DIRECT TAX – RECENT JUDGMENT

CA. Paras Savla, CA. Ketan Vajani

1. Explanation – 1 to sec. 37(1) – Loss on account of penalty or confiscation – covered by the Explanation – Not an allowable loss

A search was conducted by the DRI in the premises of the assessee. During the course of search, unrecorded slabs of silver were confiscated by the DRI under the provisions of the Customs Act. The Income-tax department made addition in respect of the same u/s. 69A of the Act. The appeal of the assessee before the CIT (A) and the Tribunal were dismissed. Before the Rajasthan High Court, the assessee claimed that the silver slabs were confiscated and hence the deduction in respect of the same shall be allowed as the business loss. The Rajasthan High Court allowed the claim of business loss relying on the judgment of the Supreme Court in the case of *CIT vs. Piara Singh 124 ITR 41 (SC).*

On revenue's appeal to the Supreme Court, the Supreme Court held that the word 'any expenditure' mentioned in Section 37 of the Act takes in its sweep loss occasioned in the course of business, being incidental to it. Consequently, any loss incurred by an assessee for any purpose which is an offence or which is prohibited by law is not deductible in terms of Explanation 1 to section 37 of the Act. Such an expenditure / loss shall not be deemed to have been incurred for the purpose of business or profession or incidental to such business or profession. Accordingly, a penalty or confiscation cannot be said to be incidental to any business.

CIT v. Prakash Chand Lunia (D) Thr. Lrs. [2023] 147 taxmann.com 416 (SC)

2. Sec. 153A of the Act – Assessment in the case of Search – Addition to be made only in case of incriminating material found during the search

In a case where a search or requisition is conducted, the assessing officer assumes jurisdiction for block assessment under Section 153A of the Act. All pending assessments/reassessments will stand abated, meaning they will no longer be valid. If any incriminating material is found during the search, the assessing officer can assess or reassess the total income, taking into consideration the incriminating material and other material available with the assessing officer, including the income declared in the returns.

However in a case where no incriminating material is found during the search, the assessing officer cannot make any additions to the completed / unabated assessments. At the same time, the assessing officer can re-open the completed assessments under the provisions of section 147 / 148 of the Act. Such reassessment proceedings will be subject to fulfilment of all the conditions provided under those sections.

Pr. CIT vs. Abhisar Buildwell P. Ltd. [2023] 149 taxmann.com 399 (SC)

3. Sec. 153C of the Act – Amendment made w.e.f. 1-6-2015 with respect to incriminating material pertaining to third party – Amendment also applicable to searches prior to 1-6-2015

Section 153C of the Act had been amended by the Finance Act 2016 w.e.f. 1-6-2015. Prior to the amendment, the section provided for proceeding against persons other than the person searched on the basis of the seizure of the books of accounts or documents seized or requisitioned if such material "belongs or belong to" a person other than the searched person. On account of the interpretation of these words by certain judicial pronouncements, a situation emerged where, though incriminating material pertaining to a third party / person was found during search proceedings under Section 132, the Revenue could not proceed against such a third party. This necessitated the legislature / Parliament to clarify by substituting the words "belongs or belong to" to the words "pertains or pertain to" and to remedy the mischief.

Considering the above object and purpose of section 153C, held that the amendment made by the Finance Act, 2015 shall also apply to searches conducted before 1-6-2015. The contention of the assessees that by way of amendment to Section 153C by Finance Act, 2015, it brings into its fold, the assessees – persons, who were not so far covered by it and, therefore, it affects the substantive rights of the assessees was rejected by the Supreme Court for the reason that even the unamended Section 153C pertained to the assessment of

income of any other person and the amendment was with the purpose to remedy the mischief. The Supreme Court further held that if the interpretation as canvassed on behalf of the respective respondents is accepted, in that case, even the object and purpose of Section 153C namely, for assessment of income of any other person (other than the searched person) shall be frustrated. Any interpretation, which may frustrate the very object and purpose of the Act / Statute shall be avoided by the Court.

ITO v. Vikram Sujitkumar Bhatia [2023] 149 taxmann.com 123 (SC) ; ACIT v. Shruti Bhamasha Shah [2023] 149 taxmann.com 271 (SC)

4. Sec. 271C of the Act – Penalty for failure to deduct Tax at Source – Penalty not to be levied in case of belated payment of tax deducted

The assessee company was engaged in software development business. The assessee deducted tax at source in respect of salaries, contract payments etc. but deposited same belatedly - Addl. CIT levied penalty under section 271C and subsequently an order under section 201(1A) was passed levying penal interest. The High Court upheld the said order of Addl. CIT on the ground that failure to deduct or remit TDS would attract penalty under section 271C.

On appeal, the Supreme Court noted that provision of section 271C(1)(a) shall be applicable in case of a failure on part of assessee to "deduct" whole of any part of tax. The Supreme Court further observed that wherever parliament wanted to have consequence of non-payment and/or belated remittance/payment of TDS, Parliament/Legislature had provided same like in section 201(1A) and section 276B. The Supreme Court also took note of the CBDT's Circular No. 551, dated 23-1-1998 which states that if there was any delay in remitting tax, it would attract payment of interest under section 201(1A) and because of gravity of mischief involve it would involve prosecution proceedings as well under section 276B. In view of the above, the Supreme Court held that it was not a case of non-deduction of TDS at all and thus assessee was not liable to pay penalty under section 271C.

US Technologies International (P.) Ltd. v. CIT [2023] 149 taxmann.com 144 (SC)

5. Sec. 80-IB of the Act – Deduction not available for profit earned from DEPB / Duty Drawback Scheme

The assessee had claimed benefit of deduction u/s. 80-IB of the Act in respect of the DEPB / Duty Drawback Scheme. This was disallowed by the assessing officer and the order of the assessing officer was eventually confirmed by the High Court.

On appeal to the Supreme Court – held that Duty Entitlement Pass Book (DEPB) / Duty Drawback Scheme is not related to the business of an industrial undertaking for manufacturing or selling its products and the DEPB entitlement arises only when the undertaking goes on to export the said product, that is, after it manufactures or produces the same. In view of the same, the High Court has rightly held that the assessee is not entitled to the deductions under Section 80-IB on the amount of DEPB as well as Duty Drawback Schemes.

Saraf Exports v. CIT [2023] 149 taxmann.com 145 (SC)

6. Sec. 6(3) of the Act – Test of Residency for a company

The assessee company claimed that it was registered in the state of Sikkim and hence the income was claimed to be exempt under the Income tax Act and liable to tax under Sikkim Manual. The assessing officer, the CIT(A) and also the High Court had denied the said claim of the assessee based on the material on record that the control and management of the affairs of the assessee Sikkim companies was with a chartered accountant and he was not merely associated with assessee companies on professional basis but also exercised the control and management from Delhi.

On appeal to the Supreme Court held that the domicile or the registration of the company is not at all relevant and the determinate test is where the sole right to manage and control of the company lies. Control and management means not merely theoretical control and power, i.e., not de jure control and power, but de facto control and power actually exercised in the course of the conduct and management of the affairs of the firm. Considering the fact that the control and management was exercised from Delhi, just because commission was earned in Sikkim, it cannot be held that income was earned in Sikkim and same could not be held to be exempt from Income tax under the Act and liable to tax under Sikkim Manual.

Mansarovar Commercial Pvt. Ltd. v. CIT [2023] 149 taxmann.com 178 (SC)

7. Sec. 263 of the Act – Orders prejudicial to the Interest of Revenue

The assessee company's property was sold for Rs. 33 Crores. Against the same, the company claimed deduction of Rs. 31.05 Crore on account of payments made to shareholders with a view to give effect to arbitral award for settling disputes among company's shareholders who were members of a family. This was allowed as cost of improvement in the original assessment. The CIT invoked the powers u/s. 263 of the Act and held that the deduction of Rs. 31.05 Crores cannot be treated as cost of improvement since the same is not covered within

the meaning of the term as provided in section 55(1)(b) of the Act. The Tribunal however held that the order of the assessing officer cannot be said to be erroneous since it followed one of the possible views of the matter. The order of the Tribunal was also confirmed by the High Court.

On revenue's appeal to the Supreme Court, it was held that the assessing officer's order was clearly erroneous and also prejudicial to the interest of revenue within the meaning of section 263 of the Act since the order had erroneously accepted the claim of the assessee in relation to the cost of improvement in contravention of section 55(1)(b) of the Act. The High Court has committed an error in setting aside the order passed by the CIT u/s. 263 of the Act. Accordingly the order of the CIT as passed u/s. 263 of the Act was restored.

CIT v. Paville Projects Pvt. Ltd. [2023] 149 taxmann.com 115 (SC)

8. Sec. 148 and Sec. 148A of the Income-tax Act – Notices issued during the period from 1-4-2021 to 30-6-2021 for the assessment years 2013-14 and 2014-15 – Validity of such notices

Writ petitions were filed by the assessee(s) challenging the validity of notices issued u/s. 148A of the Act in relation to assessment years 2013-14 and 2014-15 following the judgment of the Supreme Court in the case of Ashish Agarwal.

The Gujarat High Court held that the limitation of six years from end of relevant assessment year operated as timeline in old regime for issuance of notice under section 148 beyond which period, it was not competent for Assessing Officer to issue notice for reassessment. This embargo is made to continue in new regime also and thus, all original notices under section 148 referable to old regime and issued between 1-4-2021 to 30-6-2021 would stand beyond prescribed permissible timeline of six years from end of assessment year 2013-14 and assessment year 2014-15. Therefore, all such notices when they would relate to assessment year 2013-14 or assessment year 2014-15 would be time barred as per provisions of Act as applicable in old regime prior to 1-4-2021. Further, these notices could not be issued as per amended provision of Act. In view of above, impugned notices in respective petitions under section 148 , relatable to assessment year 2013-14 or assessment year 2014-15, as case may be, were beyond permissible time limit, therefore, liable to be treated as illegal and without jurisdiction.

Sita Creation Pvt. Ltd. v. ITO [2023] 149 taxmann.com 357 (Gujarat) ; Wallstone Ceramin v. DCIT [2023] 149 taxmann.com 358 (Gujarat) ; Bhagchand Jain HUF v. ITO [2023] 149 taxmann.com 365 (Gujarat)

9. Sec. 115O of the Act - Impact of tax applicable on Dividend in the case of Non-resident Shareholders under DTAA

Where dividend is declared, distributed or paid by a domestic company to a non-resident shareholder(s), which attracts Additional Income Tax (Tax on Distributed Profits) referred to in Sec.115-O, such additional income tax payable by the domestic company shall be at the rate mentioned in Section 115-O and not at the rate of tax applicable to the non-resident shareholder(s) as specified in the relevant DTAA with reference to such dividend income. However, wherever the Contracting States to a tax treaty intend to extend the treaty protection to the domestic company paying dividend distribution tax, only then, the domestic company can claim benefit of the DTAA, if any.

DCIT v. Total Oil India Pvt. Ltd. [2023] 149 taxmann.com 332 (Mum.)(SB)