SNR & COMPANY
CHARTERED ACCOUNTANTS

# INCOME TAX BULLETIN

MAY 2023

**Email:** snr@snr.company | **Website:** www.snr.company

# CONTENT

## - Judicial Updates



## - Circulars/Notifications



## - Compliance Calendar

# JUDICIAL UPDATES

## 1. Foreign Bank's ECB-interest not business profit

**Case of :** DCIT Vs Cooperative Rabobank UA
**Decision by :** ITAT, Mumbai
**In favour of :** Assessee

- Assessee, a branch office of Rabobank, Netherlands, filed a return of income for AY 2012-13 declaring a total income of Rs.24.03 Cr including interest income earned from ECB.

- During the course of the assessment, the Revenue observed that Assessee had an undisclosed TDS credit amounting to Rs.6.96 Cr. Assessee explained that out of the total tax, the credit of Rs.11.47 Cr reflected in Form 26AS, only a tax credit of Rs.4.96 Cr was claimed in the return for the current AY, and the remaining unclaimed tax credit of Rs.6.50 Cr, the assessee explained that has various branches around the world which operate independently and that these branches have separate businesses; hence conducting, inter alia, lending, and other business activities. Hence it was practically difficult for the assessee to comprehensively collate the details of income earned in India from the transactions undertaken by various personnel of these branches.

- Further Assessee submitted that tax was deducted as per Article 11 of India-Netherlands DTAA and contended that if the differential income is to be brought to tax, it must be taxed at the rates prescribed in DTAA and grant corresponding TDS credit.

- Rejecting Assessee's submissions, Revenue brought to tax the difference of undisclosed gross receipts as per Form 26AS and accordingly, made an addition of Rs.63.27 Cr representing interest income from ECB, as business receipts taxable at the rate of 40% as applicable to a foreign company instead of applying the tax provided in Article 11 of DTAA.

- CIT(A) relied on Assessee's own case for AY 2010-11 wherein it was held that as per provisions of Section 115A(i)(a)(ii), interest income earned by the Assessee would be chargeable to tax at 20% and directed the Revenue to apply rate prescribed in India-Netherlands DTAA, being more beneficial and deleted the additions.

- ITAT noted that there is no dispute that the Assessee has a PE in India and the taxability of interest income in the hands of the Assessee is also not disputed. It rejected Revenue's contention that interest income would become the business profit of the Assessee (Indian Branch) under Article 7 of DTAA since there is a separate provision i.e. Article 11 for taxability of interest.

- The tribunal opined that since there is no dispute to the fact that the nature of income that is sought to be taxed is interest income in the instant case, it would be just and fair to apply Article 11(2) for the purpose of determining the taxability of the said interest income.

**Full Judgement : Cooperative Rabobank UA**

***SNR's Take***

The tribunal has rightly held that since there is a specific clause in the treaty that covers interest income, therefore it cannot be overlooked by the tax authorities to apply the business profits clause.

## 2. DEPB/Duty Drawback not eligible for deduction u/s Sec.80-IB:

**Case of :** Saraf Exports
**Decision by :** Supreme Court
**In favour of :** Revenue

- For AY 2008-09, Assessee-Firm, engaged in the business of manufacturing and exporting wooden handicraft items, filed Nil return of income claiming deduction for DEPB and receipts under the duty drawback under Section 80-IB, however, the same was disallowed during assessment proceedings.
- While CIT(A) upheld the disallowance, ITAT allowed the deductions as claimed on the receipts of amount under DEPB Scheme and Duty Drawback Scheme. The HC relied on SC ruling in the case of *'Liberty India'* and *'Sterling Foods'* and overruled the ITAT ruling and restored the additions.
- The Apex Court considered the provisions of Section 28 and Section 80-IB and observed that owing to disputes on the taxability of cash incentives from the Government i.e. whether it is a capital receipt or revenue receipt, the legislature by way of inserting clauses (iiia), (iiib), (iiic), (iiid) and (iiie) to Section 28 has made the said incentives taxable under the head of "profits and gains of business and profession", likewise, for claiming deduction under Section 80-IB it must be on the "profits and gains derived from industrial undertakings" mentioned in Section 80-IB.

- It observed that coordinate bench in 'Liberty India' after taking into consideration the DEPB and Duty Drawback Schemes, observed that:

  these are incentives which flows from the schemes framed by the Central Government or from Section 75 of the Customs Act, 1962 and, hence, are not profits derived from the eligible business under Section 80-IB and are in the nature of ancillary profits, and

  duty drawback, DEPB benefits, rebates, etc. cannot be credited against the cost of manufacture of goods debited in the profit and loss account for purposes of Sections 80-IA/80-IB as such remissions (credits) would constitute an independent source of income beyond the first degree nexus between profits and the industrial undertaking.

- Thus, the court opined that *"following the law laid down by this Court in the case of Sterling Foods, Mangalore (supra) and Liberty India (supra) as such, no error has been committed by the High Court in holding that on the profit from DEPB and DutyDrawback claims, the Assessee shall not be entitled to the deductions under Section 80-IB."*

**Full Judgement: Saraf Exports**

### *SNR's Take*

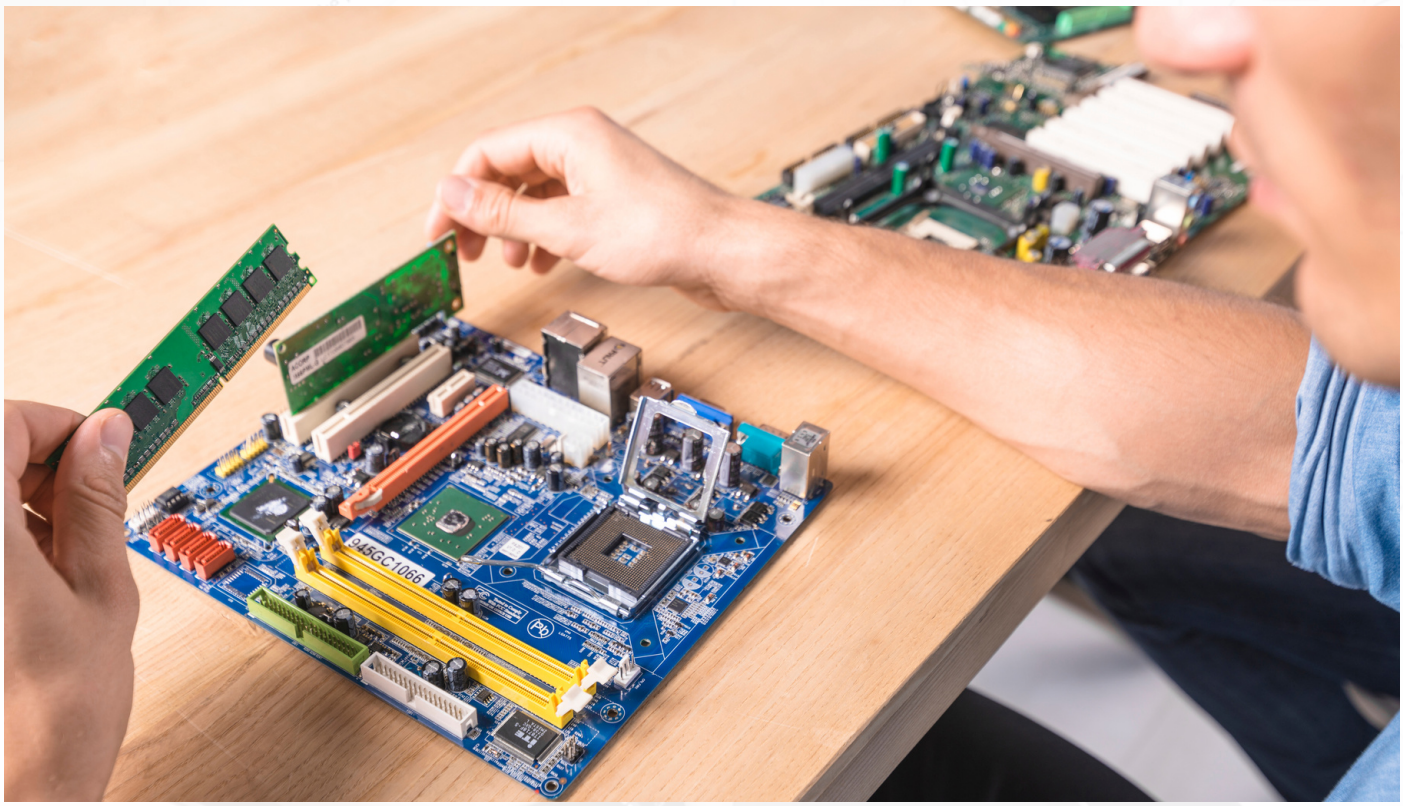
The Apex Court has further removed the ambiguities and has given a clear distinction between the judgements in the case of Liberty India and Meghalaya Steels Limited stating that in Meghalaya Steels it was case of three subsidies: a) Transport Subsidy, b) Interest Subsidy, and c) Power Subsidy, which directly affect the cost of manufacturing and have a direct nexus with the profits and gains of the undertaking & hence eligible for deduction.

## 3. Re-export of imported articles 'services' under SEZ Act, eligible for Sec.10AA deduction

**Case of :** PCIT Vs Om Nanotech Pvt Ltd
**Decision by :** High Court, Delhi
**In favour of :** Assessee

- Assessee-Company, set up a trading unit involving import of memory modules, flash drivesand electronic chips which ultimately were re-exported. For AY 2010-11, Revenue disallowed Section 10AA deduction on the basis that the deduction could be claimed only against articles manufactured in, or against the services which emanated from SEZ. However, CIT(A) deleted the disallowance which was sustained by ITAT.

- Before HC, Revenue submitted that ITAT erred in referring to the Explanation given under Rule 76 of SEZ Rules after taking recourse to the definition of the expression "services" contained in Section 2(z) of the SEZ Act. On the other hand, the Assessee contended that: (i) since the expression "services" was not defined in the Income Tax Act, the ITAT was well within its powers to advert to the definition contained in Section 2(z) of the SEZ Act and (ii) the entire purpose and object of providing deduction qua profits derived from trading activities was to promote exports and earn revenue in foreign currency.



- HC noted that undisputedly, the definition of the expression "services" is not provided in the Income Tax Act. Thus, from the definition of "services" under Section 2(z), HC observed that tradable services, which are prescribed by the Central Government for the purposes of SEZ Act, are included in the definition. It further noted that as per the Explanation to Rule 76, trading for the purposes of the Second Schedule of the SEZ Act includes import for the purposes of re-export, thus remarked that the SEZ Act and Rule 76 *"point in the direction that the expression "services" means services which are offered by way of re-export of articles that are imported into the country"*.

- The court further referred to the Notification No. 4 dt. May 24, 2006, by the Ministry of Commerce and Industry providing that no income tax benefits will be availed by the unit for trading, except for trading in the nature of re-export of imported goods which was adopted by Export Promotion Council (EPC) by its Circular No. 17 dt. May 29, 2006.

- Based on the above noting, the court held that *"having regard to the aforesaid intrinsic evidence available both in 2005 Act and Rules, we have no doubt that it was always intended that the deduction under Section 10AA of the 1961 Act will also be available qua those articles which, upon import to the unit located in SEZ, were thereafter re-exported."*; Thus, decided the question of law in favor of the Assessee.

**Full Judgement: Om Nanotech Pvt. Ltd.**

### *SNR's Take*

The court has rightly taken a broad view of the term 'services'. In the absence of definition under Income Tax Act, reliance on definitions in SEZ Act is unavoidable. Further, court's ruling is substantiated by the notification by commerce ministry stating that tax benefits can be availed only in case of such trading goods where re-export is involved.

## 4. Existence of PE 'no prerequisite' under Sec.44BB for taxability of charter-hire receipts:

**Case of :** Pacific Crest Pte. Ltd Vs DCIT
**Decision by :** ITAT, Delhi
**In favour of :** Assessee

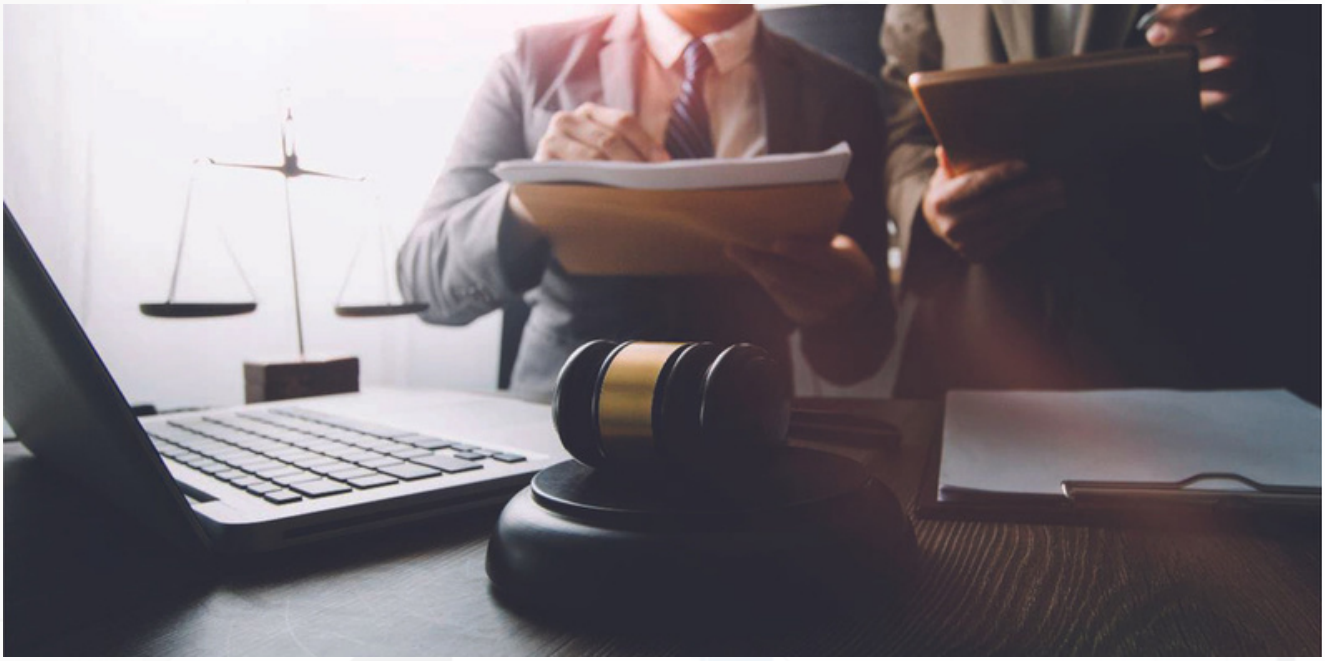
- Assessee, a Singapore based company with no PE in India, received amounts towards hiring of vessels for seismic support duties and transportation of coated pipes in India. Although tax under Section 195 was withheld, Assessee did not file return of income, thus holding that income chargeable to tax has escaped assessment, reassessment proceedings were initiated under Section 147.

- AO completed the assessment on best judgement and treated the receipts of Rs.23.85 Cr as royalty under Section 9(1)(vi) and taxed the same at 10% under Section 115A. DRP dismissed Assessee's objection that the receipts pertain to hiring of vehicles for extraction of mineral oils, thus taxable under Section 44BB and held that the said section applies only in case where the non-resident has PE in India and since Assessee did not have PE, Section 44BB would not be applicable and held that the said receipts were in the nature of royalty in terms of Explanation 2(vi) to Section 9(1)(vi).

- ITAT observed that as per the charter hire agreement, the vessels were given on hire for seismic support duties in India and vessels are operated by Assessee's personnel, notes that requirements of vessels for drilling, testing, and completing were also defined in the charter hire agreement.

- Referring to definition of royalty under Explanation 2(iva), ITAT opined that DRP overlooked the second limb of the clause which carves out an exception by providing that the amounts referred to in Section 44BB cannot be treated as royalty, remarked that *"once the receipts are covered under section 44BB of the Act, automatically, they are excluded from the definition of royalty as provided under Explanation 2(via) to section 9(1)(vi) of the Act."*

- The Tribunal stated that since the receipts of Rs.23.85 Cr pertain to hiring of vessels for use in prospecting or exploration or production activities, covered under Section 44BB, it cannot be treated as royalty under Section 9(1)(vi).



**Full Judgement: Pacific Crest Pte. Ltd**

### *SNR's Take*

The Tribunal has rightly relied on the judgements of **Western Geco** wherein it was held that the seismic data services and mining projects are inextricably linked to activities covered under Section 44BB. Further, the judgement is supported by the Bombay HC ruling in Larsen & Toubro and Mumbai ITAT ruling in Valentine Maritime (Gulf).

## 5. Reimbursement of seconded employees' salary is not FIS:

**Case of:** : Morgan Stanley International Incorporated Vs DDIT (IT)
**Decision by:** ITAT, Mumbai
**In favour of :** Assessee

- Assessee, a US-based Company and 100% subsidiary of Morgan Stanley USA, is engaged in provision of support services to its subsidiaries worldwide including India. Assessee entered into an agreement with Morgan Stanley India to provide support services for the consideration of Rs.4.26 Cr, which was offered to tax as FTS and also received Rs.14.74 Cr from Morgan Stanley Advantage Services Pvt. Ltd. (MSASPL) and Rs.2.5 Cr from MSIM global support and technology services Pvt. Ltd. (MGSTSPL) as reimbursement for secondment of its employees. Revenue held that the reimbursement of salary by the subsidiaries were taxable as FTS, which was upheld by CIT(A)

- ITAT took note of the terms of secondment in the form of deputation:

  Expatriate employees would be working under the supervision and control of the Indian AE,

  Day to day responsibility of such employees would be managed by the Indian AE's, the employees would be accountable only to the Indian AE's and shall abide by Indian AE's employee's policies, guidelines, and other directions,

  The Assessee will only be responsible for the general review of the role, discipline, promotion, etc. of the expatriate employees,

  The Assessee was required to pay the salaries of the said employees and the same was to be reimbursed to it by the Indian AE's on an actual basis without any mark-up

- The tribunal observed that the transaction between the Assessee and it's Indian AE's are simply in the nature of reimbursement of salary cost on an actual basis without any mark- up, thus the same does not fall under the category of FTS/FIS, under Article 12(4) of India-USA DTAA and under Section 9(1)(vii). The tribunal stated that since the transaction does not fall under FTS under Section 9(1)(vii) or Article 12 of DTAA, it cannot be referred to TPO for benchmarking while noting that a similar transaction was referred to TPO for earlier AY 2005-06, which was accepted in favor of the Assessee on the ground that the said transaction does not need benchmarking

- The tribunal further noted that the Revenue accepted the same transactions for AYs 2004-05, 2005-06 and 2006-07, thus, states that there is no reason for the Revenue to take a different view this year, without anything on record for not following the principle of consistency applicable both to the Assessee and the Revenue.

- The tribunal relied on the coordinate bench ruling in Assessee's own case deciding the issue in Assessee's favor, also observed that taxes on the salary of the seconded employees are already paid to the Indian exchequer, and if the same is taxed again in the Assessee's hands, it would be tantamount to double tax. Accordingly, the tribunal directed the Revenue to delete the addition.

**Full Judgement: Morgan Stanley International Incorporated**

### *SNR's Take*

In this case, the assessee was required to reimburse salaries in respect of seconded employees to its overseas parent company on an actual basis. This judgment shall provide a major relief to various taxpayers involved in similar transactions.

## 6. Mushrooms grown under controlled conditions constitute 'agricultural activity', and hence, exempt from tax

**Case of :** DCIT Vs British Agro Products (India) Pvt. Ltd.
**Decision by :** ITAT, Chennai
**In favour of :** Assessee

- Assessee filed a return of income for AY 2017-18 and treated income from cultivation or sale of white button mushrooms as 'agricultural income' to claim an exemption under Section 10. Revenue treated the said income as income from business or profession on the premise that Assessee's activities were in nature of the production of white button mushrooms in a temperature-controlled facility wherein various plants and machinery were installed and cannot be construed as 'agricultural activity'.

- CIT(A) allowed Assessee's appeal and held that the term 'agriculture' does not confine to the production of grains but also expounds on all products culminated from land and which are either used for consumption or trade/commerce, accordingly, cultivation of white mushroom is in nature of 'agricultural activity'.

- Before ITAT, Assessee contended that growing white button mushroom is an 'agricultural activity' and the income derived from the said activity is 'agricultural income which is exempt from tax. It referred to various documents and letters issued by the Ministry of Agricultural wherein mushroom cultivation was treated as an 'agricultural activity'.

- Revenue contended that Assessee's activity involves growing white mutton mushrooms in a tray that was kept in a temperature-controlled room. It contended that no essential activity to conduct 'agricultural activity' such as tilling of the soil, sowing of seeds, planting, etc. was carried out during the whole process.

- The tribunal observed that on perusal of Assessee's activities, it is evident that Assessee is carrying out basic operations on land by digging out clay soil to mix it with paddy straw (seeds) and load it in big trays placed vertically to culture it from the matured mushroom. Further, the assessee also carried out subsequent operations like the wedding of oil, usage of bactericide, plucking, harvesting, etc. which constitutes 'agricultural activity' and the income derived therefrom is an 'agricultural income which is exempt from tax.

- The tribunal rejected the revenue's contention and observed that Assessee carried out basic and subsequent operations involved in agricultural operations for the cultivation of grains, vegetables, and fruits and even if such activity is carried out in the greenhouse and temperature-controlled facility, the said activity can only be construed as 'agricultural activity' and not 'commercial activity'.

**Full Judgement: British Agro**

### *SNR's Take*

The Tribunal's ruling is in consonance with the SC ruling in Raja Benoy Kumar wherein it was held that in order to consider any activity as 'agricultural activity' there should be some basic and subsequent operations in the land for the purpose of raising grains or vegetables or fruits including plantation or groves.

# CIRCULARS/NOTIFICATIONS:

## 1. CBDT notifies Cost Inflation Index for FY 2023-24:

The CBDT has notified the cost inflation index (CII) number for the current financial year, 2023- 24. According to the notification dated April 10, 2023, the CII number for the current fiscal year is 348.

**Read Notification:** 21/2023

## 2. CBDT Notifies National Institute of Design for tax deduction u/s 35(1)(ii):

TCBDT approved National Institute of Design, Ahmedabad under the category of 'University, College or other institution' for Scientific Research for the purposes of clause (ii) of sub-section (1) of section 35 of the Income-tax Act, 1961 read with rules 5C and 5E of the Income-tax Rules, 1962.

A donor is entitled to claim a deduction equal to the amount of contribution to a university, college or other institution approved under section 35(1)(ii) for carrying out scientific research activities. The deduction is allowed where the taxpayer does not carry on the research himself but contributes to outsiders for carrying out research.

**Read Circular:** 23/2022

# COMPLIANCE CALENDER:

| DATE | PARTICULARS |
|---|---|
| **07-05-2023** | The due date for deposit of Tax deducted/collected for the month of April 2023. However, all sum deducted/collected by an office of the government shall be paid to the credit of the Central Government on the same day where tax is paid without production of an Income-tax Challan" |
| **15-05-2023** | "Due date for issue of TDS Certificate for tax deducted under section 194-IA, 194-IB, 194M, and 194S in the month of March 2023". |
| **15-05-2023** | Quarterly statement of TCS deposited for the quarter ending March 31, 2023 |
| **30-05-2023** | Submission of a statement (in Form No. 49C) by a non-resident having a the liaison office in India for the financial year 2022-23 |
| **30-05-2023** | Due date for furnishing of challan-cum-statement in respect of tax deducted under section 194-IA, section 194-IB, section 194M and section 194-S in the month of April 2023. |
| **30-05-2023** | Issue of TCS certificates for the 4th Quarter of the Financial Year 2022- 23 |
| **31-05-2023** | Quarterly statement of TDS deposited for the quarter ending March 31, 2023 |
| **31-05-2023** | The due date for furnishing of statement of financial transaction (in Form No. 61A) as required to be furnished under sub-section (1) of section 285BA of the Act with respect to the financial year 2022-23. |
| **31-05-2023** | Application in Form 9A for exercising the option available under Explanation to section 11(1) to apply the income of the previous year in the next year or in the future (if the assessee is required to submit a return of income on or before July 31, 2023). |
| **31-05-2023** | Statement in Form no. 10 to be furnished to accumulate income for future application under section 10(21) or section 11(1) (if the assessee is required to submit a return of income on or before July 31, 2023) |

SNR & COMPANY
CHARTERED ACCOUNTANTS

SNR is a firm of Chartered Accountants offering assurance, tax, accounting and consulting services to its national and international clients across the globe. The firm has its head office at New Delhi with branches at. Pune & Bengaluru. SNR has experienced a considerable growth since its inception in 1996 and is empanelled with reputed banks and with the office of the comptroller and auditor general of India The firm through its team of experts consisting of Chartered Accountants, Company Secretaries and Management professionals provides professional services to a large number of clients viz. Companies, Banks and NGOs etc.

# OUR LOCATION


**DELHI**

A-15, Second Floor, Hauz Khas,
New Delhi- 110016
Tel: +91-11 41655801, 41655802

**PUNE**

Office No. 5,Kalashree Apartment,
Opposite Bank of Maharashtra,
Karve Road, Pune 411004
Ph: +91 20 25435788

**BANGALORE**

No. 5A, Second Floor, 6th Main,
KHB Colony, Basaveshwaranagar,
Bangalore - 560079
Tel: +91 80 42064178


## Disclaimer: