SERVICE TAX

SERVICE TAX VOLUNTARY COMPLIANCE ENCOURAGEMENT SCHEME (VCES) MADE EFFECTIVE FROM 10TH MAY 2013

The VCES introduced in Budget 2013 for service tax defaulters came into force on 10th May 2013.

This is a one-time amnesty scheme for service tax defaulters to pay tax dues for the period 1st October 2007 to 31st December 2012.

A declaration must be submitted to the designated authority in 'Form VCES-1' after payment of tax to get immunity from any penalty or late payment charges for not obtaining service tax registration, non-filing of returns or delayed filing of returns.

DIRECT TAX

INCOME TAX RETURNS FORMS AND PROCEDURE FOR FILING MODIFIED

The Forms for filing income tax returns are modified for A.Y. 2013-14 and onwards. The manner of filing returns has been changed.

- Henceforth, the Tax audit reports, Transfer Pricing Reports and MAT certificates have to be submitted electronically. The procedure, standards and format of filing such audit reports will be prescribed in the amended Rules.

- It is mandatory to file returns electronically for all assessees except for those filing Form ITR-7 and having income of not more than Rs.5,00,000/-

- Non-corporate assesses have to disclose their overseas income and assets (such as foreign bank account number, offshore trusts, etc).

- Non-corporate assessees having Taxable (Total Income) income of more than Rs.25,00,000 have to disclose their personal assets at cost and liabilities against the assets owned, if filing Forms ITR-3 and ITR-4.

- IFSC code for the bank account number has to be given instead of the MICR code in all tax forms.

[Notification No. 34/2013 dated 1st May 2013]

SUMMARY OF IMPORTANT JUDGEMENTS:

Unless otherwise stated, the sections mentioned hereunder relate to the Income Tax Act, 1961.

Sr. No	Tribunal / Court	Area/ Section covered	Nature	Case Law
1	ITAT Mumbai	Speculative Transaction: *Sections 43(5)*	Loss on foreign currency forward contracts by a manufacturer / exporter is a "speculation loss" and not a "hedging loss"	S. Vinodkumar Diamonds Pvt. Ltd vs. ACIT
2	Gujarat High Court	Speculative Transaction: *Section 43(5)*	Loss on foreign currency forward contracts by a manufacturer / exporter is a "hedging loss" and not a "speculation loss"	CIT vs. Friends And Friends Shipping Pvt. Ltd
3	Gujarat High Court	Amounts not deductible: *Section 40(a)(ia)*	TDS: Special Bench verdict in Merilyn Shipping is not good law	CIT vs. Sikandarkhan N. Tunvar
4	ITAT Kolkata	Expenditure on exempt income: *Section 14A*	Rule 8D disallowance without showing how assessee is wrong is not permissible	DCIT vs. Ashish Jhunjhunwala
5	ITAT Mumbai	Deduction on actual payment: *Sections 43B and 36(1)(va)*	Employees' PF / ESI Contribution is not covered by s. 43B & is only allowable as a deduction u / s 36(1)(va) if paid by the "due date" prescribed therein (i.e. under relevant statute)	ITO vs. LKP Securities Ltd
6	Uttarakhand High Court	Due date for actual payment: *Sections 43B and 36(1)(va)*	"Due date" in s. 36(1)(va) for payment of employees' Provident Fund, ESIC etc contribution should be read with s. 43B(b) to mean "due date" for filing ROI	CIT vs. Kichha Sugar Company Ltd

7	Calcutta High Court	Concealment of income: *Sections 271*	No s. 271(1)(c) penalty for not offering capital gains on s. 50C stamp duty value	CIT vs. Madan Theatres
8	ITAT Chennai	Transfer Pricing: *Section 92C*	Method of discounted cash flow can be used for share valuation if other methods of sec. 92C are not applicable	Ascendas (India) P. Ltd vs. DY.CIT

1) Loss on foreign currency forward contracts by a manufacturer/ exporter is a "speculation loss" and not a "hedging loss"

[S. Vinodkumar Diamonds Pvt. Ltd vs. ACIT (Mumbai – Tribunal)]

Dated: 7th May 2013

The assessee, a dealer in diamonds, entered into forward contracts in US dollars. Some of the contracts were cancelled during the year and some were outstanding at the end of the year. The assessee suffered a loss of Rs. 4.02 crores on account of the cancellation and "marked to market" of the said forward contracts and claimed that sum as a deduction.

The AO & CIT(A), relied on Instruction No. 03/2010 dated 23-3-2010 and held that the said loss arose on account of a "speculative transaction" while the assessee claimed that it arose out of a "hedging transaction".

HELD by the Tribunal:

There is a difference between a "speculative transaction" and a "hedging transaction". Section 43(5) defines a "speculative transaction" to mean 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 the actual delivery or transfer of the commodity or scrips. Proviso (a) to s. 43(5) refers to a "hedging transaction" as a contract in respect of raw materials or merchandise entered into by a person in the course of his manufacturing or merchandising business to guard against loss through future price fluctuations in respect of his contracts for actual delivery of goods manufactured by him or merchandise sold by him.

In order for a transaction to be a "hedging transaction", the commodity dealt in should be the same. If the subject matter of the transaction is different, it cannot be termed a hedging transaction. Also, the merchandise in respect of which the forward transactions have been entered into by the assessee must have a direct connection with the goods sold by him.

On facts, as the assessee was not dealing in Foreign Exchange, the forward transactions entered into by it cannot be held to be hedging transactions. As the assessee is dealing in diamonds, only the forward contracts entered into for diamonds would be covered by Proviso (a) to s. 43(5). Consequently, the loss suffered by the assessee is a speculative loss.

2) Loss on foreign currency forward contracts by a manufacturer/ exporter is a "hedging loss" and not a "speculation loss"

[CIT vs. Friends And Friends Shipping Pvt. Ltd (Gujarat High Court)]

Dated: 9th May 2013

The assessee, an exporter, entered into forward contracts with Banks to hedge against any loss arising out of fluctuation in foreign currency. The forward contract provided that the assessee would buy some quantity of dollars at a particular rate to cover export bill payment. The contract gave delivery option dates and the assessee had the option to cancel the contract and pay the loss to the Bank. The assessee suffered a loss of Rs. 15 lakhs on such cancellation.

The AO & CIT(A) held that the loss constituted a "speculation loss" u/s 43(5) and could not be allowed as a deduction. On appeal, the Tribunal upheld the assessee's claim.

On appeal by the department, HELD dismissing the appeal:

Though the assessee is not a dealer in foreign exchange, it entered into forward contracts with banks for the purpose of hedging the loss due to fluctuation in foreign exchange while implementing the export contracts. The transactions in foreign exchanges were incidental to the assessee's regular course of business and the loss was thus not a speculative loss u/s 43(5) but was incidental to the assessee's business and allowable as such.

The fact that there may have been no direct co-relation between the exchange document and the precise export contract cannot be seen in isolation if there are in fact several separate contracts with the bankers.

The contrary view in S. Vinodkumar Diamonds (ITAT Mumbai) is not good law as it overlooked Badridas Gauridu 261 ITR 256 (Bom)

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3) S. 40(a)(ia) TDS: Special Bench verdict in Merilyn Shipping is not good law

[CIT vs. Sikandarkhan N. Tunvar (Gujarat High Court)]

The assessee, engaged in the business of transport contractor and commission agent, incurred expenditure of Rs. 8.74 crores on payment to contractors where no TDS was deducted.

The AO & CIT(A) held that the expenditure had to be disallowed u/s 40(a)(ia). On appeal, the Tribunal, relying on **Merilyn Shipping &**

Transports 146 TTJ 1 (Viz) (SB) held that as the said amount had already been paid and was not "payable" as of 31st March, the disallowance u/s 40(a)(ia) could not be made.

On appeal by the department to the High Court, HELD reversing the Tribunal:

In **Merilyn Shipping** 146 TTJ 1 (Viz) (SB) the majority held that as the Finance Bill proposed the words "*amount credited or paid*" and as the Finance Act used the words "*amounts payable*", s. 40(a)(ia) could only apply to amounts that are outstanding as of 31st March and not to amounts already paid during the year. This view is not correct for two reasons.

Firstly, a strict reading of s. 40(a)(ia) shows that all that it requires is that there should be an amount payable of the nature described, which is such on which tax is deductible at source but such tax has not been deducted or if deducted not paid before the due date. The provision nowhere requires that the amount which is payable must remain so payable throughout during the year. If the assessee's interpretation is accepted, it would lead to a situation where the assessee who, though was required to deduct the tax at source but no such deduction was made or more flagrantly deduction though made is not paid to the Government, would escape the consequence only because the amount was already paid over before the end of the year in contrast to another assessee who would otherwise be in similar situation but in whose case the amount remained payable till the end of the year. There is no logic why the legislature would have desired to bring about such irreconcilable and diverse consequences.

Secondly, the principle of deliberate or conscious omission is applied mainly when an existing provision is amended and a change is brought about. The Special Bench was wrong in comparing the language used in the draft bill to that used in the final enactment to assign a particular meaning to s. 40(a)(ia). Accordingly, **Merilyn Shipping** does not lay down correct law. The correct law is that s. 40(a)(ia) covers not only to the amounts which are payable as on 31th March of a particular year but also which are payable at any time during the year.

This decision from the High Court is overruling decision of Special Bench (Vizag ITAT) covered in our previous Newsletter.

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4) No Section 14A / Rule 8D disallowance without showing how assessee is wrong

[DCIT vs. Ashish Jhunjhunwala (ITAT Kolkata)]

In AY 2009-10, the assessee earned tax-free dividend of Rs. 32 lakhs on investments that had been made in earlier years. The assessee claimed that as he had not incurred any expenditure to earn the dividend income, no disallowance u/s 14A was permissible.

The AO rejected the claim and made a disallowance by applying Rule 8D. The CIT(A) deleted the disallowance on the ground that the AO had mechanically applied Rule 8D to compute the disallowance.

On appeal by the department to the Tribunal, HELD dismissing the appeal:

The AO has not brought on record anything which proves that there is any expenditure incurred towards earning of dividend income. The AO has not examined the accounts of the assessee and there is no satisfaction recorded by the AO about the correctness of the claim of the assessee and without the same he invoked Rule 8D.

While rejecting the claim of the assessee with regard to expenditure or no expenditure, as the case may be, in relation to exempted income, the AO has to indicate cogent reasons for the same. The AO has not considered the claim of the assessee and straight away embarked upon computing disallowance under Rule 8D of the Rules on presuming the average value of investment at 0.5% of the total value. This is not permissible.

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5) Employees' PF/ ESI Contribution is not covered by Section 43B & is only allowable as a deduction u/s 36(1)(va) if paid by the "due date" prescribed therein

[ITO vs. LKP Securities Ltd (ITAT Mumbai)]

In AY 2008-09 the assessee collected employees' contribution to the Provident Fund and ESIC but did not pay it within the due date prescribed by the relevant legislation. The amount was, however, paid before the due date of filing the ROI.

The AO assessed the said amounts as income u/s 2(24)(x) but declined to grant a deduction u/s 36(1)(va) as the amount had been paid after the due date. The CIT(A), relying on Alom Extrusions 319 ITR 306 (SC) and AIMIL321 ITR 508 (Del) held that the amounts had to be allowed as a

deduction u/s 43B as they had been paid before filing the ROI.

On appeal by the department to the Tribunal, HELD reversing the CIT(A):

S. 43B covers only the sums payable by way of contribution by the assessee as an employer, i.e., the employer's contribution to the PF and ESI funds. It does not cover the employees' contribution. While the employer's contribution is allowable u/s 37(1), the employees' contribution collected by the employer is deemed to be his income u/s 2(24)(x) and is allowable as a deduction u/s 36(1)(va) only if it is paid to the relevant fund by the due date as prescribed in the relevant legislation.

Even if one assumes that s. 43B(b) applies to s. 36(1)(va) payments, a deduction would not be admissible because the s. 36(1)(va) payments are not 'otherwise allowable' if they are paid beyond the "due date".

The decisions in Vinay Cement 213 CTR (SC) 268 & Alom Extrusions 319 ITR 306 (SC) are not an authority on the point that employees' contributions are also covered by s. 43B. Though in AIMIL 321 ITR 508 (Del) it was held that employees' contribution to EPF and ESI funds are covered by s. 43B, it cannot be followed because:

i. The Court moved on the premise that employees' contribution is subject to clause (b) of s. 43B and did not notice the condition in s. 36(1)(va),
ii. The decision by the tribunal, which was approved by the High Court in AIMIL was rendered without considering the decision of the Special Bench in ITC Ltd **and**
iii. It is inconsistent with Godaveri (Mannar) Sahakari 298 ITR 149 (Bom).

Accordingly, AIMIL cannot be followed and the deductibility of employees' contribution has to be seen only with reference to s. 36(1)(va) (together with grace period).

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6) "Due date" in s. 36(1)(va) for payment of employees' Provident Fund, ESIC etc contribution should be read with s. 43B(b) to mean "due date" for filing ROI

[CIT vs. Kichha Sugar Company Ltd (Uttarakhand High Court)]

The assessee collected employees' Provident Fund contribution for payment to the provident fund

authorities. However, the amount was not paid to the provident fund authorities within the "due date" specified in the Provident Fund Act though it was paid before the due date of filing the return of income.

The AO assessed the amounts received as income u/s 2(24)(x) but refused to allow a deduction u/s 36(1)(va) on the ground that the amounts were not paid within the prescribed "due date". The CIT(A) and Tribunal allowed the assessee's claim for deduction u/s 43B(b). The Department filed an appeal in the High Court claiming that s. 43B did not apply to employees' contribution.

HELD by the High Court dismissing the appeal:

Section 2(24)(x) provides that the amounts of employees' contribution to PF, etc. collected by the employer shall be assessed as his income. Section 36(1)(va) provides that the said employees' contribution shall be allowed as a deduction if paid within the "due date" specified in the relevant legislation. Section 43(B)(b) provides that any sum payable by the assessee as an employer by way of contribution to any provident fund etc shall be allowed if paid before the due date of filing the ROI.

The "due date" referred to in s. 36(1)(va) must be read in conjunction with s. 43B(b) to mean the "due date" of filing the ROI. The AO wrongly proceeded on the basis that the "due date" in s. 36(1)(va) is the due date fixed by the Provident Fund authority, whereas read in the context of s. 43B(b) it is the "due date" fixed for filing the ROI.

Note: The same view is taken in AIMIL 321 ITR 508 (Del) & Bharati Shipyard 132 ITD 53 (SB)(Mum). However, the ITAT Mumbai has refused to follow this law in LKP Securities on the ground that s. 43B applies only to "employer's contribution"

7) No Section 271(1)(c) penalty for not offering capital gains on Section 50C stamp duty value

[CIT vs. Madan Theatres (Calcutta High Court)]

The assessee sold property for a consideration of Rs. 2.50 crore. However, for the purpose of stamp duty, the property was valued at Rs. 5.19 crore and stamp duty was paid on that value. The assessee offered capital gains on the basis that the sale consideration was Rs. 2.50 crore.

The AO invoked s. 50C and held that the sale consideration had to be taken

at Rs. 5.19 crore and capital gains computed on that basis. The AO imposed penalty u/s 271(1)(c) which was deleted by the CIT(A) ~~and there by relying on Renu Hingorani~~.

On appeal by the department to the High Court, HELD dismissing the appeal:

Though the assessee could have disputed the valuation on the basis of the deemed value and chose not to do so, the fact remains that the actual amount received was offered for taxation. It is only on the basis of the deemed consideration that the proceedings u/s 271(1)(c) started. The revenue has failed to produce any iota of evidence that the assessee actually received one paise more than the amount shown to have been received by him. As such, there is no scope to admit the appeal.

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8) Method of discounted cash flow can be used for share valuation if other methods of Sections 92C are not applicable

[Ascendas (India) P. Ltd vs. DY.CIT (Chennai - Tribunal)]

In the instant case, the assessee-company owning 84.97% of shareholding of AITPCL India, an Indian company, entered into a contract with its Foreign associate company (AE) for sale of its stake in AITPCL.

The TPO valued the shares using discounted cash flow method and made Transfer Pricing adjustment. The objections filed by the assessee were rejected by the Dispute Resolution Panel. Aggrieved assessee filed instant appeal.

The Tribunal held as under:

As per Section 92C, ALP in relation to an international transaction has to be determined by one of the six methods mentioned therein;

Re-sale price Method couldn't be applied in the instant case because the shares sold by the assessee were, in turn, not sold to anybody else. Cost Plus Method couldn't be applied since assessee had made no value addition to any item. Original cost per share was only its face value, and the cost incurred which resulted in increase of its intrinsic value couldn't be correctly ascertained. Neither Profit Split Method nor TNM Method could be used. Further, similar companies doing similar share transactions were hard to find;

Purpose of transfer pricing rules is to verify whether the prices at which an international transactions have been carried out is comparable with the market value of the underlying asset or commodity or service. This might require some subtle adjustments in the methodology prescribed for evaluation of an international transaction;

A water-tight attitude of interpretation of the prescribed methods will defeat the very purpose of enactment of transfer pricing rules and regulations and also detrimentally affect the effective and fair administration of an international tax regime;

Interpretation of the word 'shall' need not always be mandatory and could also be read as 'may', is a rule laid down by the Gujarat High Court in the case of CIT v.Gujarat Oil & Allied Industries [1993] 201 ITR 325;

Hence, while finding the most appropriate method, it is not that modern valuation methods fitting the type of underlying service or commodities have to be ignored. Fixing enterprise value based on discounted value of future profits or cash flow is a method used worldwide. Endeavour was only at arriving at a value which would give a comparable uncontrolled price for the shares sold. If viewed from this angle, it couldn't be said that the discounted cash flow method adopted by the TPO was not in accordance with section 92C(1).

NOTE: The Judgments should not be followed without studying the complete facts of the case law.

DUE DATES CHART FOR THE MONTH (Various Acts):

Date	Particulars
5th	Service Tax Payment by Companies for May
6th	Payment of Excise Duty for the previous month (other than SSI units)
7th	Income Tax – TDS payment for May
10th	Monthly Excise return by all assessees (except SSIs & EOUs) coming under CEA in Form ER-1
10th	Quarterly Excise return by EOU assessees coming under CEA in Form ER-2
10th	Monthly Excise Return by specified class of Assessees regarding principal units in Form ER-6
15th	Advance Income Tax payment for Companies
15th	Provident fund payment for May
20th	MVAT: TDS Annual Return 2012-13
21st	Payment of contribution under Employees State Insurance Act, 1948
21st	MVAT Monthly Return for May (Tax > Rs.10,00,000/-)
21st	Payment of Monthly MVAT return under MVAT Act, 2002
21st	Filing of Monthly/quarterly/half-yearly return for MVAT
30th	Filing Annual MVAT return by Non-MVAT audit dealers
30th	Profession tax enrolment and payment for the Financial Year 2013-14
30th	Payment of Profession Tax for the employees

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This communication is intended to provide general information, guidance on various professional subjects and should not be regarded as a basis for taking decisions on specific matters. In such instances, separate advice should be taken.