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Tax Digest

- Recent case laws

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NEWS FEED

- ***Circular No. 8/2022 T***

Extension of time line for electronic filing of Form NO.10AB for seeking registration or approval under Section 10(23C), 12A or 80G of the Income-tax Act,1961 (the Act): ***30th Sep 2022***

Direct Tax Updates

1. Section-68 "Cash Credits."

No additions under Section 68 on account of cash deposited post demonetization if same represented sale proceeds.

In the instant case[1], the assessee-individual deals in beedi, tea powder and pan masala. In the course of assessment, AO noticed that there were several cash deposits in two of the bank accounts of the assessee. Some of the deposits were made of bank notes that were declared as not legal tender owing to demonetization of currency.

The AO held that, as per the cash book the closing balance as on 08.11.2016 was Rs. 4.90 lakh. After reducing Rs. 4.90 lakh from total deposit of Rs. 14.50 lakh, the balance is Rs. 9.60 lakh. Out of Rs. 9.60 lakh, the old Specified Bank Notes are totaling to Rs. 4.50 lakh which stands unexplained. Hence, the same was treated as unexplained cash credits under Section 68 in the books of account of the assessee and the same is required to be brought to tax. Accordingly, a sum of Rs. 4.50 lakh is brought to tax under Section 68.

Aggrieved by the AO's order assessee preferred an appeal before Ld. CIT(A), and submitted that the cash deposits in question were the cash collections from the small and medium class traders out of the business of the assessee. Old demonetized notes could be accepted till 30.12.2016 and a payee can continue to accept old demonetized notes of Rs. 500 or 1000 since those notes can be accepted as valid tender and there was no prohibition or lawful direction not to pay or accept old notes. The Assessee relied on the decision of *ACIT v. Dewas Soya Ltd. (ITAT, Indore) (2012)*, wherein on identical facts of the case it was held that the claim of the assessee that such addition resulted into double taxation of the same income in the same year because on one hand cost of the sales has been taxed (after deducting gross profit from same price ultimately credited to profit & loss account) and on the other hand amounts received from above parties has also been added under Section 68.
The CIT(A) did not accept the contention of the assessee and held that, once the Rs. 500 and Rs. 1,000 notes are declared as not valid legal tender on 09.11.2016, the assessee cannot accept cash payments after 09.11.2016 that are demonetized and doing so was patently illegal.

The assessee preferred further appeal before the Hon'ble Tribunal wherein it was observed and held that the sale proceeds for which cash was received from the customers was already admitted as income and if the cash deposits are added under Section 68 that will amount to double taxation once as sales and again as unexplained cash credit which is against the principles of taxation. Thus when cash receipts represent the sales which the assessee has offered for taxation, and when the trading account showed sufficient stock to effect the sales, and when no defects are pointed out in the books of account, and when Assessee already admitted the sales as revenue receipt, there is no case for making the addition under Section 68 again. The additions made were deleted.

2. Section-28 "Profit and gains of business or profession":

Remuneration/interest can't be taxed in hands of partners relying upon deed if same wasn't claimed by firm

In the instant case[2], the assessee – partner in a firm, AO reopened assessment on ground that she failed to show remuneration and interest on capital received from partnership firm in return of income filed, to which assessee filed objections pointing out that she had not received any income in form of remuneration and interest on capital from

[1] **Anantpur Kalpana Vs. ITO (ITAT, Bangalore) [2022]**

[2] **Mamta Bhavesh Deva Vs. ITO (High Court of Gujarat) [2022]**

partnership firm and, therefore, there was no question of adding such income or showing such income in return of income. AO disposed the objections raised by assessee on ground that assessee had received share of profit from firm and such share received by assessee as per partnership deed would include remuneration and interest on capital which had not been debited from profit and loss account of firm.

Assessee went for an appeal, the Ld. CIT(A) directed the AO to tax the amount of remuneration/interest on the partners' capital account in the hands of the partners instead of addition made in the hands of firm.

Assessee went for a further appeal before Hon'ble Tribunal, where it held that - It is an undisputed fact that the deed of partnership requires a partner to claim the deduction for the remuneration and the interest on capital. The dispute arises whether the clause mentioned in the deed of partnership is compulsory/mandatory on the part of the assessee. It is not possible to carry on a business without a written deed in the current module. Clauses mentioned in the partnership deed are not mandatory but made to avoid any ambiguity and misunderstanding. As such, there is no dispute among the partners for not claiming the remuneration/interest of on capital in the profit and loss account of the firm. Partners of the firm suggest that it was agreed not to claim any remuneration/interest on the capital account.
Tribunal set aside the CIT(A) view to tax the amount of remuneration/interest on the partners' capital account in the hands of the partners.

Assessee filed a writ petition to Hon'ble High Court, and it upheld the order passed by the Tribunal and held that nothing survives in the present matter so far as the reopening of the assessment of the partner of the partnership firm is concerned. The notice under consideration was quashed and set aside.

3. Section-145A "Method of accounting in certain cases":

No revision under Section 263 on issue which was raised by AO during assessment to which assessee had offered explanation.

In the instant case[3], the assessing officer (AO) completed assessment under Section 143(3) after raising specific queries with regard to valuation of closing stock of tools and tackles to which assessee offered complete explanations which were accepted by AO.

The Ld. CIT set aside the order passed by AO taking a view that the order passed was erroneous as the assessee did not follow the provision of Section 145A relating to the Method of Accounting in certain cases where the valuation of purchase and sale of goods and adjustments of tax duty and cess is dealt which does not provide for depreciation as claimed by the assessee.

Assessee went for an appeal before the Hon'ble Tribunal, were it held that whether the CIT was justified in invoking his power under Section 263 to set aside the order of assessment passed by the Assessing Officer under section 143(3).
Tribunal held that, it is a settled legal position that to invoke the power under section 263 of the Act, it is not sufficient that the order should be shown to be erroneous alone but it should be shown to be erroneous and prejudicial to the interest of the revenue. In other words, the power under section 263 is not a power to review the order passed by the AO, and merely because the CIT is of different view, such power cannot be invoked. It further held that, on going through the facts of the case found that a specific query was raised by the AO to the assessee with regard to the valuation of closing stock of tools and tackles and the assessee had offered an explanation which found favour with the AO and

[3] **PCIT Vs. Bridge & Roof Co. (India) Ltd (High Court of Calcutta) [2022]**

assessment was completed. This factual position was put to the revenue during the course of argument before the Tribunal and the revenue was not able to controvert or revert this factual position which was manifestly clear from the records. Tribunal allowed assessee's appeal and set aside the order passed by CIT.

Aggrieved by the Tribunal order, the Revenue went for an appeal to Hon'ble High Court. It upheld the order passed by the Tribunal and dismissed the appeal.

4. Section-56 "Income from Other Sources" and Section 37: "General"

Rental income earned even after completion of rehabilitation which was approved by BIFR would be treated as Income from other sources. Quality loss to be allowed only to the assessee carrying out manufacturing activities.

In the instant case[4], the assessee is a tyre manufacturing company. Over the years, the company incurred business losses, and the company's entire net worth eroded. Assessee was declared as a sick company under the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA). Thereafter, a scheme for rehabilitation and revival was prepared, which obtained the approval of the Board for Industrial and Financial Reconstruction (BIFR). The scheme provided for an arrangement between M/s.Apollo Tyres Ltd. (ATL) and the assessee. The approved scheme contemplated ATL to operate the plant and machinery of the assessee under a lease deed for eight years, i.e. 1-4-1995 till 31-3-2003, on a total rent of Rs. 45.5 crores for the entire period. As per the scheme, the entire production was taken over by ATL and the expenses incurred by the assessee, including the labour charges for operating the plant were reimbursed by ATL.

By the AY 2001-02, the assessee's net worth had turned positive. Thus, at the end of the eight years sanctioned by BIFR, the assessee could have revived and resumed its operations by itself. Instead, assessee chose to continue the lease arrangement by renewing the lease with ATL for one more year from 1-4-2003 to 31-3-2004. This arrangement was continued in the coming years too.

AO held that for AY 2004-05, the rental income received by the assessee from ATL could not be treated as income from business but is to be assessed as income from other sources, as the assessee had not carried out any manufacturing activity. It also disallowed the claim towards quality loss, stating that the assessee had no role in the manufacture of tyres or its sale and that if any quality loss had occurred, the same was the responsibility of ATL and not that of the assessee.

Aggrieved by the AO's order, assessee preferred an appeal before the Ld. CIT(A) which held that the lease rent received is to be treated as business income and rejected the claim of quality loss after finding that the loss was attributable to ATL and not to the assessee.

Aggrieved by the Ld. CIT(A) order both assessee and revenue went for further appeal before the Hon'ble Tribunal which after going through records held that the rental income has to be assessed under the head "income from other sources" since the assessee had no intention to revive its business activity and there was no attempt to exploit the commercial assets of the company and instead the assessee merely renewed rental arrangement and

[4] **PTL Enterprise Ltd Vs. DCIT (Supreme Court of India) [2022]**

received rent as a passive receipt. Regarding the quality loss, it upheld the decision of AO and CIT(A).

Assessee went for a further appeal to the Hon'ble High Court which upheld the decision taken by the Tribunal.

Assessee filed a Special Leave Petition (SLP) in Hon'ble Supreme Court of India against the Hon'ble High Court order, which was dismissed by the apex court and it upheld the decision taken by ITAT and High Court.