Direct Tax Vista

Your weekly Direct Tax recap

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1. Statement by a data entry operator is not a 'reason to believe' for re-opening

Every Tax Case is unique and incase it is suitably differentiated, it can be successfully argued. In the 15th Edition of Direct Tax Vista we had discussed that The Hon'ble Apex Court in the decision in the case of PRINCIPAL DIRECTOR OF INCOME TAX (INVESTIGATION) & ORS. Vs LALJIBHAI KANJIBHAI MANDALIA [2022-VIL-15-SC-DT] laid down that for a search operation the authority must have information in its possession on the basis of which a reasonable belief can be founded. The relevance of the reasons for the formation of the belief is to be tested by the judicial restraint as in administrative action, as the Court does not sit as a Court of appeal but merely reviews the manner in which the decision was made. The Court shall not examine the sufficiency or adequacy thereof;

However, an admission made by a data entry operator was held to not be a ground on which an AO can jump to the conclusion that since the assessee had transacted with a Company making bogus bills, the assessee is also a beneficiary of bogus bills. Furthermore, the said data entry operator did not name the company. Without any other material, the conclusion drawn by the AO, on receipt of the aforesaid information does not muster the requirement of law to validly form the reason to believe escapement of income. The same was held in the case of PRINCIPAL COMMISSIONER OF INCOME TAX Vs M/s COAL SALE CO. LTD. [2022-VIL-185-CAL-DT]. Herein, it seems that the reasons for the formation of the belief was tested with a judicial knife.

2. Trusts, NGOs, NPOs, Schools/Colleges, Hospitals, etc to start maintaining extensive books of Accounts

Previously, there was no specific provision under the Act providing for the books of accounts to be maintained by trusts or institutions. However, they were required to get Audited. The Finance Act 2022 sought to rectify the anomaly by amending Section 12A(1)(b) to state that to be eligible for exemption u/s 11 or 12 of the Act, the books of account and other documents should be kept and maintained in such form and manner and at such place, as may be prescribed. On the same lines Sec 10(23C) – 10th proviso had been amended to align any university, educational institution, hospital or other medical institution with Sec 12A organisations.

The CBDT has accordingly notified Income-tax (24th Amendment) Rules, 2022 to amend the Income-tax Rules, 1962. A new Rule namely Rule 17AA Books of account and other documents to be kept and maintained has been introduced which is applicable for every fund or institution or trust or any university or other educational institution or any hospital or other medical institutions.

The institutions have to maintain records of all the projects and institutions run by the person, details of income of the person during the previous year, records related to application of income earned during the previous year and application of accumulated income, money invested or deposited, record of voluntary contribution made with a specific direction that they shall form part of the corpus, record of contribution received for the purpose of renovation or repair of temple, mosque, gurdwara, church or other place notified under clause (b) of sub-section (2) of section 80G which is being treated as corpus, record of loans and borrowings, record of properties held by the assessee, record of specified persons, as referred to in sub-section (3) of section 13 of the Act.

Relaxation is provided from keeping and maintaining the books of accounts and other documents at a place other than the registered office in a case where the management has passed a resolution for keeping the prescribed books of accounts and other documents at any other place in India and shall intimate full address of such other place to the jurisdictional Assessing Officer within 7 days thereof. Such books of accounts and other documents shall be maintained for a period of ten years from the end of the relevant assessment year.

Where the assessment in relation to any assessment year has been reopened under section 147 of the Act within the period specified in section 149 of the Act, the books of account and other documents which were kept and maintained at the time of reopening of the assessment shall continue to be so kept and maintained till the assessment so reopened has become final.

3. There cannot be two different yardsticks for the same set of sale transaction made by five co-owners

An addition u/s 50C of the Act and levy of interest u/s. 234A/B/C/D of the Act in the case of one co-owner to the exclusion of other co-owners cannot be done. Differential treatment cannot be met out to another co-owner while making the assessment of the same property or while valuing the same property. It is trite that if during the same assessment year the same quantity of wealth in possession of one co-sharer is subjected to a lower rate of taxation, it would be improper to burden a similarly situated co-sharer with a higher rate of tax. Different treatments cannot be given on the same set of facts in respect of different co-owners of a common property which are subjected to capital gains. This would be against Article 14 of The Constitution. The same was held in the case of SHRI BABUBHAI Vs THE INCOME TAX OFFICER [2022-VIL-1014-ITAT-AHM]

4. Bilateral Netting of Qualified Financial Contracts - Amendments to Prudential Guidelines

Banks and financial institutions enter a multitude of simultaneous financial transactions with each other and their customers. The payables/ receivables arising from them should logically be allowed to be netted. However, ambiguous prior legislations and regulatory interpretations mean that these obligations would not be netted. These invariably inflate capital requirements under the assumption that, in case of a default, the payables would be paid, while the receivables would be paid basis seniority. In this regard, circular DOR.CAP.51/21.06.201/2020-21 dated March 30, 2021 and circular DOR.CAP.REC.No.97/21.06.201/2021-22 dated March 31, 2022 on the captioned subject had been earlier issued. Bilateral netting is a significant reform that helps banks in obtaining benefits of regulatory capital

reduction and sets a mechanism for close-out netting that improves financial stability.

Now, the RBI has clarified w.r.t. Regulated Entities (REs) w.r.t. Exemption or capping in computing capital requirements for counterparty credit risk that the exemption for foreign exchange (except gold) contracts which have an original maturity of 14 calendar days or less shall be applicable to entities calculating the counterparty credit risk under Original Exposure Method without taking the benefit of bilateral netting. Accordingly, the exemption would be applicable only to Regional Rural Banks, Local Area Banks and Co-operative Banks, where the bank has not adopted the bilateral netting framework. For other entities, the exemption shall stand withdrawn. W.r.t. 'sold options', provided the entire premium / fee or any other form of income is received / realised – they can be excluded only when such 'sold options' are outside the netting and margin agreements; For Credit Default Swaps where the bank is the protection seller and that are outside netting and margin agreements - the exposure may be capped to the amount of premium unpaid. Banks have the option to remove such credit derivatives from their legal netting sets in order to apply the cap.

This circular is applicable to all Commercial Banks, Co-operative Banks, Standalone Primary Dealers, Systemically Important Non-Deposit taking Non-Banking Financial Companies (NBFC-ND-SIs), Deposit taking Non-Banking Financial Companies (NBFC-Ds) and Housing Finance Companies (HFCs)

5. If a particular relief is legitimately due to an assessee, the authorities cannot circumscribe it by creating such circumstances leading to its denial

No technicality can be allowed to operate as a speed breaker in the course of dispensation of justice. Hence assessees have to be given opportunity to file information and documents so that a fair decision can be taken. The AO has to consider all the information and documents before deciding whether the return of income is valid or invalid. The assessee cannot be made remediless with no option to claim benefits/exemptions. The decision in this matter in the case of MAHILA

SEVA MANDAL Vs ITO [2022-VIL-998-ITAT-PNE] would apply to not only this case but all such similar cases.

6. Interest on refund mandatory even when it is on “interest deposit”

Even though an amount is deposited towards 'interest' due to the Revenue, there has to be an award of interest on the refund as any interest is only deposited due to an underlying demand raised by the Revenue. Grant of such interest It would not amount to 'interest on interest'. This was held in the case of PCIT-7 VERSUS PUNJAB & SIND BANK (DELHI HC), The judgment of the Supreme Court in the case of Gujarat Fluoro Chemicals arose on issue as regards payment of interest in the event of the failure of Revenue to refund the interest payable within the statutory period. The Supreme Court held that it is the interest provided under the statute which may be claimed by an assessee from the Revenue and no other interest on statutory interest is payable.

7. Site Eviction charges would fulfill the test laid down u/s 37(1)

Real Estate is a business prone to litigation and encroachment of property is not uncommon. If it is argued that since an assessee bought and already encroached property and thus the site eviction charges would not be allowed, many real estate players would have to build in additional tax cost to already high cost of construction. In a relief, in such a matter it was held by The ITAT Chennai that If an assessee is into the business of real estate development, Site Eviction expenditure would fulfill the test laid down u/s 37(1) and it could very well be said that the expenditure was incurred for business purposes of the assessee. However certain pre-conditions need to be satisfied like payments were made through banking channel and acknowledgment / receipts from evictees were produced. Also the assessee should able to produce the evictees who would confirm having received the eviction charges. Merely because the evictees did not have PAN or not assessed to tax, the same would not jeopardize the claim of the assessee. The same was held by M/S. ORCHID FOUNDATIONS PVT. LTD. VERSUS ITO CORPORATE WARD, CHENNAI.

8. Relatives as defined under the Senior Citizens Act is not to be treated at par with ‘relative’ under the Income Tax Act

Casus omissus are ‘cases of omission’. They are situation or circumstance not provided for by legislation; a gap or omission in the law. Courts do not stray into usurping the legislative function so that casus omissus is not created or supplied, so that a statute may not be extended to meet a case for which provision has clearly and undoubtedly not been made. A statutory definition in one context cannot be imported in another Act especially when the two Acts define the same term differently. The same was held in the case of MISS INDIRA UPPAL VERSUS UNION OF INDIA & ANR.

9. No Personal hearing, no draft assessment along with show cause notice as required under section 144B(1) and section 144B(7): Faceless Assessment Order is invalid

Yet another case of denial of Natural Justice in the matter of Faceless Assessments. Section 144B(1)(xii) provides that on receipt of show cause notice, assessee may furnish his response to the National Faceless Assessment Centre and as per clause (xiv), assessment unit shall make a revised draft assessment order after considering the response of the assessee and send it to the National Faceless Assessment Centre. As per the provisions of section 144B(7) in case of variation prejudicial to the assessee as proposed in the draft assessment order, the assessee is entitled to request for personal hearing and upon such request, the personal hearing may be provided by the authority, if the case of the assessee is covered by circumstances provided therein in exercise of powers under sub-clause (h) of clause (xii) of section 144B(7) of the Act, 1961.

If the procedure laid down as per the provisions of section 144B of the Act, 1961 for Faceless assessment, is not followed, it would tantamount to denial of natural justice. The same was held in the case of HIRABEN PRAGIBHAI TALA VERSUS ADDITIONAL/JOINT/DEPUTY/ASSISTANT COMMISSIONER OF INCOME TAX/INCOME TAX OFFICER [GUJ HC]

Hopefully after the issuance of the SOP on faceless Assessments by the NFaC, these matters would reduce. We have discussed the SOP in the 18th Edition of Direct Tax Vista.

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