Direct Tax Vista

Your weekly Direct Tax recap

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1. Fate of "Charitable Activities" cases u/s 2(15) in Income Tax post the Supreme Court's judgement in the case of Ahmedabad Urban Development Authority

The Supreme Court in the case of ACIT (Exemptions) Vs. Ahmedabad Urban Development Authority and Ors. dated 19/10/2022, held as follows in Para 253 & 254-

A. An assessee advancing general public utility (GPU) cannot engage itself in any trade, commerce or business, or provide service in relation thereto for any consideration.

B. However, in the course of achieving the object of GPU, the entity, can carry on trade, commerce or business or provide services in relation thereto for consideration, provided that (1) the activities of trade, commerce or business are connected and (2) the receipt from such business or commercial activity or service in relation thereto, does not exceed the quantified limit, now 20% of total receipts of the previous year, w.e.f. 01.04.2016

C. The charging of any amount towards consideration for such an activity (advancing GPU), which is on cost-basis or nominally above cost, cannot be considered to be "trade, commerce, or business" or any services in relation thereto. It is only when the charges are markedly or significantly above the cost incurred by the assessee in question, that they would fall within the mischief of "cess, or fee, or any other consideration" towards "trade, commerce or business".

D. Section 11(4A) must be interpreted harmoniously with Section 2(15), with which there is no conflict. Carrying out activity in the nature of trade, commerce or business, or service in relation to such activities, should be conducted in the course of achieving the GPU object, and the income, profit or surplus or gains must, therefore, be incidental. The requirement in Section

11(4A) of maintaining separate books of account is also in line with the necessity of demonstrating that the quantitative limit prescribed in the proviso to Section 2015), has not been breached.

E. In every case, the assessing authorities would have to apply their minds and scrutinize the records, to determine if, and to what extent, the consideration or amounts charged are significantly higher than the cost and a nominal mark-up. If such is the case, then the receipts would indicate that the activities are in fact in the nature of "trade, commerce or business" and as a result, would have to comply with the quantified limit

Hence, the entities claiming exemption have to prove the following –

A. That there is no standalone activity in the nature of on trade, commerce or business. If that be so, then separate books of accounts be maintained and the profits be offered for tax.

B. However, in the course of advancing the object of GPU, the entity can carry on ‘connected’ activities in the nature of trade, commerce or business. But, the receipts from these activities should not be more than 20% of the total receipts. The consideration for such connected activities should also be on cost-basis or nominally above cost. How much above cost is not mentioned. But, it is a fact that 15% accumulation is officially allowed by The income tax Act and possibly that could be a benchmark.

In one of the first few orders after the said judgement of The Hon’ble Supreme Court, the ITAT Ahmedabad in the case of THE ACIT (EXEMPTIONS), CIRCLE-1, AHMEDABAD Vs GUJARAT INDUSTRIAL DEVELOPMENT CORPORATION [2023-VIL-870-ITAT-AHM], has held in favour of the assesee. However, the said decision was only due to the fact that the decision of High Court was rendered prior to passing of impugned order and as the matter was already on remanded back to the AO to decide as per the High Court’s Order in favour of the assessee. Hence it was considered that there was no reason for the AO to compute income ignoring provisions of Section 11 and 12 of the Act.

Again, in the case of IMPROVEMENT TRUST Vs THE ACIT [2023-VIL-873-ITAT-CHD] it was held that the objects / activities of the trust were to bring about improvement in the town of Sangrur by providing streets, housing facilities, development of parks, development of roads and other infrastructures, providing drinking water, etc. However, for carrying out all this activity, the Assessee has to incur expenditure on advertisement, quoting tenders in newspapers for sale of land to the general public, and quoting tenders for civil contract works, and all these activities had to be done for fulfilling the main objects, which are charitable in nature. To get the funds for the same, plots were developed and sold at a profit. Hence, it was held that the schemes were driven by public requirements and not as a commercial venture per se, and which schemes are incidental to the main and pre-dominant object of the trust.

A lot of water still would be flowing under the bridge. However, this can be seen as a start of sorts.

2. No deemed dividend u/s 2(22)(e) to other than actual shareholders - beneficial shareholding should not be considered

The intention behind the provisions of section 2(22)(e) of the Act is to tax dividend in the hands of shareholders. The deeming provisions as it applies to the case of loans or advances by a company to a concern in which its shareholder has substantial interest, is based on the presumption that the loans or advances would ultimately be made available to the shareholders of the company giving the loan or advance. Hence on strict interpretation of section 2(22)(e) of the Act, unless the recipient of the amount is the shareholder of the company lending him money, no occasion to apply it can arise. The Hon'ble Karnataka high court in the case of Sarva Equity P. Ltd. (2014) 214 taxmann.com 28(Karnataka) following the ratio of Hon'ble Delhi high court’s decision in the case of National Travels Services held accordingly. The deeming fiction envisaged in section 2(22)(e) of the Act is only with respect to dividend and its scope therefore cannot be enlarged to extend to other than shareholders also. The said proposition was also confirmed in the case Commissioner of Income Tax vs Madhur Housing & Development Co.(2018) 93

taxmann.com 502(SC) and relied upon in the case of DCIT, CIR.1(1)(1) AHMEDABAD Vs AARYAVART INFRASTRUCTURE P. LTD [2023-VIL-871-ITAT-AHM]

3. Assesses' right in Investigation cases

Cases of bogus purchases are investigated by GST as well as Income Tax Authorities. In these cases, there is an allegation of 'cash for cheque' i.e. cheque payments are made by the assessee and are finally withdrawn in cash and the some are handed over to the assessee. Statements of suspicious masterminds are recorded wherein admission is made of providing accommodation bills/entries to various business houses/ business concerns/ entities/persons. However, assesses have bills, vouchers, delivery challans, E-Waybills, proof of delivery, etc. The payment is made vide bank. Hence while the contention of the department cannot be brushed aside, yet the issue cannot be decided without providing full opportunity to assessee also to prove his case.

While there are rights of the department, there are various rights of assesses in these cases, which should be allowed by the department. These rights are to retract statement made under coercion, to not make a deposit of tax under pressure, to not be made to sit in department beyond office hours, etc. Also one of the rights of the assessees is to cross examine the parties who have made a statement against it and an addition made without such cross examination cannot be sustained in view of decision of Hon'ble Gujarat High Court in the case of Chartered Speed Pvt. Limited (Tax Appeal No. 126 of 2015). Hence it was decided to give an opportunity of cross-verifying the witnesses in the case of DATA PROCESSING FORMS PVT. LTD Vs THE DY. CIT, CIRCLE-1(1)(2), AHMEDABAD [2023-VIL-872-ITAT-AHM]

4. No denial of exemption u/s 11 of Income tax for Gratuity Trust

Any trust that has been created for the purpose of managing the statutory obligations of employees of the parent trust would certainly fall within the ambit of advancement of general public utility and, hence, to be considered as a charitable activity as defined u/s 2(15) of the Act. Hence registration u/s 12AA of Income Tax Act have to be provided to such Trusts. The same was held in the case of ICRW

GROUP GRATUITY TRUST Vs CIT (EXEMPTIONS), DELHI [2023-VIL-883-ITAT-DEL]. This judgement would be helpful for all gratuity trusts.

5. Faceless Assessments Issues under Income Tax being decided – Portal cannot be closed without accepting or rejecting adjournment application; Revision u/s 263 cannot normally be invoked

The Faceless assessments regime is evolving and there are multiple issues which are now being taken up by Courts. Many of us have faced situations that adjournments are not granted during faceless assessments and the portal closes leaving assessees remediless. However, cases where adjournment petitions are not reverted to, post further hardship as the whole position becomes uncertain. This is notwithstanding that Section 144B(1)(xii)(b) of The Income Tax Act indicates for faceless assessments that after the show cause notice is issued stating the variations prejudicial to the interest of the assessee, which are proposed to be made to the income of the assessee, he has to be called upon to submit as to why the proposed variation should not be made. Such show cause notice shall be served on the assessee through the National Faceless Assessment Centre. Clause (xiii) of Section 144B(1) mandates the Assessee to file his reply to the show cause notice on the date and time as specified therein or such time as may be extended on the basis of the application made in this regard to the NFAC, which shall forward the reply to the Assessment Unit.

Hence, it was held in the case of SHRI VENKATESH REFINERIES LIMITED Vs DEPUTY COMMISSIONER OF INCOME TAX CIRCLE 1 AND OTHERS [WRIT PETITION NO. 2172 OF 2023 - BOMBAY HIGH COURT] that incase an adjournment petition is made, then the same has to atleast be rejected by The Authorities before closing the portal. This judgement shall be quite useful in similar cases.

Again, another issue is whether Assessment in the faceless cases can be re-opened where it is a fact that any faceless assessment is carried out through a teamwork of assessment unit, technical unit, review unit, verification unit etc. In this regard it was held in the case of M/S. AGRANI BUILDESTATE Vs THE PR. CIT-1 JAIPUR [ITA No. 205/JP/2023] that since different units are headed by Principal Commissioner

of Income Tax, therefore, in a faceless regime, normally there cannot be a case of prejudice of lack of enquiry for the reason that there is application of mind by multiple officers of Department and not by a single officer and thus incase the assessee had furnished the requisite information and the NFAC has completed the assessment after considering all the facts, the order passed by the AO cannot be termed as erroneous.

6. High Seas Sale not speculative

Incase of High Seas sale, the seller neither takes nor gives delivery of goods. It is all executed vide a High Seas Sale agreement. Hence the question arose whether High Seas Sale profit was to be considered as speculative or non-speculative. In this regard it is to be proved that delivery of the goods actually took place to the purchaser in the High Seas Sale. Document need to be produced such as High Seas Sale agreement, bill of lading, BoE filed, Foreign Party's invoice, IGM, Out of Charge, copy of purchased account along with "high sea sale" accounts as per books of account, copy of invoice showing import made by the assessee from outside party as per purchase account and "high sea sale" made on as per sale account, etc which prove that that the said goods are duly taken delivery by the purchaser during the course of purchase from seller. These would prove that it is not a paper transaction or the transfer of the goods before taking the delivery.

Thus, when the goods are not taken by the delivery the entire issue is treated as speculative transaction. But incase the entire transaction is going through by proper delivery of the goods during purchase and the documents are provided for evidence of delivery of goods related to high sea sale, it is non-speculative. The same was held in the case of DY. COMMISSIONER OF INCOME TAX, CIRCLE-I, BATHINDA. VERSUS M/S G.G. CONTINENTAL TRADERS PVT. LTD. AND Oths [I.T.A. No. 506/Asr/2019-ITAT]

7. Taxability of Loan Waivers: Amount not taxable on receipt changes colour when it becomes assessee's own money

Two questions of taxability arise when a loan is waived off –

A. Whether the interest waived off is revenue receipt or capital receipt
B. Whether the principal waived off is revenue receipt or capital receipt

The principle laid down by The Hon'ble Supreme Court in this regard in the case of CIT Vs. TV Sundaram Iyengar & Sons Ltd (1996) 88 Taxman 429 (SC) was that incase an amount is received for working capital purpose, even though it is not taxable in the year of receipt as being of revenue character, the amount changes its character when the amount becomes the assessee's own money because of limitation or by any other statutory or contractual right. However, the Hon'ble Supreme Court in the case of CIT vs. Mahindra & Mahindra (404 ITR 1) has held that wherein it has been held that in a case of a term loan barrowed for acquisition of capital assets, any interest or principal waiver relating to the principal amount cannot be brought to tax either u/s. 28(iv) of the Act, or u/s. 41(1) of the Act.

Now again the definition of "income" as per Section 2(24)(viii) includes –

"*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,-*
(a) 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 clause (1) of section 43; or
*(b) the subsidy or grant by the Central Government for the purpose of the corpus of a trust or institution established by the Central Government or a State Government, as the case may be;];****"***

Again Section 28(iv) requires *that the following income shall be chargeable to income-tax under the head "Profits and gains of business or profession*

(iv) the value of any benefit or perquisite arising from business or the exercise of a profession, whether—
(a) convertible into money or not; or

(b) in cash or in kind or partly in cash and partly in kind;]

Further while clarifying on TDS u/s 194R vide Circular 18/2022, dated 13 September 2022, The CBDT laid down that TDS u/s 194R was not applicable incase of loan waiver by specified institutions. However it made it very clear that this clarification is only for the purposes of section 194R of the Act. The treatment of such settlement/waiver in the hands of the person who had got benefitted by such waiver would not be impacted by this clarification. Taxability of such settlement/waiver in the hands of the beneficiary will be governed by the relevant provisions of the Act.

Therefore, to answer the questions framed above, we refer squarely to the decision of The Hon'ble ITAT in the case of SHARE MICROFIN LTD Vs DY. C. I. T. CIRCLE 3(1) HYDERABAD [2023-VIL-868-ITAT-HYD] and frame our answers as follows –

> A. Interest on a loan which is earlier debited to P/L A/c will be added to the income in the year of waiver of repayment. However, the interest which was earlier capitalised, and in the year of waiver the same is written off from the value of the asset, would be treated as a capital receipt.
> B. The purpose test have to be applied on the Principal loan amount. Incase the principal was taken for working capital purposes, then the loan waiver would be taxed as a revenue receipt. Incase the principal was taken on capital account, then the loan waiver would be taxed as a capital receipt.

Hence the "purpose" for which the loan is taken is material (capital expenditure or revenue expenditure). Incase the loan is taken to run day to day operations, then its waiver is a 'revenue receipt' and incase it is for expansion of an undertaking then it is 'capital receipt'.

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