposite to that of in the physical market.

BOC is short on crude oil and therefore they must go long on the futures of crude oil.

Following would be the hedging strategy :

June : Buy futures contract now

August : Purchase crude oil at the price prevailing then in the spot market, and Sell the future contracts.

(b) Quantity to be imported/hedged = 100 tonnes or 733 barrels

Contract size = 100 barrels

Nos of contracts bought = 733/100 = 8 (rounded off)

(c) In August, the firm would buy its requirements of crude oil in the market and unwind its position in the futures market by selling the contracts bought in June. By doing so, the gains/loss in the physical market would be offset significantly.

August futures on crude oil = ₹5,668 per barrel

(i) When the price of crude oil rises :

Spot crude oil price = ₹5,750 Future price = ₹5,788

Purchase price in the spot for = 733 × 5750 = ₹42,14,750

Cash flow on futures position

Buying price	5668
Selling price	5788
Profit	120

Realizations from futures market = 8 × 100 × 120

= – ₹96,000

Net amount paid ₹41,18,750

Effective price per barrel = 41,18,750/733 = ₹5,619

(ii) When the price of crude oil falls :

Sport crude oil price = ₹5,417

Futures price = ₹5,455

Purchase price in the spot for = 733 × 5417 = ₹39,70,661

Cash flow on futures position

Buying price	5668
Selling price	5455
Profit	– 213

Realisations from futures market = 8 × 100 × – 213

= ₹1,70,400

Net amount paid ₹41,41,061

Effective price per barrel = 41,41,061/733 = ₹5,649

(d) If positions in the physical market and futures market were matched then

The effective price would be = $S_1 - (F_1 - F_0)$

When price rose the effective price paid is

= 5750 – (5788 – 5668) = ₹5,630 per barrel

When price fell the effective price paid is

= 5417 – (5455 – 5668) = ₹5,630 per barrel

Illustration 23:

Cancelling a swap

A company has borrowed through a fixed rate instrument of 8%. The swap quote from the bank is 7.80/7.90, i.e., bank pays 7.80 fixed for receiving LIBOR and would receive 7.90% fixed for paying LIBOR. The company enters the swap deal with the bank.

After some time, the swap market changes to 6.40/6.50 and the company again reverses the original swap by entering into 2nd swap opposite to that of the first one.

(a) What does the structure of the first wap achieve?

(b) What is the cost of funds for the firm before and after the swap?

(c) What is the structure of 2nd swap and what does it do?

(d) Find the cost of funds for the company after the second swap?

Answer 23.

(a) The company would undertake the transform the fixed rate liability to floating rate, as it possibly expects a decline in the interest rates.

(b) Cost of funds after swap = L + 0.2%

(c) The company would enter into a swap opposite to that of the first one. In the first swap, the firm received fixed and paid variable. Now in the second swap, it would pay fixed while receiving LIBOR. This would enable cancelling the floating leg. The company would gain the differential of the fixed legs of first and second swap.

(d) Pay fixed to borrowers	8.00
Receive fixed from bank (1st swap)	– 7.80
Pay fixed to bank (2nd swap)	6.50
Effective cost after 2nd swap	6.70

Effect of change in Foreign Investments in equity on Arm's Length Price

(through Cost Plus Method)

Illustration 24: Milano Inc., Italian Company, holds 45% of Equity in the Indian Company, Systems Technologies Ltd (STL). STL is engaged in development of software and maintenance of the same for customers across the globe. Its clientele includes Milano Inc. During the year, STL had spent 2,400 Man Hours for developing and maintaining software for Milano Inc, with each hour being billed at ₹1,300. Costs incurred by STL for executing work for Milano Inc. amount to ₹20,00,000.

STL had also undertaken developing software for Harsha Industries Ltd for which STL had billed at ₹2,700 per Man Hour. The persons working for Harsha Industries Ltd. and Milano Inc. were part of the same team and were of matching credentials and caliber. STL had made a Gross Profit of 60% on the Harsha Industries work.

STL is wholly dependent on the use of know-how from Milano Inc.

STL's transactions with Milano Inc. are comparable to the transactions with Harsha Industries, subject to the following differences:

(a) Milano Inc. gives technical know-how support to STL which can be valued at 8% of the normal gross profit. Harsha Industries does not provide any such support.

(b) Since the work for Milano involved huge number of man hours, a quantity discount of 14% of Normal Gross Profits was given.

(c) STL had offered 90 Days credit to Milano the cost of which is measured at 2% of the Normal Billing Rate, No such discount was offered to Harsha Industries Ltd.

Compute ALP and the amount of increase in Total Income of Systems Technologies Ltd.

Alternate proposition I:

Will there be any impact on your assessable value, as determined, if Milano Inc., Italian Company, a year ago, having their shareholding at 8% of Equity in the Indian Company, Systems Technologies Ltd (STL) was charged @ ₹2,500 per man hour ?

Alternate proposition II:

Milano Inc. intends to hold investment in STL for a indefinite period of time and it has no intention to resell for short-term profits. i.e. they classify quoted equity securities as Available-for-Sale (AFS) financial assets.

As at 31st December, 2010, the fair value (represented by the quoted bid price) of STL shares was ₹75 per share as compared with the original acquisition cost of ₹100 per share, representing a decline of 25%.

STL's share price has been trading at around ₹75 per share for the past three months. The historical volatility of STL's share price for the past 5 years is approximately 30 percent. Recent financial analyst reports indicate a target price range of ₹90 to ₹125 for STL's share.

Milano Inc. assessed the recoverability of the investment based on internally established criteria. Based on the assessment, Milano Inc. concluded that the decline in fair value below cost is not considered to be significant or prolonged and thus, investment is not impaired. Therefore, the unrealized holding loss remains in equity and is not charged to profit or loss.

The financial statements for the year ended 31st December 2016 reflected a fair value loss of ₹1 crore in fair value reserve, under shareholders' equity. This is equal to approximately 10% of profit of the year. What should the directors consider when validating the reasonableness of the estimates made by management?

What is the impact on assessment of Arm's Length Price?

Basic Proposition:

(a) Computation of Arms Length Gross Profit Mark Up

Particulars	%	%
Normal Gross Profit Mark Up		**60.00**
Less: Adjustment for differences: (which had the effect of reducing the profit of STL)		
(i)Technical support from Milano Inc. (8% of Normal Gross Profit 60%)	4.80	
(ii)Quantity Discount @ 14% of Normal Gross Profit (14% of 60%)	8.40	**13.20**
Normal Gross Profit Rate of STL, had the transaction been unrelated and there been no technical support or quantity discount		46.80
Add: Cost of Credit to Milano Inc. @2% of Normal Gross Profit (2% of Gross Profit 60%) [since this had effect of reducing the gross profit of STL]		1.20
Arms Length Gross Profit Mark-up		48.00

(b) Computation of Increase in Total Income of STL for services to Milano Inc.

Particulars	Amount (₹)
Cost of Services provided to Milano	20,00,000
Billed Value at Arm's Length [Cost / (100 – Arm's Length Mark) = [₹20,00,000/ (100% -48%]	38,46,154
Less: Actual Billing to Branch Inc.[2,400 x 1,300]	31,20,000
Increase in Total Income of Milano Inc.	7,26,154

Alternate Proposition I:

It is proposed to ascertain the effect of change in equity on determination of Arm's Length Price, with increase in foreign ownership ratio, as compared to past years.

The ownership structure can be classified into two class of shareholders:

(i) The market investor;

(ii) The stable investor.

The stable investor, including financial institutions and affiliated firms, tends to have on-going business ties with firms in which it holds shares. Financial institutions such as banks and insurance companies usually have lending, corporate insurance, and other financial transactions with the firms in which they hold shares. Corporate shareholders are usually business partners, suppliers or customers of the firms in which they have cross-shareholdings. Stable shareholders are more interested in stabilizing their business relationship than in the return on investment since the **relative cash flows from the former far exceed those of the later.**

Market investors are those who buy, sell and hold stocks primarily for investment purposes. The main objective of market investors is a high investment return because, unlike stable investors, they have only arm's length financial relations with firms in which they own shares. Thus, firms with a larger percentage of outstanding shares held by market investors are under great pressure to adopt profit-maximizing policies.

Thus, increase in foreign ownership ratio is positively associated with firm performance.

Foreign ownership change is measured in the ratio of firm's outstanding shares held by foreign shareholders.

Assuming this following information relating to ratio of foreign ownership in comparison to total outstanding shares is already available.

Year/Particulars	1	2	3	4	5
Total shares outstanding	1,00,000	1,20,000	1,50,000	1,50,000	2,00,000
Foreign ownership	2,000	2,400	3,000	3,000	90,000
% of Foreign ownership on firm's outstanding shares held by stable investors	2%	2%	2%	8%	45.00%
% Increase in foreign equity	-	-	-	300%	2150%
Price charged per man-hour	₹2,500	₹2,500	₹2,500	₹2,200	₹1,300
Decrease in price charged per man-hour	-	-	-	₹300	₹1,200
% decrease in price charged per man-hour	-	-	-	12%	54.55%

Impact of decrease in price –change on increase in foreign equity:

= (% decrease in price charged per man-hour) / (% Increase in foreign equity) x 100

= (54.55% /2150%) x **100 = 2.54%**

(a) Computation of Arms Length Gross Profit Mark Up

Particulars	%	%
Normal Gross Profit Mark Up		**60.00**
Less: Adjustment for differences:(which had the effect of reducing the profit of STL)		
(i)Technical support from Milano Inc. (8% of Normal Gross Profit 60%)	4.80	
(ii)Quantity Discount @ 14% of Normal Gross Profit (14% of 60%)	8.40	**13.20**
Normal Gross Profit Rate of STL, had the transaction been unrelated and there been no technical support or quantity discount		46.80
Add: Cost of Credit to Milano Inc. @2% of Normal Gross Profit (2% of Gross Profit 60%) [since this had effect of reducing the gross profit of STL]		1.20
Add: impact of decrease in price charged due to increase in foreign equity investment in STL by Milano Inc.		2.54
Arms Length Gross Profit Mark-up		50.54

(b) Computation of Increase in Total Income of STL for services to Milano Inc.

Particulars	Amount (₹)
Cost of Services provided to Milano	20,00,000
Billed Value at Arm's Length [Cost / (100 – Arm's Length Mark) = [₹20,00,000/ (100% - 50.54%]	40,43,672
Less: Actual Billing to Branch Inc. [2,400 x 1,300]	31,20,000
Increase in Total Income of Milano Inc.	9,23,672

Increase in total income of Milano Inc. due to change in Proposition

=Total Income vide Alternate proposition II (-) Total Income vide Alternate proposition I

= ₹9,23,672 (-) ₹7,26,154 = ₹1,97,518

However, Return on Assets (ROA) and Return on Investments (ROI), Sales and Leverage Ratio could also be considered for analyzing the impact of change in equity.

Alternate Proposition II:

It is important to understand the impairment criteria established by management for assessing whether a decline below cost is "significant" or "prolonged" and consider whether the criteria are reasonable and supportable based on relevant facts and circumstances.

The share price of an investment could be a relevant supporting criterion if it increases shortly after the reporting date or has a high level of volatility.

After looking at the basis, underlying the criteria established, it is important to consider whether the unimpaired share price is reasonable and sensible in light of available market evidence. This could be performed by comparing the cost with relevant factors, for example:

(i) Recent financial analysts' target price range and outlook;

(ii) The net assets per share of the investee; or the fundamental value of the investee;

(iii) The earnings multiple, such as price-to-earnings ratios, implied by the acquisition price.

In this case, since the historical volatility of STL's share price is approximately 30 percent, the decline does not appear to be significant. The decline of three months would not be considered to be prolonged.

Hence, impact of change may be ignored for computation of Arm's Length Price.

Working Capital Adjustment

The need for working capital adjustment

Performing working capital adjustment is necessary to ensure that returns derived from a set of comparables can be applied reliably to a tested party operating in a non-arm's-length setting.

Rationale:

The adjustments is economically sound, tax authorities/administrations in many countries across the globe accept/recognise this concept and usually require or at least recommend that taxpayers make such adjustments during the course of defending a transfer pricing audit, or while preparing and advance pricing agreement (APA) to ensure that the results are comparable by smoothening differences in working capital levels amongst otherwise functionally similar companies.

Example:

For example, in China, the State Administration for Taxation — SAT (issued notice on capital adjustment issues in transfer pricing tax administration), vide the release of Circular [2005] 745, explicitly identifies the working capital issue as follows:

"In this regard, if there are differences in working capital (such as accounts receivables, accounts payables, inventories, etc.) between the investigated enterprise and the comparable companies, adjustments should be made for the effects of implicit interest cost embedded in working capital on profitability levels. Hence, when comparing the profit level of the investigated enterprise and the comparable companies, capital adjustments will increase operating profit reliability from an economic perspective and improve the profit level comparability."

Approach adopted for performing working capital adjustments

The basis for making the working capital adjustment is that a uniform and harmonised formula is adopted globally for the outcome of this adjustment.

The assumption normally considered for such adjustment is that the debtors/ creditors whose name appears in the books of a company or receivables/payables which are there in the books of a company arise during the course of discharge of the business by the company.

Working capital adjustment implies adjustment for differences in the credit terms or working capital policies.

Companies with higher working capital requirements, other things being equal, would be expected to earn higher levels of operating profit to compensate for the greater use of capital. There are three critical elements in the working capital policy of any entity:

1) time-lag between the sale of products and payments received, which creates accounts receivable;
2) time-lag between the purchase of inputs and payments becoming dur, which creates accounts payable; and
3) time-lag between production and sale, which create inventories.

The objectives of the adjustments to accounts receivables (AR) and accounts payable (AP) are to remove the interest embedded in the AR/AP, attributable to the different levels of AR/AP, carried by the comparables and by the tested party.

The step-by-step procedure (synopsis) (explained in detail in the ensuing sections) adopted in performing the accounts receivables (AR) and accounts payables (AP) adjustment(s) are set out as under:

Step 1: Calculation of the average AR/AP amount during the year

$$= \left[\frac{AR\,(beginning\_of\_yr) + AR\,(end\_of\_yr)}{2} \right]$$

This is performed by both the tested party and the comparables.

Step 2: Calculation of AR/AP turnover (times)

AR/AP turnover represents the number of times the debtors have been turned over to produce the sales for the year.

AR T/o (times) $= \left[\frac{\text{Sales}}{\text{AR}}\right]$

Step 3: Calculation of average credit period

Average credit period represents the number of days' sales that remains with the debtors.

AR days $= \left[\frac{365}{\text{AR\_t/0}}\right]$

Step 4: Calculation of the differential AR/AP of the comparable vis-à-vis the tested party.

The comparables (C) and the tested part (T) have different credit policies which are reflected in the differential levels of receivables, vis-à-vis, their sales (S) that they carry. This step aims at identifying the differential values of receivables that are carried by the comparable vis-à-vis the tested party.

Differential AR of C (vis-à-vis TP) $= \left[\frac{AR_T}{S_T} - \frac{AR_C}{S_C}\right] * S_C$

Step 5: Calculation of the interest embedded in the differential AR/AP of the comparable vis-à-vis the tested party. The differential AR/AP of the comparable vis-à-vis the tested party) contains two elements:

- the sales price (that would have been paid in a cash sale and referred to as the AR/AP base);
- an interest element that is a compensation for the credit period advanced.

The interest rate for this purpose is often taken to be the prime lending rate as available on the Reserve Bank of India website. However, it is important to note that depending on the specific facts and circumstances, a different interest rate can also be justified for the purposes of making the working capital adjustments.

Diff AR base $= \left[\frac{\text{Diff\_AR}_C}{1 + i * \frac{\text{AR\_Days}_C}{365}}\right] \text{OR} \left[\frac{\text{Diff\_AR}_C}{1 + i * \frac{\text{AR\_AR}_C}{S_C}}\right]$

Interest embedded in Diff AR of Comparable = Differential AR of C Minus Diff AR base (as computed above).

Step 6: AR/AP adjustment – calculation of the differential interest embedded in the sales of the comparable vis-à-vis the tested party.

AR/AP adjustment is the differential interest embedded in the sales of the comparable company vis-à-vis the tested party and is calculated as follows:

Interest embedded in sales of comp = Interest embedded in Diff AR of Comp X Debtors turnover.

Capital adjustments often improve the reliability of TNMM comparisons if the tested party differs from the comparables with respect to their relative levels of certain balance sheet items (eg accounts payable, accounts receivable or inventory). Adjustments may differ depending on the profit level indicator selected. The following describes capital adjustments for accounts payable, accounts receivable, and inventory.

Accounts payable adjustment

1) The accounts payable adjustment removes implicit interest in the price of goods purchased on other than a cash basis from suppliers.

2) The purpose of this adjustment is to eliminate from profit comparisons the effects of companies' decisions on how to finance purchases.

3) A company purchasing goods on a cash basis would receive a lower price than a company purchasing the same goods on terms, because purchasing on terms subjects the seller to a capital cost that will be reflected in the price. Accordingly, if an adjustment is not made to reflect the implicit interest charged by suppliers, then a company that incurs more accounts payable would appear to be less profitable than an otherwise identical company that incurred less accounts payable.

4) The adjustment for this difference, referred to as "accounts payable adjustment", adjusts the cost of goods sold for each company by an estimate of the amount of interest included in the purchase price of the goods (or services). In other words, the cost of goods sold and, accordingly, operating profit is adjusted to a level that would be expected to exist if the companies purchased on a cash basis rather than on terms.

5) In simple terms, the embedded interest in cost of goods sold relating to accounts payable financing is estimated by multiplying an interest factor by the average outstanding accounts payable.

6) The amount of the adjustment to operating income is identical, regardless of the PLI. Moreover, because the decision on financing purchases does not affect a company's operating assets, sales or operating expense, this adjustment does not affect the denominator of the ROA, operating margin or Berry ratio. The adjustment affects cost of goods sold and also the denominator of the net cost plus ratio.

7) The company receiving longer terms will report a higher cost of goods sold and as a result lower operating profit.

8) The accounts payable adjustment thus estimates the implicit interest cost embedded in the cost of goods sold ("CGS"). The adjustment reduces the cost of goods sold (and as a result increases the gross profit) of the tested party and each of the comparables by the implicit interest paid to suppliers for financing received throughout the year. The amount financed by suppliers in a year is reflected by the average reported accounts payable ("AVGAP") during that year.

9) To determine the accounts payable adjustment, an "interest-free" average accounts payable by eliminating the embedded interest from AVGAP is computed. To calculate these interest-free accounts payable by dividing AVGAP by one plus a fraction of a year's interest rate corresponding to the number of days, the accounts payable remained outstanding. Finally, the embedded interest paid to the suppliers by multiplying the interest-free accounts payable by an annual interest rate ("RATE") is calculated. Accordingly, the formula for the accounts payable adjustment ("PAYZ") is:

$$\mathrm{PAYZ} = \frac{\mathrm{RATE} \times \mathrm{AVGAP}}{1 + \mathrm{RATE} \times \dfrac{\mathrm{AVGAP}}{\mathrm{CGS}}}$$

This formula is applicable to both the tested party and the comparable companies.

If cost of goods sold is controlled (sales in the denominator of the PLI)

Payables Adjustment $= \left[\dfrac{AP_T}{S_T} - \dfrac{AP_C}{S_C}\right] * S_C * \left[\dfrac{i}{1 + i * \dfrac{AP_C}{S_C}}\right]$

If sales are controlled (costs – TC is the denominator of the PLI)

$$\text{Payables Adjustment} = \left[\frac{AP_T}{TC_T} - \frac{AP_C}{TC_C}\right] * TC_C * \left[\frac{i}{1 + i * \frac{AP_C}{TC_C}}\right]$$

This formula is applicable only to the comparable companies.

Accounts receivable adjustment

1) The accounts receivable adjustment removes implicit interest in the price of goods or services sold on other than cash basis to customers.

2) The purpose of this adjustment is to eliminate the profit related to finance decisions of the seller.

3) A company selling on cash basis would receive a lower price than a company selling the same goods on terms, because selling on terms subjects the seller to a capital cost that will be reflected in the price.

4) Accordingly, if an adjustment is not made to reflect the implicit interest charged to customers, a company that extended longer payment terms would have higher accounts receivable and would appear to be more profitable than an otherwise identical company that extended shorter terms.

5) The adjustment for this difference, referred to as an "accounts receivable adjustment", adjusts the sales for each company by an estimate of the amount of interest included in the selling price of the goods or services. In other words, the sales, and accordingly the operating profit, are adjusted to a level that would be expected if the companies sold on cash basis rather than on terms.

6) The amount of the adjustment to operating income is identical, regardless of the PLI. However, the adjustment to the denominator depends on the PLI. For ROA, as the selling terms are being adjusted to a cash basis, accounts receivable are adjusted to zero. Accordingly, accounts receivable are removed from the asset base. For operating margin, as the adjustment for imputed financing costs is to sales, the denominator is reduced by the same amount of imputed interest as the numerator. For the Berry ratio and net cost *plus* ratio, as the accounts receivable adjustment is to sales, no adjustment is made to the denominator.

7) In simple terms, the embedded interest in sales relating to accounts receivable financing is estimated by multiplying an interest factor by the average outstanding accounts receivable.

8) By allowing customers to defer payment for a certain period, a firm foregoes the right to receive its revenues immediately and to earn additional income by reinvesting these revenues over the deferral period. For instance, a firm which demands immediate payment could invest its revenues in a financial instrument and earn interest over the next 90 days, an opportunity that is not available to a firm that allows its customers 90 days to pay for their purchases.

9) The accounts receivable adjustment thus estimates the implicit interest income embedded in sales ("SALE"). The adjustment reduces the sales (and as a result reduces the gross profit) of the tested party and each of the comparables by the implicit interest received from customers for financing provided throughout the year. The amount of financing provided to customers in a year is reflected in the reported average accounts receivable ("AVGAR") during that year.

10) The prime lending rate has been used as a proxy for computing the opportunity cost to the comparable of choosing a particular level of receivables, and thereby foregoing the interest it could have earned by investing in short-term interest bearing security the excess cash that was "tied up" in receivables. In the case of cash related assets (ie accounts receivable and accounts payable), the prime-lending rate is appropriately discounted since receivables/payables are stated at their future value (ie its value in 1 year).

11) To determine the accounts receivable adjustment, we first compute an "interest- free" average accounts receivable by eliminating the embedded interest from AVGAR. We then calculate these

interest-free accounts receivable by dividing AVGAR by one plus a fraction of a year's interest rate corresponding to the number of days the accounts receivable remained outstanding. Finally, we calculate the embedded interest received from customers by multiplying the interest-free accounts receivable by an annual interest rate ("RATE"). Accordingly, the formula for the accounts receivable adjustment ("RECZ") is provided as under:

$$\text{RECZ} = \frac{\text{RATE} \times \text{AVGAR}}{1 + \text{RATE} \times \frac{\text{AVGAR}}{\text{SALE}}}$$

This formula is applicable not only to the tested party but also to the comparable companies.

If the cost of goods sold is controlled (sales in the denominator of the PLI)

$$\text{Receivables Adjustment} = \left[\frac{AR_T}{S_T} - \frac{AR_C}{S_C}\right] * S_C * \left[\frac{i}{1 + i * \frac{AR_C}{S_C}}\right]$$

If cost of goods sold is controlled (sales in the denominator of the PLI)

$$\text{Inventory Adjustment} = \left[\frac{INV_T}{S_T} - \frac{INV_C}{S_C}\right] * S_C * i$$

If sales are controlled (costs in the denominator of the PLI)

$$\text{Inventory Adjustment} = \left[\frac{INV_T}{TC_T} - \frac{INV_C}{TC_C}\right] * TC_C * i$$

This formula is applicable only to the comparable companies.

Treasury instruments are cited here only for illustrative purposes. Clearly, the firm could consider alternative investments with different profiles of risk and expected return.

Particulars	**Reference**	**Comparable**	**Tested**
		Financial year ended 31.3.2010	
Sales	A	8.17	54.92
Operating cost	B	7.44	44.13
Purchases	C	3.60	22.77
Cost of goods sold	D	3.61	22.31
Operating profit	E=A-B	0.73	10.79
Operating profit margin (PLI)	F=E/A*100	8.94%	19.64%
Inventory	G	2.00	7.58
Accounts receivables	H	3.33	14.17
Accounts payables	I	0.79	8.92
Accounts receivables period	J	148.77	94.20
Accounts payables period	K	80.10	142.92
Inventory holding period	L	202.22	124.11
Receivables adjustment	M	(0.09)	
Payables adjustment	N	0.04	
Inventory adjustment	O=[7.58/54.92	(0.07)	
Capital adjusted operating profits	P=E+N+M-O	0.94	
Adjusted sales	Q=A-M	8.26	
Capital adjusted Operating	R=P/Q*100	11.34%	

Case Study 1:

J Inc. of Korea and CD Ltd, an Indian Company are associated enterprises. CD Ltd manufactures Cell Phones and sells them to J.K. & F Inc., a Company based at Nepal. During the year CD Ltd. supplied 2,50,000 Cellular Phones to J Inc. Korea at a price of ₹8,000 per unit and 35,000 units to JK & F Inc. at a price of ₹16,800 per unit. There being no other customer for CD Ltd. during this year. The transactions of CD Ltd with JK & F Inc. are comparable subject to the following considerations -

Sales to J Inc. are on FOB basis, sales to JK &F Inc. are CIF basis. The freight and insurance paid by J Inc. for each unit @ ₹700. Sales to JK &F Inc. are under a free warranty for Two Years whereas sales to J Inc. are without any such warranty. The estimated cost of executing such warranty is ₹500. Since J Inc.'s order was huge in volume, quantity discount of ₹200 per unit was offered to it. CD Ltd. has borrowed funds amounting to ₹100 crores, from its parent company at LIBOR plus 150 basis points. The fund is utilized for capital investment purposes, viz, expansion of capacity. The LIBOR prevalent at the time of borrowing is 6% for US$, thus its cost of borrowings is 7.50%. The borrowings allowed under the External Commercial Borrowings guidelines issued under FEMA, for example, say is LIBOR plus 250 basis points, then it can be said that Pharma's borrowing at 7.50% is less than 6.50% and thus at not at arm's length. Installed Capacity: 4,00,000 units. Industry utilization rate: 90%. The company works for 300 days in a year at 8 hours per day and has 300 employees. Cost of employees ₹1,00,000. Total Depreciation charged during the year ₹10,00,000. Net Profit for the year for CD Ltd. ₹8,54,000. Net profit ratio is 8%.

Compute the Arm's Length Price and the subsequent amount of increase in the Total Income of CD Ltd, if any.

(a) Computation of Arm's Length Price of Products sold to J Inc. Korea by CD Ltd

Particulars	₹	₹
Price per Unit in a Comparable Uncontrolled Transaction		16,800
Less: Adjustment for Differences -		
(a) Freight and Insurance Charges	700	
(b) Estimated Warranty Costs	500	
(c) Discount for Voluminous Purchase	200	
(d) External Commercial Borrowings (Working Note 1)	35	
(e) Depreciation adjustment (Working Note 2a)	1	
(f) Adjustment for under-utilisation of manpower (Working Note 2 c)	3333.29	(4,769.29)
Arms's Length Price for Cellular Phone sold to J Inc. Korea		12,030.71

(b) Computation of Increase in Total Income of CD Ltd

Particulars	₹
Arm's Length Price per Unit Less: Price at which actually sold to J Inc. Korea	12,030.71 (10,000)
Increase in Price per Unit	**2,030.71**
No. of Units sold to J Inc. Korea	2,50,000
Increase in Total Income of CD Ltd (2,50,000 x ₹2,030.71)	**₹50,76,77,500 Crores.**

Working Note 1: Adjustment for External Commercial Borrowings:

Excess Interest rate provided in comparison to ECB guidelines = (7.50 -6.50) % = 1%

Excess Interest cost = 1% of ₹ 100 crores = ₹ 1 crore.

Installed Capacity = 4,00,000 units.

Interest Cost per unit, based on Utilised Capacity = ₹ 1,00,00,000 / (2,50,000 + 35,000) = ₹ 35 (appx)

Capacity Utilised = 2,85,000 /4,00,000 x 100 = 71.25%

Working Note 2:

(a) Depreciation related to "idle assets" should be adjusted from Profit & Loss Account.

Year Ended	₹
Total depreciation charged in Profit & Loss Account	10,00,000
Add: Proportionate depreciation in relation to "idle assets" to the extent of 28.75%, since utilized capacity is 71.25% =[10,00,000 x 28.75%]	2,87,500
Depreciation adjusted in line with capacity utilisation	7,12,500

Depreciation adjustment per unit based on utilized capacity = 2,87,500 / 2,85,000 = 1.01 = 1.00 (appx)

(b) Adjustment in Profit & Loss Account

Year Ended	₹
Net Profit as per Profit & Loss Account	8,54,000
Add: Proportionate depreciation in relation to "idle assets" to the extent of 28.75%, since utilized capacity is 71.25% =[10,00,000 x 28.75%], now written back	2,87,500
Adjusted Net Profit	11,41,500

(c) Adjustment related to under-utilization of man-power

Steps	**Year Ended**	**INR'000**
(a)	Head counts	300
(b)	Maximum number of hours per employee (ie 300 days * 8 hrs per day)	2,400
(c)	Total available hours (c = a * b)	7,20,000
(d)	Utilisation rate	71.25%
(e)	Utilised hours (= c * d)	5,13,000
(f)	Unutilised hours (= c – e)	2,07,000
(g)	Unutilised hours after considering the industry unutilised rate of 10% (= f / 0.2875*0.10)	72,000
(h)	Total Unutilised head counts (= g/2,400)	30
(i)	Proportionate unutilized head counts on the basis of output provided to AE = (30 x 2,50,000/2,85,000)	26.316
(j)	Total Employment related costs	1,00,000
(k)	Proportionate employee related cost on the basis of output provided to Associated Enterprise = (1,00,000/2,85,000 x 2,50,0000)	87,719
(l)	Adjustment to total employee related Cost proportionate to output provided to AE (= k/ i)	3333.29

Case Study 2

Happy Ltd., an Indian Company is a wholly-owned subsidiary of Happy Inc. Happy Ltd. is engaged in provision of software development services to its associated enterprise Happy Inc. The following is the income statement if Happy Ltd. for the year ended 31.3.2016 Happy Ltd.

All figures in Rupees '000

Revenue from associated enterprises	
- Total operating income	95,000
Costs	
- Pay roll	40,000
- Rent	16,500
- Depreciation	9,500
- General administration expenses	8,200
- Other operating expenses	11,800
Total operating expenses	86,000
Operating profit	9,000
Net Cost plus mark-up (%) [Operating profit /total operating expenses]	10.46%

For the financial year ended 31st March, 2016, Happy Ltd has earned a Net Cost Plus mark-up of 10.46% from its associated enterprises. Accordingly, it is reasonable to conclude that Happy Ltd's international transactions with Happy Inc., relating to the provision of software services, appears to be consistent with the arm's length standard from the Indian transfer pricing perspective.

If Happy Ltd's actual mark-up is less than the arm's length mark-up benchmark of 11.77%, what would be the impact on assessment of arm's length price?

Solution:

It would need further examination as to whether it is compliant with the arm's length standard from an Indian Transfer pricing perspective. We may have two different scenarios:

Scenario 1: where Happy Ltd's margin is below the arm's length mark-up but within the range permissible under the proviso to Sec.92C (2)

Scenario 2: Where Happy Ltd's margin falls below the lower limit of the range of permissible under the proviso.

The calculation of range of permissible margins applying the proviso is shown in Table A. The arithmetic mean of 11.77% is applied to the costs of the tested party (₹86,000) to derive the arm's length price of the international transaction (refer col.2 –figure indicated as ALP ₹96,122) is a balancing figure and refers to the arm's length price of the international transaction.

The adjustment of (+/-) 3 percent permitted by the proviso is applied to the ALP to give the range of values that would be considered at arm's length. Further, as the international transactions consists of export of services, the lower end of the range is 97% of ALP ₹93,238 (Col.4) representing the lowest possible transaction value that would be considered compliant with the arm's length principle.

Table A

Calculation of Range of outcomes that would meet the arm's length standard applying the proviso to Section 92C (2)

Profit & Loss Account for the year ended 31st March, 2016 [All figures in Rupees '000]

Particulars	**Col. 1**			**Col. 2**		**Col.3**		**Col.4**
	Actual	**At ALP**	**Refer Note No.**		**At ALP (+) 3% of ALP**		**At ALP (-)3% of ALP**	
(a) Revenue								
-From associated enterprises (international transaction)	95,000	96,122	2	ALP	1,00,928	ALP (+)3%	93,238	**ALP (-) 3%**
Total Operating Income	**95,000**	**96,122**			**1,00,928**		**93,238**	
(b)Costs (all unrelated, no international transactions)								
Pay roll	40,000	40,000			40,000		40,000	
Rent	16,500	16,500			16,500		16,500	
Depreciation	9,500	9,500			9,500		9,500	
General administration exp.	8,200	8,200			8,200		8,200	
Other operating expenses	11,800	11,800			11,800		11,800	
Total Operating expenses	**86,000**	**86,000**			**86,000**		**86,000**	
(c)**Operating Profit**[=(a) – (b)]	9,000	10,122	1		14,928		7,238	
Net Cost Mark-up (%)	10.46%							
Arm's length mark-up [i.e. arithmetical mean of the Net Cost Plus mark-up(%) of broadly comparable independent companies]		11.77%						
Range of net cost plus mark-ups that would be considered compliant with the arm's length standard applying the +/- 3% variation permitted by proviso to Sec.92C(2) [= Operating Profit / Operating expenses]					17.36%		8.42%	

Notes:

4. Operating profit in Col.2 is a derived figure by applying mark-up of 11.77% to the tested party's total operating expenses of ₹86,000

5. (a) Revenue from associated enterprises (international transaction) in Col.2 is the balancing figure considering operating profit derived in Col.1 above and the total operating expenses remaining unchanged at ₹86,000. This revenue figure is the Arm's Length Price (ALP).

(b) Revenue from associated enterprises (international transaction) in Col.3 represents the upper limit of the range permissible under the proviso the Section 92C(2)

(c) Revenue from associated enterprises (international transaction) in Col.4 represents the lower limit of the range permissible under the proviso the Section 92C(2)

6. The Net Cost Plus Mark-up earned by the tested party (col.1) is higher than the arm's length mark-up (col.2), accordingly the international transaction complies with the arm's length principle.

Workings: Computation of Weighted Net Cost-plus mark-ups of broadly comparable independent companies. (on the basis of hypothetical data of 5 such companies for 5 years.)

Comparable Company 1 **(₹in Crores)**

Profit and Loss Account (Summary) year ended…..						
Comparable 1	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	125	143	155	134	175	732
(3)Total Cost	118	129	140	128	159	674
(4)Net profit [=(2) – (3)]	7	14	15	6	16	58
(5)Net cost plus mark-up [=(4)/(3) *100]	5.93%	10.8%	10.71%	4.69%	10.06%	----
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	----	----	----	----	----	8.61%

Comparable Company 2 **(₹ in Crores)**

Profit and Loss Account (Summary) year ended…..						
Comparable 2	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	152	134	155	143	157	741
(3)Total Cost	118	129	140	128	135	674
(4)Net profit [=(2) – (3)]	34	5	15	15	22	91
(5)Net cost plus mark-up [=(4)/(3) *100]	28.81%	3.88%	10.71%	11.72%	16.30%	----
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	----	----	----	----	----	13.50%

Comparable Company 3 **(₹ in Crores)**

Profit and Loss Account (Summary) year ended…..						
Comparable 3	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	15	13	15	14	17	74
(3)Total Cost	13	12	14	12	15	66
(4)Net profit [=(2) – (3)]	2	1	1	2	2	8
(5)Net cost plus mark-up [=(4)/(3) *100]	15.38%	8.33%	7.14%	16.67%	13.33.%	----

(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	----	----	----	----	----	12.12%

Comparable Company 4 **(₹ in Crores)**

Profit and Loss Account (Summary) year ended…..						
Comparable 4	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	215.38	183.68	176.85	244.73	267.57	1088.21
(3)Total Cost	191.21	162.55	169.29	212.11	223.34	958.50
(4)Net profit [=(2) – (3)]	24.17	21.13	7.56	32.62	44.23	129.71
(5)Net cost plus mark-up [=(4)/ (3) *100]	12.64%	13.00%	4.47%	15.38%	19.80%	----
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	----	----	----	----	----	13.53%

Comparable Company 5 **(₹ in Crores)**

Profit and Loss Account (Summary) year ended…..						
Comparable 5	**March 2012**	**March 2013**	**March 2014**	**March 2015**	**March 2016**	**Total**
(1)Time period	12 mnths	12 mnths	12 mnths	12 mnths	12 mnths	
(2)Total Income	231.15	138.89	157.86	424.37	327.75	1280.02
(3)Total Cost	211.29	132.46	129.19	392.21	303.34	1168.49
(4)Net profit [=(2) – (3)]	19.86	6.43	28.67	32.16	24.41	129.71
(5)Net cost plus mark-up [=(4)/ (3) *100]	9.40%	4.85%	22.19%	8.20%	8.05%	----
(6)Weighted Average [= {Total of col. (4)/ Total of col. (3)} x 100]	----	----	----	----	----	11.10%

Summary of Net Cost Plus Mark-ups of broadly comparable independent companies

Sl No.	Company name	March 2012	March 2013	March 2014	March 2015	March 2016	Weighted average
1	Comparable 1	5.93%	10.8%	10.71%	4.69%	10.06%	8.61%
2	Comparable 2	28.81%	3.88%	10.71%	11.72%	16.30%	13.50%
3	Comparable 3	15.38%	8.33%	7.14%	16.67%	13.33.%	12.12%
4	Comparable 4	12.64%	13.00%	4.47%	15.38%	19.80%	13.53%
5	Comparable 5	9.40%	4.85%	22.19%	8.20%	8.05%	11.10%
	Arithmetic Mean	14.43%	8.17%	11.04%	11.33%	13.51%	11.77%

Conclusion: On the basis of the above, the Net Cost-plus mark-ups of broadly comparable independent companies range from 8.61% to 13.53% with an arithmetical mean of 11.77%.

Scenario 1: *where Happy Ltd's margin is below the arm's length mark-up but within the range permissible under the proviso to Sec.92C (2)*

Profit & Loss Account for the year ended 31st March, 2016 [All figures in Rupees '000]

Particulars	**Col. 1**			**Col. 2**		**Col.3**		**Col.4**
	Actual	**At ALP**	**Refer Note No.**		**At ALP (+) 3% of ALP**		**At ALP (-)3% of ALP**	
(a) Revenue								
-From associated enterprises (international transaction)	93,500	96,122	2	ALP	1,00,928	ALP (+)3%	93,238	**ALP (-) 3%**
Total Operating Income	**93,500**	**96,122**			**1,00,928**		**93,238**	
(b)Costs (all unrelated, no international transactions)								
Pay roll	40,000	40,000			40,000		40,000	
Rent	16,500	16,500			16,500		16,500	
Depreciation	9,500	9,500			9,500		9,500	
General administration exp.	8,200	8,200			8,200		8,200	
Other operating expenses	11,800	11,800			11,800		11,800	
Total Operating expenses	**86,000**	**86,000**			**86,000**		**86,000**	
(c)**Operating Profit** [= (a) – (b)]	7,500	10,122	1		14,928		7,238	
Net Cost Mark-up (%)	8.72%							
Arm's length mark-up [i.e. arithmetical mean of the Net Cost Plus mark-up(%) of broadly comparable independent companies]		11.77%						
Range of net cost plus mark-ups that would be considered compliant with the arm's length standard applying the +/- 3% variation permitted by proviso to Sec.92C(2) [= Operating Profit / Operating expenses]					17.36%		8.42%	

Notes:

4. Operating profit in Col.2 is a derived figure by applying mark-up of 11.77% to the tested party's total operating expenses of ₹86,000

5. (a) Revenue from associated enterprises (international transaction) in Col.2 is the balancing figure considering operating profit derived in Col.1 above and the total operating expenses remaining unchanged at ₹86,000. This revenue figure is the Arm's Length Price (ALP).

(b) Revenue from associated enterprises (international transaction) in Col.3 represents the upper limit of the range permissible under the proviso the Section 92C(2)

(c) Revenue from associated enterprises (international transaction) in Col.4 represents the lower limit of the range permissible under the proviso the Section 92C(2)

6. The Net Cost Plus Mark-up of 8.72% earned by the tested party (col.1) even though below the arm's length Net Cost plus mark-up (col.2), still falls within the range permissible under the proviso to Section 92C(2) [Col.(3) & (4)] . Hence no adjustment needs to be made.

Scenario 2: Where Happy Ltd's margin falls below the lower limit of the range of permissible under the proviso

Profit & Loss Account for the year ended 31st March, 2016 [All figures in Rupees '000]

Particulars	**Col. 1**			**Col. 2**		**Col.3**		**Col.4**
	Actual	**At ALP**	**Refer Note No.**		**At ALP (+) 3% of ALP**		**At ALP (-)3% of ALP**	
(a) Revenue								
-From associated enterprises (international transaction)	91,000	96,122	2	ALP	1,00,928	ALP (+)3%	93,238	**ALP (-) 3%**
Total Operating Income	91,000	96,122			1,00,928		93,238	
(b)Costs (all unrelated, no international <u>transactions)</u>								
Pay roll	40,000	40,000			40,000		40,000	
Rent	16,500	16,500			16,500		16,500	
Depreciation	9,500	9,500			9,500		9,500	
General administration exp.	8,200	8,200			8,200		8,200	
Other operating expenses	11,800	11,800			11,800		11,800	
Total Operating expenses	**86,000**	**86,000**			**86,000**		**86,000**	
(c)**Operating Profit** [=(a) – (b)]	5,000	10,122	1		14,928		7,238	
Net Cost Mark-up (%)	5.82%							
Arm's length mark-up [i.e. arithmetical mean of the Net Cost Plus mark-up(%) of broadly comparable independent companies]		11.77%						
Range of net cost plus mark-ups that would be considered compliant with the arm's length standard applying the +/- 3% variation permitted by proviso to Sec.92C(2) [= Operating Profit / Operating expenses]					17.36%		8.42%	

Notes:

5. Operating profit in Col.2 is a derived figure by applying mark-up of 11.77% to the tested party's total operating expenses of ₹86,000

6. (a) Revenue from associated enterprises (international transaction) in Col. 2 is the balancing figure considering operating profit derived in Col.1 above and the total operating expenses remaining unchanged at ₹86,000. This revenue figure is the Arm's Length Price (ALP).

   (b) Revenue from associated enterprises (international transaction) in Col.3 represents the upper limit of the range permissible under the proviso the Section 92C (2).

   (c) Revenue from associated enterprises (international transaction) in Col.4 represents the lower limit of the range permissible under the proviso the Section 92C (2).

7. The Net Cost Plus Mark-up earned by the tested party (col.1) falls below the lower limit of the range permissible under proviso 92C(2) [Col.(4)] . This situation may expose the tested party to an adjustment to the price charged by it in its international transaction. Such adjustment, if recommended to be made by the TPO to the AO should amount to ₹2,238 As explained hereunder.

8. Quantum of adjustment:

(v)	Value of the international transaction	91,000
(vi)	Arm's length price	96,122
(vii)	Arm's length price applying the proviso to Sec.92C(2)	93,238
(viii)	Adjustment (iii) – (i)	2,238

Case Study 3:

ABC ENGINEERING INC

The use of Cost Accounting Principles could lead to establishment of an Arms' Length Price which is different from the price arrived at by assessee in the TP Study Report.

The objective of our study would be to find out whether the Arms Length Price (ALP) worked out using CPM was in accordance with generally accepted cost accounting principles.

The assessee had a revenue model that was based on a man-hour rate with it's AE. Institute is finding was that the assessee was computing the total cost incurred over the entire available man-hours, which included idle time. Institute's contention was that the total cost needed to be segregated into variable costs and fixed costs and for the purpose of computing cost per hour, the variable costs should be computed based on capacity utilized and not on total hours (including idle hours). Cost of fixed expenses could, however, be computed based on total hours (including idle hours).

Computation of cost using CPM (in which it accepted the profit margins adopted by the assessee based on study of comparables) and recommended that the ALP be revised upwards to the tune of ₹55,83,930.

The computation made based on Cost Records are:

Annexure - Computation of Arm's Length Price		
ABC ENGINEERING INC.		
Total available hours	A	172,804
Hours billed to HO for work done	B	47,543
Idle hours billed to HO	C	48,447
External hours billed	D	16,465
Total billed hours	E=B+C+D	112,455
Capacity utilised for actual work	F= (B+D)*100/A	37.04%
Idle capacity billed	G= C*100/A	28.04%

Idle capacity not billed	H= (A-E)*100/A	34.92%
Total Variable costs reported in Annexure 3 of TP Study Report(₹)		15,399,050
Total actual hours of work done		64,008
Variable Cost per hour (₹)		241
Total Fixed Costs reported in Annexure 3 as per TP Study Report(₹)		54,427,999
Total available hours		172,804
Fixed Cost per hour		315
Total Cost per hour		556
Normal Margin per Hour (on sales)		27.55%
Arms Length charge per hour (CPM)		767
Variation (-5%)		728
Arms Length Price considered by assessee		645
Adjustment required (upward) per hour		83
Total upward adjustment required for the year (₹)		3,946,069
Tax thereon @ 40%		1,578,428
Surcharge @ 2.50%		39,461
		1,617,888
E-Cess /H.S.E-Cess @ 3%		48,537
		1,666,425

COST RECORDS – as an important tool for Assessment under Tax Laws

RELEVANCE OF COST ACCOUNTING PRINCIPLES IN ARM'S LENGTH PRICING

As a concept, the worldwide acceptability of Arm's Length Pricing (aka Transfer Price) as the price at which transactions between Associated Enterprises should take place is no more a matter of debate. It is true that some countries in South America have specific guidelines on Transfer Price which do not match with the methods recommended by the OECD but even those guidelines are generally in keeping with the concept of Arm's Length.

In a business environment in which competitive forces determine revenue earnings, profits are budgeted for by keeping a close control over costs. "Cost Control" is a byword in all corporate across the world and the better one is able to control costs, the more competitive one can price one's product or services.

Global corporations are increasingly centralizing essential functions like purchasing, IT infrastructure, legal service and R & D efforts with the objective of cutting costs and negotiating economies of scale with vendors. As a result, it is quite common now for the parent company to charge a "Management Fee" from its subsidiaries /associated enterprises or apportion a part of costs as a part of "Cost Contribution Arrangements".

The term "Management Fees" is usually used to loosely describe any Inter-Company Transfer that is neither a transfer of tangible property nor one of intangible property. It is often difficult to find comparables for such services or evaluate the benefits received. As a result, tax administrations are generally sceptical about "Management Fees" and consider them to be prone to potential abuse.

There are two views on the issue of Management Fees: Developed nations have adopted rules and regulations on deductibility of Management Fees as an expense so long as it complies with the applicable domestic tax law and Arm's Length Principle. However, other nations do not permit deductibility of these expenses and do not even recognize such kinds of expenses. Such nations impose restrictions by way of exchange controls and withholding taxes thus creating a barrier for such nature of remittances.

Before any structure can be defined for Management Fees, it is vital to establish the following:

- The exact nature of the services to be performed (taking care to exclude "Shareholder Activities").

- Which entities are to render the services and which are to receive the services.

- Actual costs involved in rendering the services.

- Deductibility of the expenses in the recipient country

The structure of the fees, scope of services and other aspects relating to the arrangement may be documented in the form of a written agreement (bilateral or multilateral) and would also require evidence of costs incurred and services actually rendered. Additionally, country-specific documentation should be added wherever applicable. A recent trend that has been discussed is that tax administrations are now seeking to establish that a direct benefit has resulted and the benefits are not indirect.

As mentioned earlier, for such nature of services, it is not easy to establish a comparable with an independent party. When a comparable cannot be established, the usual preference is to use the CPM (Cost Plus Method). **This requires establishing the costs, which may be ascertained by using an appropriate cost accounting method**. Furthermore, care should also be taken to distinguish between what constitutes a reimbursement and what constitutes a service function. Subject to the limitations discussed above, it would be appropriate to add a cost markup on the actual costs of the service function.

Cost sharing is based on the idea that a number of group companies/related companies may get together to fund the costs of research and development of new technologies or know-how. By sharing in the costs, each participant in the CCA obtains a right to the R&D. As soon as viable commercial opportunity arises, each participant may choose to exploit the opportunity optimally.

While the concept of **cost sharing** is simple, there are complex accounting and regulatory issues that arise in practice from such arrangements. For example, if the costs include cost of equipments /machinery, how will this be captured in the books of accounts of the participating entities. Will this be capitalized or charged to revenue? Should there be a profit markup in sharing?

There are benefits, too, that arise from cost sharing. For example, it may eliminate the need to pay royalties for transfer of intangible properties because each of the participants, by being a co-funder of the expenses, is entitled to enjoy the fruits of the intangible. Secondly, cost sharing is also a means of financing of R&D. Since related entities /group companies may be expected to benefit from R&D activity carried out by one of the entities (usually the parent company or a Research Centre), if they do not share the costs, it leads to a situation where the related entities get benefits at the cost of one entity only. Cost sharing eliminates this inequity.

A valid CCA between related entities involves a written agreement, signed preferably before commencement of the R&D work, to share the costs and risks of the R&D effort under mutual direction and benefit. Each participant agrees to bear a part of the costs and risks and in turn reaps proportionate benefits.

Acceptance of CCAs by all tax administrations has not happened yet but these are being recognized more and more by different administrations.

The strongest theoretical basis for cost allocation is by reference to the actual benefits derived from the activity (it is respectfully suggested that a recent ruling by the ITAT in the matter of Dressner Rand may not reflect international thought in this matter). However, all R&D expenditure may not necessarily result in commercially exploitable situations and there must be a method of dealing with abortive expenditure as well as successful expenditure. It is because of this that the preferred method of cost allocation is referenced to expected benefit. This calculation, however, is very complicated and may not be economical to perform. In practice, considerable weight is given to expected sales/revenue of each participant.

An important point to be remembered in this connection is that while tax administrations, in general, prefer to follow OECD guidelines in the matter of CCAs, some tax administrations have designed and brought into force special regulations dealing with these: For example, Article 41 of the Corporate Income Tax Law of China; Guidelines on CCAs issued in March 2006 by Japan; Taxation Ruling 2004/1 issued by Australia etc.

As mentioned earlier, a key issue is on the deductibility of expenses under CCAs. Should they be revenue expenditure of capital expenditure. There is no prescribed guideline on this and the accounting and tax treatment shall have to follow local tax law.

A more fundamental issue is on the proportion of costs charged under a CCA and whether this is reasonable. Tax administrations may wish to examine the CCA at a group level rather than at company level to examine this matter. A considerable amount of disclosure may be required to be made by the group in this matter and consequently, the documentation required for this is of crucial importance. From a practical standpoint, it should be remembered that examination by tax authorities is with the benefit of hindsight whereas when CCAs are entered into, it is on the basis of foresight. Therefore, there may be instances of abortive expenditure which tax administrations may use to relook at the expected benefits (and consequently the proportion of sharing).

In general, whether one is talking about Management Fees or Cost Contribution Arrangements, the Cost Plus Method & Transactional Net Margin Method are of increasing relevance in view of the fact that with such levels of globalization, it is difficult and complex to use CUP as the method of establishing transfer prices because comparables are more and more difficult to identify. In fact, it is expected that once India introduces Advance Pricing Arrangements, the Transactional Net Margin Method will be more commonly applied that CUP or CPM.

General Anti Avoidance Rule (GAAR)

Applicable of general anti- avoidance rule [Sec.95]

General Anti Avoidance Rules (GAAR) have been inserted with effect from April 1, 2014. The following explanation is given in the "Memorandum Explaining the provision in the Finance Bill, 2012" –

" The question of substance over form has consistently arisen in the implementation of taxation laws. In the Indian context, judicial decisions have varied. While some courts in certain circumstances had held that legal form of transactions can be dispensed with and the real substance of transaction can be considered while applying the taxation laws, others have held that the form is to be given sanctity. The existence of anti- avoidance principles is based on various judicial pronouncements. There are some specific anti-avoidance provisions but general anti-avoidance has been dealt only through judicial decisions in specific cases.

In an environment of moderate rates of tax, it is necessary that the correct tax base be subject to tax in the face of aggressive tax planning and use of opaque low tax jurisdictions for residence as well as for sourcing capital. Most countries have codified the "substance over form" doctrine in the form of General Anti Avoidance Rule (GAAR).

In the above background and keeping in view the aggressive tax planning with the use of sophisticated structures, there is a need for statutory provision so as to codify the doctrine of "substance over form" where the real intention of the parties and effect of transactions and purpose of an arrangement is taken into account for determining the tax consequences, irrespective of the legal structure that has been superimposed to camouflage the real intent and purpose. Internationally several countries have introduced, and are administering statutory General Anti Avoidance provisions. It is, therefore, important that Indian taxation law also incorporate a statutory General Anti Avoidance Provisions to deal with aggressive tax planning. The basic criticism of statutory GAAR which is raised worldwide is that it provides a wide discretion and authority to the tax administration which at times is prone to be misused. This vital aspect, therefore, needs to be kept in mind while formulating any GAAR regime."

Impermissible Avoidance Arrangements

An arrangement whose main purpose (or one of the main purposes) is to obtain a tax benefit (and which also satisfies at least one of the four tests), can be declared as an "impermissible avoidance arrangements".

Four tests- The four tests are —

- The arrangement creates rights and obligations, which are not normally created between parties dealing at arm's length.
- It results in misuse or abuse of provisions of tax laws.
- It lacks commercial substance or is deemed to lack commercial substance.
- It is carried out in a manner , which is normally not employed for bona fide purpose

Onus of Proof – In the Finance Bill (as presented in Lok Sabha on March 16, 2012) the onus of establishing that the main purpose of the arrangement is not to obtain tax benefit, was on the taxpayer. However, this provision has been removed at the time of passing of the Finance Bill in Lok Sabha.

Lack of commercial substance – An arrangement will be deemed to lack commercial substance if-

a. The substance or effect of the arrangements as a whole, is inconsistent with, or differs significantly from, the form of its individual steps or a part ; or

b. It involves or includes-

   i. Round trip financing;

   ii. An accommodating party:

   iii. elements that have effect of offsetting or cancelling each other; or

   iv. a transaction which is conducted through one or more persons and disguises the value, location, source, ownership or control of fund which is subject matter of such transaction; or

c. it involves the location of an asset or of a transaction or of the place of residence of any party which is without any substantial commercial purpose other than obtaining tax benefit for a party

   - **Round trip financing**- For the above purpose round trip financing includes any arrangement in which, through a series of transaction –

a. funds are transferred among the parties to the arrangement; and

b. such transactions do not have any substantial commercial purpose other than obtaining the tax benefit, without having any regard to –

   - whether or not the funds involved in the round trip financing can be traced to any funds transferred to, or received by, any party in connection with the arrangement;
   - the time or sequence, in which the funds involved in the round trip financing are transferred or received; or
   - the means by, or manner in or mode through, which funds involved in the round trip financing are transferred or received.

It is also provided that certain circumstances like period of existence of arrangement, taxes arising from arrangement, exit route, shall not be taken into account while determining 'lack of commercial substance' test for an arrangement.

Consequences of an impermissible avoidance arrangement – Once the arrangement is held to be an impermissible avoidance arrangement then the consequences of the arrangement in relation to tax or benefit under a tax treaty can be determined by keeping in view the circumstances of the case, however, some of the illustrative steps are –

a. Disregarding or combining any step of the arrangement,

b. Ignoring the arrangement for the purpose of taxation law,

c. Disregarding or combining any party to the arrangement,

d. Reallocating expenses and income between the parties to the arrangement,

e. Relocating place of residence of a party, or location of a transaction or situs of an asset to a place other than provided in the arrangement,

f. Considering or looking through the arrangement by disregarding any corporate structure, and

g. Re-characterizing equity into debt, capital into revenue, etc.

- These provisions can be used in addition to or in conjunction with other anti-avoidance provisions or provisions for determination of tax liability, which are provided in the taxation law.
- For effective application in cross border transaction and to prevent treaty abuse, a limited treaty override is also provided.

Procedure for invoking GAAR

The procedure for invoking GAAR is as under-

1. The Assessing Officer shall make a reference to the Commissioner for invoking GAAR and on receipt of reference the commissioner shall hear the taxpayer and if he is not satisfied by the reply of taxpayer and is of the opinion that GAAR provision are to be invoked, he shall refer the matter to an Approving Panel. In case the assessee does not object or reply, the Commission shall make determination as to whether the arrangements is an impermissible avoidance arrangement or not.
2. The Approving Panel has to dispose of the reference within a period of 6 months from the end of the month in which the reference was received from the Commissioner.
3. The Approving Panel shall either declare an arrangement to be impermissible or declare it not to be so, after examining material and getting further inquiry to be made.
4. The Assessing Officer will determine consequences of such a positive declaration of arrangement as impermissible avoidance arrangement.
5. The final order in case any consequence of GAAR is determined shall be passed by the Assessing Officer only after approval by the Commissioner and, thereafter, first appeal against such order shall lie to the Appellate Tribunal.
6. The period taken by the proceedings before the Commissioner and Approving Panel shall be excluded from time limitation for completion of assessment.
7. The Board will set-up an Approving Panel consisting of not less than 3 members being —
   a. Income – tax authorities (not below the rank of Commissioner) and
   b. An official of the Indian Legal Service (not below the rank of Joint Secretary.)
8. The panel will have a minimum of three members. The procedure and working of Panel shall be administered through subordinate legislation.
9. In addition to the above, it is provided that the Board shall prescribe a scheme for regulating the condition and the manner of application of these provisions.

Advance Pricing Agreement Scheme (APA)

Advance Pricing Agreement (APA) [Section 92CC & 92CD] [W.e.f. 1.7.2012]

Advance Pricing Agreement is an agreement between a taxpayer and a taxing authority on an appropriate transfer pricing methodology for a set of transactions over a fixed period of time in future.

The APAs offer better assurance on transfer pricing methods and are conducive in providing certainty and unanimity of approach.

New sections 92CC and 92CD have been inserted in the Act to provide a framework for advance pricing agreement under the Act.

Advance pricing agreement (APA) [Section 92CC]

Section 92CC (1): It empowers Board, to enter into an advance pricing agreement with any person undertaking an international transaction.

Such Advance Pricing Agreements (APAs) shall include determination of the arm's length price or specify the manner in which arm's length price shall be determined, in relation to an international transaction to be entered into by that person.

Section 92CC (2): The manner of determination of arm's length price in such cases shall be any method including those provided in section 92C (1), with such adjustments or variations as may be necessary or expenditure so to do.

Section 92CC (3): The arm's length price of any international transaction, which is covered under such APA, shall be determined in accordance with the APA so entered and the provisions of section 92C or section 92CA which normally apply for determination of arm's length price would be modified to this extent and arm's length price shall be determined in accordance with APA.

Section 92CC(4): The APA shall be valid for such previous year as specified in the agreement which in no case shall exceed five consecutive previous years.

Section 92CC (5): The APA shall be binding only:

(a) on the person in whose case, and in respect of the transaction in relation to which, the agreement has been entered into; and

(b) on the Commissioner, and the income-tax authorities subordinate to him, in respect of the said person and the said transaction.

Section 92CC (6): The APA shall not be binding if there is any change in law or facts having bearing on such APA.

Section 92CC (7): The Board is empowered to declare, with the approval of Central Government, any such agreement to be void ab initio, if it finds that the agreement has been obtained by the person by fraud or misrepresentation of facts.

Section 92CC (8):

(a) Once an agreement is declared void ab initio, all the provisions of the Act shall apply to the person as if such APA had never been entered into, and

(b) For the purpose of computing any period of limitation under the Act, the period beginning with the date of such APA and ending on the date of order declaring the agreement void ab initio shall be excluded. However if after the exclusion of the aforesaid period, the period of limitation referred to in any provision of the Act is less than sixty days, such remaining period shall be extended to sixty days.

Section 92CC (9): The Board is empowered to prescribe a Scheme providing for the manner, form, procedure and any other matter generally in respect of the advance pricing agreement.

Section 92CC(9A): The agreement referred to in sub-section (1), may, subject to such conditions, procedure and manner as may be prescribed, provide for determining the arm's length price or specify the manner in which arm's length price shall be determined in relation to the international transaction entered into by the person during any period not exceeding four previous years preceding the first of the previous years referred to in sub-section (4), and the arm's length price of such international transaction shall be determined in accordance with the said agreement.

Section 92CC (10): Where an application is made by a person for entering into such an APA, proceedings shall be deemed to be pending in the case of the person for the purposes of the Act like for making enquiries under section 133(6) of the Act.

Effect to Advance Pricing Agreement [Section 92CD]

Section 92CD (1): The person entering in to such APA shall necessarily have to furnish a modified return within a period of three months from the end of the month in which the said APA was entered in respect of the return of income already filed for a previous year to which the APA applies. The modified return has to reflect modification to the income only in respect of the issues arising from the APA and in accordance with it.

Section 92CD (2): Except as otherwise provided in this section. All the other provisions of this Act shall apply accordingly as if the modified return is a return furnished under section 139.

Section 92CD (3): If the assessment or reassessment proceedings for an assessment year relevant to a previous year to which the agreement applies has been completed before the expiry of period allowed for furnishing of modified return, the Assessing Officer shall, in a case where modified return is filed, proceed to assess or reassess or recomputed the total income of the relevant assessment year having regard to and in accordance with the APA and to such assessment, all the provisions relating to assessment shall apply as if the modified return is a return furnished under section 139 of the Act.

In this case, notwithstanding anything contained in section 153 or section 153B or section 144C, the order of assessment, reassessment or recomputation of total income under section 92CD(3) shall be passed within a period of one year from the end of the financial year in which the modified return under section 92CD(1) is furnished [Section 92CD(5) (a)].

Section 92CD (4): Where the assessment or reassessment proceedings for an assessment year relevant to the previous year to which the agreement applies are pending on the date of filing of modified return, the Assessing Officer shall proceed to complete the assessment or reassessment proceedings in accordance with the agreement taking into consideration the modified return so filed.

In this case, notwithstanding anything contained in section 153 or section 153B or section 144C, the period of limitation as provided in section 153 or section 153B or section 144C for completion of pending assessment or reassessment proceedings referred to in section 92CD(4) shall be extended by a period of twelve months. [Section 92CD(5)(b)].

Meaning of expressions used in matters in respect of advance pricing agreement.

10F For the purposes of this rule and rules 10G to 10T,–

(a) 'agreement' means an advance pricing agreement entered into between the Board and the applicant, with the approval of the Central Government, as referred to in sub-section (1) of section 92CC of the Act;

(b) "application" means an application for advance pricing agreement made under rule 10 I ;

(c) "bilateral agreement" means an agreement between the Board and the applicant, subsequent to, and based on, any agreement referred to in rule 44 GA between the competent authority in India with the competent authority in the other country regarding the most appropriate transfer pricing method or the arms' length price;

(d) "competent authority in India" means an officer authorised by the Central Government for the purpose of discharging the functions as such for matters in respect of any agreement entered into under section 90 or 90A of the Act;

(e) "covered transaction" means the international transaction or transactions for which agreement has been entered into;

(f) "critical assumptions" means the factors and assumptions that are so critical and significant that neither party entering into an agreement will continue to be bound by the agreement, if any of the factors or assumptions is changed;

(g) "most appropriate transfer pricing method" means any of the transfer pricing method, referred to in sub-section (1) of section 92C of the Act, being the most appropriate method, having regard to the nature of transaction or class of transaction or class of associated persons or function performed by such persons or such other relevant factors prescribed by the Board under rule 10B and 10C;

(h) "multilateral agreement" means an agreement between the Board and the applicant, subsequent to, and based on, any agreement referred to in rule 44GA between the competent authority in India with the competent authorities in the other countries regarding the most appropriate transfer pricing method or the arms' length price;

(i) "tax treaty" means an agreement under section 90, or section 90A, of the Act for the avoidance of double taxation;

(j) "team" means advance pricing agreement team consisting of income-tax authorities as constituted by the Board and including such number of experts in economics, statistics, law or any other field as may be nominated by the Director General of Income Tax (International Taxation);

(k) "unilateral agreement" means an agreement between the Board and the applicant which is neither a bilateral nor multilateral agreement.

Persons eligible to apply

10G Any person who –

(i) has undertaken an international transaction; or

(ii) is contemplating to undertake an international transaction,

shall be eligible to enter into an agreement under these rules.

Pre-filing Consultation

10H (1) Every person proposing to enter into an agreement under these rules shall, by an application in writing, make a request for a pre-filing consultation.

(2) The request for pre-filing consultation shall be made in Form No. 3 CEC to the Director General of Income Tax (International Taxation).

(3) On receipt of the request in Form No. 3 CEC, the team shall hold pre-filing consultation with the person referred to in rule 10G.

(4) The competent authority in India or his representative shall be associated in pre-filing consultation involving bilateral or multilateral agreement.

(5) The pre-filing consultation shall, among other things,-

  (i) determine the scope of the agreement;

  (ii) identify transfer pricing issues;

  (iii) determine the suitability of international transaction for the agreement;

  (iv) discuss broad terms of the agreement.

(6) The pre-filing consultation shall–

  (i) not bind the Board or the person to enter into an agreement or initiate the agreement process;

  (ii) not be deemed to mean that the person has applied for entering into an agreement.

Application for advance pricing agreement

10I (1) Any person, who has entered into a pre-filing consultation as referred to in rule 10H may, if desires to enter into an agreement furnish an application in Form No. 3 CED alongwith the requisite fee.

(2) The application shall be furnished to Director General of Income Tax (International Taxation) in case of unilateral agreement and to the competent authority in India in case of bilateral or multilateral agreement.

(3) Application in Form No. 3 CED may be filed by the person referred to in rule 10G at any time–

  (i) before the first day of the previous year relevant to the first assessment year for which the application is made, in respect of transactions which are of a continuing nature from dealings that are already occurring; or

  (ii) before undertaking the transaction in respect of remaining transactions.

(4) Every application in Form No. 3 CED shall be accompanied by the proof of payment of fees as specified in sub-rule (5).

Withdrawal of application for agreement

10 J (1) The applicant may withdraw the application for agreement at any time before the finalisation of the terms of the agreement.

(2) The application for withdrawal shall be in Form No. 3CEE.

(3) The fee paid shall not be refunded on withdrawal of application by the applicant.

Preliminary processing of application

10 K (1) Every application filed in Form No. 3CED shall be complete in all respects and accompanied by requisite documents.

(2) If any defect is noticed in the application in Form No. 3CED or if any relevant document is not attached thereto or the application is not in accordance with understanding reached in pre-filing consultation referred to in rule 10H, the Director General of Income-tax (International Taxation) (for unilateral agreement) and competent authority in India (for bilateral or multilateral agreement) shall serve a deficiency letter on the applicant before the expiry of one month from the date of receipt of the application.

(3) The applicant shall remove the deficiency or modify the application within a period of fifteen days from the date of service of the deficiency letter or within such further period which, on an application made in this behalf, may be extended, so however, that the total period of removal of deficiency or modification does not exceed thirty days.

(4) The Director General of Income Tax (International Taxation) or the competent authority in India, as the case may be, on being satisfied, may pass an order providing that application shall not be allowed to be proceeded with if the application is defective and defect is not removed by applicant in accordance with sub-rule (3).

(5) No order under sub-rule (4) shall be passed without providing an opportunity of being heard to the applicant and if an application is not allowed to be proceeded with, the fee paid by the applicant shall be refunded.

Procedure

10 L (1) If the application referred to in rule 10K has been allowed to be proceeded with, the team or the competent authority in India or his representative shall process the same in consultation and discussion with the applicant in accordance with provisions of this rule.

(2) For the purpose of sub-rule (1), it shall be competent for the team or the competent authority in India or its representative to–

  (i) hold meetings with the applicant on such time and date as it deem fit;

  (ii) call for additional document or information or material from the applicant;

  (iii) visit the applicant's business premises; or

  (iv) make such inquiries as it deems fit in the circumstances of the case.

(3) For the purpose of sub-rule (1), the applicant may, if he considers it necessary, provide further document and information for consideration of the team or the competent authority in India or his representative.

(4) For bilateral or multilateral agreement, the competent authority shall forward the application to Director General of Income Tax (International Taxation) who shall assign it to one of the teams.

(5) The team, to whom the application has been assigned under sub-rule (4), shall carry out the enquiry and prepare a draft report which shall be forwarded by the Director General of Income Tax (International Taxation) to the competent authority in India.

(6) If the Applicant makes a request for bilateral or multilateral agreement in its application, the competent authority in India shall in addition to the procedure provided in this rule invoke the procedure provided in the rule 44 GA.

(7) The Director General of Income Tax (International Taxation) (for unilateral agreement) or the competent authority in India (for bilateral or multilateral agreement) and the applicant shall prepare

a proposed mutually agreed draft agreement enumerating the result of the process referred to in sub-rule (1) including the effect of the arrangement referred to in sub-rule (5) of rule 44GA which has been accepted by the applicant in accordance with sub-rule (8) of the said rule.

(8) The agreement shall be entered into by the Board with the applicant after its approval by the Central Government.

(9) Once an agreement has been entered into the Director General of Income Tax (International Taxation) or the competent authority in India, as the case may be, shall cause a copy of the agreement to be sent to the Commissioner of Income Tax having jurisdiction over the assessee.

Terms of the agreement

10 M (1) An agreement may among other things, include –

(i) the international transactions covered by the agreement;

(ii) the agreed transfer pricing methodology, if any;

(iii) determination of arm's length price, if any;

(iv) definition of any relevant term to be used in items (ii) or (iii);

(v) critical assumptions;

(vi) the conditions if any other than provided in the Act or these rules.

(2) The agreement shall not be binding on the Board or the assessee if there is a change in any of critical assumptions or failure to meet conditions subject to which the agreement has been entered into.

(3) The binding effect of agreement shall cease only if any party has given due notice of the concerned other party or parties.

(4) In case there is a change in any of the critical assumptions or failure to meet the conditions subject to which the agreement has been entered into, the agreement can be revised or cancelled, as the case may be.

(5) The assessee which has entered into an agreement shall give a notice in writing of such change in any of the critical assumptions or failure to meet conditions to the Director General of Income Tax (International Taxation) as soon as it is practicable to do so.

(6) The Board shall give a notice in writing of such change in critical assumptions or failure to meet conditions to the assessee, as soon as it comes to the knowledge of the Board.

(7) The revision or the cancellation of the agreement shall be in accordance with rules 10Q and 10R respectively.

Amendments to Application

10 N (1) An applicant may request in writing for an amendment to an application at any stage, before the finalisation of the terms of the agreement.

(2) The Director General of Income Tax (International Taxation) (for unilateral agreement) or the competent authority in India (for bilateral or multilateral agreement) may, allow the amendment to the application, if such an amendment does not have effect of altering the nature of the application as originally filed.

(3) The amendment shall be given effect only if it is accompanied by the additional fee, if any, necessitated by such amendment in accordance with fee as provided in rule 10 I.

Furnishing of Annual Compliance Report

10 O (1) The assessee shall furnish an annual compliance report to Director General of Income Tax (international Taxation) for each year covered in the agreement.

(2) The annual compliance report shall be in Form 3CEF.

(3) The annual compliance report shall be furnished in quadruplicate, for each of the years covered in the agreement, within thirty days of the due date of filing the income tax return for that year, or within ninety days of entering into an agreement, whichever is later.

(4) The Director General of Income Tax (International Taxation) shall send one copy of annual compliance report to the competent authority in India, one copy to the Commissioner of Income Tax who has the jurisdiction over the income-tax assessment of the assessee and one copy to the Transfer Pricing Officer having the jurisdiction over the assessee.

Compliance Audit of the agreement

10 P (1) The Transfer Pricing Officer having the jurisdiction over the assessee shall carry out the compliance audit of the agreement for each of the year covered in the agreement.

(2) For the purposes of sub-rule(1), the Transfer Pricing Officer may require –

(i) the assessee to substantiate compliance with the terms of the agreement, including satisfaction of the critical assumptions, correctness of the supporting data or information and consistency of the application of the transfer pricing method;

(ii) the assessee to submit any information, or document, to establish that the terms of the agreement has been complied with.

(3) The Transfer Pricing Officer shall submit the compliance audit report, for each year covered in the agreement, to the Director General of Income Tax (International Taxation) in case of unilateral agreement and to the competent authority in India, in case of bilateral or multilateral agreement, mentioning therein his findings as regards compliance by the assessee with terms of the agreement.

(4) The Director General of Income Tax (International Taxation) shall forward the report to the Board in a case where there is finding of failure on part of assessee to comply with terms of agreement and cancellation of the agreement is required.

(5) The compliance audit report shall be furnished by the Transfer Pricing Officer within six months from the end of the month in which the Annual Compliance Report referred to in rule 10 O is received by the Transfer Pricing Officer.

(6) The regular audit of the covered transactions shall not be undertaken by the Transfer Pricing Officer if an agreement has been entered into under rule 10L except where the agreement has been cancelled under rule 10R.

Revision of an agreement

10 Q (1) An agreement, subsequent to it having been entered into, may be revised by the Board, if.-

(a) there is a change in critical assumptions or failure to meet a condition subject to which the agreement has been entered into;

(b) there is a change in law that modifies any matter covered by the agreement but is not of the nature which renders the agreement to be non binding ; or

(c) there is a request from competent authority in the other country requesting revision of agreement, in case of bilateral or multilateral agreement.

(2) An agreement may be revised by the Board either *suo-moto* or on request of the assessee or the competent authority in India or the Director General of Income Tax (International Taxation).

(3) Except when the agreement is proposed to be revised on the request of the assessee, the agreement shall not be revised unless an opportunity of being heard has been provided to the assessee and the assessee is in agreement with the proposed revision.

(4) In case the assessee is not in agreement with the proposed revision the agreement may be cancelled in accordance with rule-10R.

(5) In case the Board is not in agreement with the request of the assessee for revision of the agreement, the Board shall reject the request in writing giving reason for such rejection.

(6) For the purpose of arriving at the agreement for the proposed revision, the procedure provided in rule 10 L may be followed so far as they apply.

(7) The revised agreement shall include the date till which the original agreement is to apply and the date from which the revised agreement is to apply.

Cancellation of an agreement

10 R (1) An agreement shall be cancelled by the Board for any of the following reasons:

- (i) the compliance audit referred to in rule 10P has resulted in the finding of failure on the part of the assessee to comply with the terms of the agreement;
- (ii) the assessee has failed to file the annual compliance report in time;
- (iii) the annual compliance report furnished by the assessee contains material errors; or
- (iv) the agreement is to be cancelled under sub-rule (4) of rule 10Q.

(2) The Board shall give an opportunity of being heard to the assessee, before proceeding to cancel an application.

(3) The competent authority in India shall communicate with the competent authority in the other country or countries and provide reason for the proposed cancellation of the agreement in case of bilateral or multilateral agreement.

(4) The order of cancellation of the agreement shall be in writing and shall provide reasons for cancellation and for non acceptance of assessee's submission, if any.

(5) The order of cancellation shall also specify the effective date of cancellation of the agreement, where applicable.

(6) The order under the Act, declaring the agreement as *void ab initio*, on account of fraud or misrepresentation of facts, shall be in writing and shall provide reason for such declaration and for non acceptance of assessee's submission, if any.

(7) The order of cancellation shall be intimated to the Assessing Officer and the Transfer Pricing Officer, having jurisdiction over the assessee.

Renewing an agreement

10 S Request for renewal of an agreement may be made as a new application for agreement, using the same procedure as outlined in these rules except pre filing consultation as referred to in rule 10H.

Miscellaneous

10 T (1) Mere filing of a application for an agreement under these rules shall not prevent the operation of Chapter X of the Act for determination of arms' length price under that Chapter till the agreement is entered into.

(2) The negotiation between the competent authority in India and the competent authority in the other country or countries, in case of bilateral or multilateral agreement, shall be carried out in accordance with the provisions of the tax treaty between India and the other country or countries.".

(b) after rule 44G of the principal rules, the following rule shall be inserted, namely.-

Roll back provision in Advance Pricing Agreement Scheme [Section 92CC] [W.e.f. 1-10-2014]

Section 92CC provides for Advance Pricing Agreement (APA). It empowers the Central Board of Direct Taxes, with the approval of the Central Government, to enter into an APA with any person for determining the Arm's Length Price (ALP) or specifying the manner in which ALP is to be determined in relation to an international transaction which is to be entered into by the person. The agreement entered into is valid for a period, not exceeding 5 previous years, as may be mentioned in the agreement. Once the agreement is entered into, the ALP of the international transaction, which is subject matter of the APA, would be determined in accordance with such an APA.

In many countries the APA scheme provides for "roll back" mechanism for dealing with ALP issues relating to transactions entered into during the period prior to APA. The "roll back" provisions refers to the applicability of the methodology of determination of ALP, or the ALP, to be applied to the international transactions which had already been entered into in a period prior to the period covered under an APA. However, the "roll back" relief is provided on case to case basis subject to certain conditions. Providing of such a mechanism in Indian legislation would also lead to reduction in large scale litigation which is currently pending or may arise in future in respect of the transfer pricing matters.

Therefore, the Act has inserted section 92CC(9A) to provide that the agreement referred to in section 92CC(1) (i.e. APA) may, subject to such conditions, procedure and manner, as may be prescribed provide for determining the arm's length price or specify the manner in which arm's length price shall be determined in relation to an international transaction entered into by the person during any period not exceeding four previous years preceding the first of the previous years referred to in section 92CC(4) and the arm's length price of such international transaction shall be determined in accordance with the said agreement.

"Procedure to deal with requests for bilateral or multilateral advance pricing agreements.

44GA

(1) Where a person has made request for a bilateral or multilateral advance pricing agreement in an application filed in Form No. 3 CED in accordance with rule 10 I, the request shall be dealt with subject to provisions of this rule.

(2) The process for bilateral or multilateral advance pricing agreement shall not be initiated unless the associated enterprise situated outside India has initiated process of advance pricing agreement with the competent authority in the other country.

(3) The competent authority in India shall, on intimation of request of the applicant for a bilateral or multilateral agreement, consult and ascertain willingness of the competent authority in other country or countries, as the case may be, for initiation of negotiation for this purpose.

(4) In case of willingness of the competent authority in other country or countries, as the case may be, the competent authority in India shall enter into negotiation in this behalf and endeavour to reach a set of terms which are acceptable to the competent authority in India and the competent authority in the other country or countries, as the case may be.

(5) In case of an agreement after consultation, the competent authority in India shall formalise a mutual agreement procedure arrangement with the competent authority in other country or countries, as the case may be, and intimate the same to the applicant.

(6) In case of failure to reach agreement on such terms as are mutually acceptable to parties mentioned in sub-rule 4, the applicant shall be informed of the failure to reach an agreement with the competent authority in other country or countries.

(7) The applicant shall not be entitled to be part of discussion between competent authority in India and the competent authority in the other country or countries, as the case may be; however the applicant can communicate or meet the competent authority in India for the purpose of entering into an advance pricing agreement.

(8) The applicant shall convey acceptance or otherwise of the agreement within thirty days of it being communicated.

(9) The applicant, in case the agreement is not acceptable may at its option continue with process of entering into an advance pricing agreement without benefit of mutual agreement process or withdraw application in accordance with rule 10J ".

(c) In Appendix-II of the principal rules, after Form No. 3 CEB, the following Forms shall be inserted, namely: -

"Form No. 3CEC (See sub-rule (2) of rule 10 H)	**Application for a pre-filing meeting**
Form No. 3 CED (See sub-rule (1) of rule 10 I)	**Application for an Advance Pricing Agreement I. General II. Functional analysis III. Industry and market analyses IV. Transfer pricing background V. Transfer Pricing Methodology analysis: VI. Impact of proposed TPMs**
Form No. 3 CEE (See sub-rule (2) of rule 10 J)	**Application for withdrawal of APA request**
Form No. 3 CEF (See sub-rule 2 of rule 10 O)	**Annual Compliance Report on Advance Pricing Agreement**

Notes

Notes