

Direct Tax Vista

Your weekly Direct Tax recap

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1. Application for re-computation of income for 'Surcharge deduction' taken earlier

The Finance Act 2022 enacted that the term 'tax' would include any surcharge or cess for the purpose of disallowance from business profits [with effect from assessment year (AY) 2005–06]. It was further deemed that the deduction taken in past years with respect to surcharge or cess would be regarded as an under-reported income (for penalty purposes). The Tax Officer would be empowered to pass the necessary rectification order and to recompute the income of taxpayers in respect to such claims. The time limit of four years to process this rectification would begin from 1 April 2022. However, no penalty was to be levied if a suo-moto application in a prescribed form was made by the taxpayer for re-computation of income, without claiming deduction for surcharge or cess and on payment of appropriate taxes (if any) within the prescribed time.

Now, a new Rule 132 alongwith Form 69 is introduced for submitting Application by an Assessee, latest by 31/03/2023, for Re-computation of Income under new IT Section 155(18), as inserted by the Finance Act, 2022, which deals with retrospective disallowance of surcharge/ cess as per amended Section 40(a)(ii). Accordingly, the AO shall modify the assessment order of past years on account of such retrospective disallowance of deduction for surcharge/ cess. Further, new IT Form 70 is meant for intimating the AO about payment of tax on re-computed income u/s 155(18).

2. Exemption u/s 11 cannot be denied to surplus generated from activity sub-servient to the main object

Very many trusts are denied the exemption u/s 11 on a part of their activities which are considered distinct from the core activities and the surplus from such activity is carved out for taxation purpose. Many Tax Practitioners also file the return of income considering such view. In our opinion this is a very narrow view. It is to be considered that If the profits feed a charitable purpose, under the terms of the trust, the mere fact that the activities of the trust yield profit will not alter the charitable character of the trust. The test is very clear that, the genuineness of the purpose should be tested by the obligation created to spend the money exclusively or essentially on charity.

Similar view was again taken in the case of AKASH EDUCATION SOCIETY Vs CIT(A)-I [2022-VIL-1214-ITAT-DEL] where it was held that Transport & Hostel Facilities surplus of a hostel cannot be considered as Business Income of the Society if the same was an integral part of its objects. It is to be considered as sub-servient to the activity of provision of education.

3. Conundrum of Netting of Expenses with Income

Disclosures in financial statements is an aspect of Taxation these days, especially during adjudication. Netting of expenses against Sales should be only as per Accounting Principles, otherwise it could lead to suspicion in the minds of authorities. This is the reason we always advise that incase of reimbursements, incase TDS has been deducted by the Customer, then it is better to disclose the amount in income and claim a corresponding expenditure, so that the P/L A/c matches with the Form 26AS.

However, during appellate stages such anomalies can be sorted where it has been held many times that the provisions of section 69C cannot be applied in the matters where all the purchases and sales transactions are a part of regular books of accounts, even though for the purpose of disclosure in the Financial statements, they may be netted off. The bedrock for making an addition under section 69C is that there must have been some expenditure incurred by the assessee, the source of which is not disclosed. If the expenditure is recorded in the books of accounts, there cannot be any reason to invoke the provisions of section 69C of the Act.

Similarly, it was held in the case of SHRI SADHU RAM Vs THE DCIT [2022-VIL-1229-ITAT-CHD], that Where assessee has offered satisfactory explanation about the source of License Fee paid and the copy of expenditure and sales accounts produced, the addition made by AO u/s 69C cannot be sustained.

4. LSF options available across

Under FEMA regulations, the payment of LSF (Late Submission Fees) is an additional option for regularising reporting delays without undergoing the compounding procedure. Both compounding and LSF options are available to the applicant for the transactions undertaken. The Late Submission Fee (LSF) was introduced for reporting delays in Foreign Investment (FI), External Commercial Borrowings (ECBs) and Overseas Investment related transactions with effect from November 07, 2017, January 16, 2019 and August 22, 2022 respectively. By issuing A.P. (DIR Series) Circular No. 16 dated 30th Sept 2022, LSF has been prescribed across for Form ODI Part-II/ APR, FCGPR (B), FLA Returns, Form OPI, evidence of investment or any other return which does not capture flows or any other periodical reporting 7500 2 FC-GPR, FCTRS, Form ESOP, Form LLP(I), Form LLP(II), Form CN, Form DI, Form InVi, Form ODI-Part I, Form ODI-Part III, Form FC, Form ECB, Form ECB-2, Revised Form ECB or any other return which captures flows or returns which capture reporting of non-fund transactions or any other transactional reporting.

However, the facility for opting for LSF shall be available up to three years from the due date of reporting/ submission.

5. Interest on enhanced compensation is not 'income from other sources' but a capital receipt

The Apex Court in case of Rama Bai versus CIT 181 ITR 400 held that arrears of interest computed on delayed or enhanced compensation shall be taxable on accrual basis. This caused undue hardship to the taxpayers. With a view to mitigate that hardship provisions of Section 145A were amended to provide that the interest received by an assessee on compensation or enhanced compensation shall be deemed to be income for the year in which it was received, irrespective of the

method of accounting followed by the assessee. Further amendment u/s 56 was also made to provide that such income shall be taxable as income from other sources in the year in which it is received.

However, the judicial precedents still held that the interest awarded to landowners u/s 28 of the land acquisition act, 1894 on enhanced compensation is still a part of compensation and is a capital receipt taxable Under the head capital gains. The Department circular 5/2010 dated 3/6 / 2010 also clearly demonstrates the intention of the legislature. The same was upheld in the case of KAMLA DEVI Vs ITO [2022-VIL-1222-ITAT-DEL]

6. RBI Reports show a rosy picture... in contrast to ground realities

The success of predictions depend upon the source of data and its attachment to the ground realities. While speaking to MSME Businesses in the market, this festive season demand scenario does not seem encouraging, yet as per RBI reports published, Manufacturers remained optimistic on demand conditions during Q3:2022-23 as reflected in their expectations on production, order books and employment. Pressures from purchase of raw materials and staff cost are predicted as likely to soften during Q3:2022-23. Selling prices and profit margins are expected to rise further; Overall, as per reports, manufacturers remained optimistic about business conditions: the business expectations index (BEI) remained high at 134.4 in Q3:2022-23 though it moderated marginally from 137.7 in the previous quarter. Consumer confidence for the next one year, as measured by the future expectations index (FEI), remained steady and the expectation at the aggregate level remains close to its level in the previous survey round. However it is expected that inflation will be higher for the next one year ahead periods.

Only time will tell whether this report is a true reflection of the ground realities or not.

7. Interest paid out of interest earned is allowable as a deduction

Incase there is a direct nexus in earning interest on deposits with Bank and payment of interest on the deposits received by an assessee, there cannot be a dispute w.r.t.

the interest income earned by an assessee on deposit made by it. The interest expenditure has to be considered as incurred wholly and exclusively for earning such interest income on Bank deposit. In this case, the interest expenditure has to be allowed to be set off against the interest income. The same was held in the case of INCOME TAX OFFICER Vs M/s CORPORATE GREENS CONDOMINIUM ASSOCIATION [2022-VIL-1212-ITAT-DEL].

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