Direct Tax Vista

Your weekly Direct Tax recap

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1. "Substantial Contributors" Data to be provided by trusts, etc, only "if available"...Reason for non-availability may also be kept ready for assessment purposes

The CBDT issued Circular No. 17/2023, shedding light on crucial audit report requirements to funds, trusts, educational institutions, hospitals, and medical institutions. The circular seeks to provide explicit guidance regarding the reporting of 'substantial contributors' in Form No. 10B or 10BB, a key aspect of tax audits conducted for the assessment year 2023-24. One of the conditions for availing exemptions under Sections 11/12 or Section 10(23C) of The Income Tax Act is a requirement to get the audit of the accounts of the trust or institution registered under Section 12AB or approved under Section 10(23C). The trust or institutions with income exceeding the maximum amount not chargeable to tax are required to get their accounts audited. Form 10B and Form 10BB are audit reports that must be filed by trusts or institutions registered under Section 12AB or approved under Section 10(23C) of the Income-tax Act. Row 41 in annexure to Form no. 10B & Row 28 in annexure to Form no. 10BB seeks details of persons who have made a 'substantial contribution to the trust or institution', that is to say, any person whose total contribution up to the end of the relevant previous year exceeds Rs. 50,000.

Section 13(3)(b) of the Act prescribes any person who has made a substantial contribution to the trust or institution, that is to say, any person whose total contribution up to the end of the relevant previous year exceeds fifty thousand rupees as a specified person. Section 13(3)(d) prescribes any relative of such person as a specified person. Further, section 13(3)(e) of the Act prescribes any concern in which such person or any relative of such person has a substantial interest as a specified person. Now, in the audit reports, form 10 B and form 10BB, the details of

such persons can be provided “if available”. This measure aims to simplify the reporting process for the assessment year 2023-24.

While this circular is to remove difficulties, yet incase this reporting is not done, there is a fair chance that that assesses should be ready with the answer as to why such details “is not available” with them.

2. If Income Tax Demand is on the basis of GST Investigations... then, when GST case is dropped, income tax case should also be dropped

We have already on earlier occasions written about data exchange between Income Tax Authorities and GST/ Indirect Tax Authorities. However, sometimes the officers go beyond too and incase there is an allegation of evasion by either authority, the other authority also moves in the same direction. Hence many a times Income Tax AOs rely on the Central Excise Department’s / GST Department’s Investigation and findings, and these are made basis to conclude that assessee companies are involved in booking bogus purchases through various persons/parties which are found to be non-existing. However, thereafter incase the CESTAT/ GSTAT accepts the claim of the assessee companies that they are engaged into genuine purchases by holding that the allegations are baseless, then the Income tax demand should also be dropped immediately.

The department cannot state that subsequent inquiries made during assessment proceedings can be considered falling in category of seized or incriminating material found during search, so as to validate the assessment u/s 153A. The subsequent proceedings are only of corroborative nature and may be considered relevant to be one for the purpose of ascertaining the extent of evasion. However, the preliminary piece of evidence would be the one allegedly found during the search as was held in the case of ACIT, CENTRAL CIRCLE-19, NEW DELHI Vs SHIVA MINT INDUSTRIES [2023-VIL-1326-ITAT-DEL]

3. Provision for warranty allowed only when it is determined on a scientific basis and as per historical trend

Provision for warranty expenses should have a scientific co-relation with sales of respective years and should not be a mere average of figures of different years. Simple average of warranty expenses of certain no:of years was not considered a scientific method for arriving at a certain percentage or an amount in the case of M/s SENIOR INDIA PRIVATE LIMITED Vs DY.CIT CIRCLE-23(2), DELHI [2023-VIL-1321-ITAT-DEL]. This could lead to a distortion of warranty cost as a percentage to revenue. It was considered a most simple method which can be applied anywhere and everywhere. The Hon'ble Supreme Court in the case Rotork Controls India (P) Ltd 180 Taxman 422 held that the warranty expenses should be computed on the basis of historical trend and scientific methodology. Hence warranty expenses should also see the claims made also on an actual basis over the past few years; further it should factor in process/technology improvements and reduction of warranty costs. Other factors too should be taken into consideration when creating a provision for warranty which can be allowed as a deduction u/s 37 of The Income Tax Act.

4. Are Crates & Pellets Furniture or Plant?

The Hon’ble Bombay High Court in the case of Parle Bisleri Pvt. Ltd. in ITA No.252 of 2002 dated 15.6.2022 held that Crates & Pellets are ‘Plant’, which as per Section 43(3) of The Income Tax Act means to include books, scientific apparatus, etc used for the purposes of the business or profession.

The Division Bench of Rajasthan High Court in the case of Jai Drinks (P.) Ltd. followed the decision of the Supreme Court in the case of Taj Mahal Hotel, where the Supreme Court, after considering the term "Plant" under the provisions of the Act, observed that the same has to be construed in a wide manner. In Taj Mahal Hotel, the Supreme Court construed the definition of "Plant" as occurring in Section 10(5) of the Indian Income-tax Act, 1922 ("the 1922 Act"), which corresponded to Section 43(3) of the 1961 Act. It was held that had the definition of "Plant" was an inclusive definition, and the intention of the Legislature was to give it a wide meaning which is evident from the fact that articles like books and surgical instruments were expressly included in the definition of "Plant".

The word "plant" is to be given a "very wide" meaning. In its ordinary sense, it includes whatever "apparatus" is used by a businessman for carrying on his business, but it does not include his stock-in-trade, which he buys or makes for sale. It, however, includes all goods and chattels, fixed or movable, live or dead, which the tradesman keeps for permanent employment in his business. But the building or the "setting" in which the business is carried on cannot be plant. The thing need not be part of the machine used in the manufacturing process but could be merely an apparatus used in carrying on the business but having a "degree of durability". It may have a passive or an active role. The subject must have a function in the trader's operation and if it has, it is prima facie a plant unless there was good reason to exclude it from that category. It must be a "tool in the trade" of the businessman. Gross materiality or tangibility is not necessary and, in fact, intangible things like ideas and designs contained in a book could be "plant". They fall under the category of "intellectual storehouse". In considering whether a structure is plant or premises, one must look at the finished product and not at the bits and pieces as they arrive from the factory. The fact that a building or part of a building holds the plant in position does not, convert the building into the plant. A piecemeal approach is not permissible, and the entire matter must be considered as a single unit unless, of course, the component parts can be treated as separate units having different purposes. The functional test was a decisive test.

The bottles are essential tools of the trade for it is through them that the soft drink is passed on from the assessee to the customer. Without these bottles, the soft drink cannot be effectively transported. The bottles and shells also satisfy the durability test as their life is too transitory or negligible to warrant an inference that they have no function to play in the assessee's trade. They are, therefore "plant" for the purposes of the Act." The same was held in the case of M/s UNITED BREWERIES LIMITED Vs JCIT [2023-VIL-1315-ITAT-BLR].

5. Filing of Form 10-IFA vide Rule 21AHA by new manufacturing co-operatives to avail benefit of concessional rate of Income Tax

The Taxation Laws (Amendment) Act, 2019, inter-alia, inserted section 115BAB in the Act which provides that new manufacturing domestic companies set up on or

after 01.10.2019, which commence manufacturing or production by 31.03.2023 and do not avail of any specified incentive or deductions, may opt to pay tax at a concessional rate of 15%. The time for commencing manufacturing or production had been extended to 31.03.2024 by the Finance Act, 2022. However, the same provision had not been provided for new manufacturing co-operative societies. Representations were made for providing a level playing field between new manufacturing co-operative societies and new manufacturing companies by providing for the concessional tax regime of 15% to new manufacturing co-operative societies as well. In view of the same, a new section 115BAE was introduced in which concessional tax regime was provided for the new manufacturing cooperative societies as well. The conditions are materially similar to the conditions applicable to new manufacturing companies, and they are as under:-

i. Rate of tax would be 15% if the total income of the new manufacturing co-operative society is computed,-

a) without any deduction under the provisions of section 10AA or clause (iia) of sub-section (1) of section 32 or section 33AB or section 33ABA or sub-clause (ii) or sub-clause (iia) or sub-clause (iii) of sub-section (1) or sub-section (2AA) of section 35 or section 35AD or section 35CCC or under any of the provisions of Chapter VI-A other than the provisions of section 80JJAA;

b) without set off of any loss carried forward or depreciation from any earlier assessment year, if such loss or depreciation is attributable to any of the deductions referred to in ii(a) above; and

c) by claiming the depreciation, if any, under section 32, other than clause (iia) of sub-section (1) of the said section, determined in such manner as may be prescribed;

ii) the loss and depreciation referred above shall be deemed to have been given full effect to and no further deduction for such loss shall be allowed for any subsequent year.

iii. the concessional rate shall not apply unless the option is exercised by the person in the prescribed manner on or before the due date specified under Section 139(1) for furnishing the first of the returns of income for any previous year relevant to the assessment year commencing on or after 1st day of April, 2024 and such option once exercised shall apply to subsequent assessment years;

iv. the option so exercised cannot be withdrawn;

v. On any income, Not from or incidental to manufacturing or production and in respect of which no specific rate of tax has been provided separately under this Chapter 22% tax shall apply and no deduction or allowance in respect of any expenditure or allowance shall be made;

vi. where owing to the close connection between the assessee and any other person, or for any other reason, the course of business between them is so arranged that the business transacted between them produces to the assessee more than the ordinary profits which might be expected to arise in such business, the profits as may be reasonably deemed to have been derived therefrom and such income shall be charged at the tax rate of30%;

vii. in case the aforesaid arrangement involves a specified domestic transaction referred to in section 92BA, the amount of profits from such transaction shall be determined having regard to arm's length price as defined in clause

viii. of section 92F. The amount, being profits in excess of the amount of the profits determined by the Assessing Officer, shall be deemed to be the income of the assessee. The income-tax payable in respect of the income, in such case shall be computed at the rate of thirty per cent;

ix. short term capital gains derived from transfer of a capital asset on which no depreciation is allowable under the Act shall be computed at the rate of 22%;

x. where the assessee fails to satisfy the specified conditions under the section in any previous year, the option shall become invalid in respect of the assessment year relevant to that previous year and subsequent assessment years and other provisions of the Act shall apply to the assessee as if the option had not been exercised for the assessment year relevant to that previous year and subsequent assessment years.

Further any machinery or plant which was used outside India by any other person shall not be regarded as machinery or plant previously used for any purpose, on fulfilment of certain specified conditions. Where any machinery or plant or any part thereof previously used for any purpose is put to use by the assessee and the total value of such machinery or plant or part thereof does not exceed 20% of the total value of the machinery or plant used by the assessee, then, the concessional rate shall apply on fulfilment of the specified conditions.

It is provided that the assessee shall not be engaged in any business other than the business of manufacture or production of any article or thing and research in relation to, or distribution of, such article or thing manufactured or produced by it.
Further, the business of manufacture or production of any article or thing shall include the business of generation of electricity, but not include certain specified businesses.

A new clause (vb) in the section 92BA was introduced to include the transaction between the Cooperative society and the other person with close connection within the purview of 'specified domestic transaction'.

As per Section 115BAE(5) the eligible co-operative society has to exercise the option to choose new tax scheme in the prescribed manner and now such manner has been prescribed for which a new Rule 21AHA vide Income-tax (Twenty-Third Amendment) Rules, 2023 has been inserted. The new Rule 21AHA provides that a resident co-operative society can exercise the option under section 115BAE(5) by furnishing Form No. 10-IFA. The form shall be furnished electronically either under digital signature or electronic verification code. The Principal Director General of Income-

tax (Systems) or the Director General of Income-tax (Systems) shall specify the procedure for filing Form no. 10-IFA.

The Form is a simple one, wherein the conditions specified in Section 115BAE have to affirmed to be complied with by the assessee.

6. Dispute Resolution Panel cannot remand back cases.. Incase it does and AO Acts on such case, then it is not legal

Section 144C(8) of Income Tax Act provides that The Dispute Resolution Panel may confirm, reduce or enhance the variations proposed in the draft order. However, it shall not set aside any proposed variation or issue any direction Section 144C(5) for further enquiry and passing of the assessment order. Hence, it is clear that Section 144C(8) prohibits DRP to delegate its power to the AO and incase such prohibition is violated, such a transgression is only an irregular exercise of power which can be cured by setting aside such order or action back to the same stage and to the same authority from where the irregularity had crept in. Now, incase a final assessment order is passed by the AO in conformity with these directions on an issue, the same is not legally sustainable and is liable to be quashed as was held in the case of M/s CELIO FUTURE FASHION PVT. LTD Vs ADDL. COMMISSIONER OF INCOME TAX [2023-VIL-1286-ITAT-MUM].

7. Implementation of the global minimum tax Subject to Tax Rule

Pillar Two of the Two-Pillar Solution includes the implementation of a global minimum tax, as well as a new subject to tax rule (STTR). The 15% global minimum tax is now a reality in all 27 European Union (EU) member states and extends to countries beyond the EU such as the United Kingdom, Switzerland, Japan, Korea and Singapore. Many multinational organizations will be confronted with Pillar Two global minimum tax rules starting in January 2024. On Oct. 3, 2023, the Organization for Economic Cooperation and Development (OECD) published the Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to Tax Rule (STTR MLI) as part of the concluded negotiations in September 2023 between the OECD/G20 Inclusive Framework.

The Subject to Tax Rule (STTR) will enable developing countries to tax certain intragroup payments, in instances where these payments are subject to a nominal corporate income tax rate below 9%. The STTR allows source jurisdictions – those in which covered income arises – to impose a tax where they otherwise would be unable to do so under the provisions of tax treaties. The OECD/G20 Inclusive Framework on BEPS has concluded negotiations on a multilateral instrument that will protect the right of developing countries to ensure multinational enterprises pay a minimum level of tax on a broad range of cross-border intra-group payments, including for services.

Developed over the past 12 months through negotiations between governments supporting the OECD, including OECD members and G20 countries, the Multilateral Convention to Facilitate the Implementation of the Pillar Two Subject to Tax Rule is a major step in concluding Pillar Two of the OECD's proposed reforms, which would introduce a 15% tax minimum for multinationals.

The Global Anti-Base Erosion Model Rules (GloBE) and the STTR are key components of Pillar Two and ensures multinational enterprises pay a minimum level of tax on the income arising in each of the jurisdictions in which they operate. More specifically, the STTR is a treaty-based rule that has the potential to protect the right of developing countries to tax certain intragroup payments where these are subject to a nominal corporate income tax that is below the minimum rate.

8. Where the assessee has not earned any exempt income, no disallowance is required to be made u/s 14A of the Act

It is settled in many cases including the decision in the case of Cheminvest Ltd. vs CIT reported in [2015] 378 ITR 33 (Delhi) and CIT Vs. Ashika Global Securities Ltd. in ITAT 100 of 2014 GA _2122 of 2014 that if the assessee has not earned any exempt income, no disallowance is required to be made u/s 14A of the Act. The same was duly followed and held accordingly in the case of ACIT, CIRCLE-1(1) Vs M/s GOLD RUSH SALES AND SERVICE LIMITED [2023-VIL-1284-ITAT-KOL], where the AO during the course of assessment proceedings observed that the assessee was holding investments which were capable of generating exempt income. The AO

noted that the assessee has claimed expenses of interest payment in the profit and loss account and since the assessee has not maintained separate books of accounts for expenses incurred in relation to income not forming part of the total income and therefore, the same cannot be ascertained from the books of accounts of the assessee, Section 14A of the Act read with Rule 8D of the Rules was invoked disallowance of interest under Rule 8D(2) of the Income Tax Rules was made.

9. Thousand culprits can escape, but, one innocent person should not be punished... One last opportunity should be granted

Negligence means a breach of duty (duty to take care). It is an act of carelessness and ignorance to perform a function which a rational and prudent man would perform. Breach of duty to take care and measures in order to avoid any kind of performance of an act is the basic requirement in order to raise liability of negligence. However, justice requires that the negligent be also provided a last opportunity as no innocent should be punished. This principle was followed in the case of BHIWADI INTEGRATED DEVELOPMENT AUTHORITY Vs INCOME TAX OFFICER [2023-VIL-1289-ITAT-JAI]. The Bench observed that the assessee was really lethargic and unserious in pursuing his case in spite of providing various opportunities by the ld. CIT(A) and ld.AO. The assessee did not appear or filed any reply to the notices which were issued by the ld. AO during the assessment proceedings, finally the AO completed ex-parte assessment u/s 144 of the Income Tax Act. Further, the assessee or his legal representative did not appear even at appellate proceedings in spite of several notices. However, the Bench still held that since the assessee because of any reasons could not advance his arguments/submissions to contest the case before the lower authorities and the ld. AR for the assessee also prayed to give one more opportunity to submit the evidences concerning the issue in question, with grounds so raised by the assessee, to decide it afresh by providing one more opportunity of hearing. However, the assessee was directed to not seek any adjournment on frivolous ground and remain cooperative during the course of proceedings before the ld. AO.

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