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CHARTERED ACCOUNTANTS

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DIRECT TAX REVIEW
OCTOBER 2020

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HIGH COURT RULINGS

Third Party Administrator is required to deduct TDS on payments made to hospitals u/s 194J of the Income Tax Act, 1961

Facts

The assessee is a company engaged in the business of providing Third Party Administration (TPA) services on medical/health insurance policies issued by the insurance companies. The services provided by the assessee includes enabling the policy holders, the patients to obtain medical treatment from the hospital without making upfront payments to the hospitals by direct settlement i.e., cashless scheme and reimbursement of claims of policy holders in accordance with the terms of the insurance policy. The assessee makes payment to the hospitals under the cashless scheme in fulfillment of contractual obligations between the insurance companies and the policy holders on one hand and the insurance companies and the assessee on the other hand. The assessee's obligation to make payment to the hospitals is as an agent to the insurance companies and not in consideration for any professional services rendered by the hospital to the assessee.

The DCIT (TDS) conducted a survey of the premises of the assessee and recorded the statement of assessee's CEO u/s 133A of the Act.

Thereafter, a SCN was issued and DCIT (TDS) passed orders u/s 201(1) and 201(1A) of the Act for FYs 2003-04 to 2008-09 and held that the payments made by the assessee to the hospitals constituted fees for professional services liable for TDS u/s 194J of the Act. The assessee thereupon filed an appeal before CIT(Appeals) who further held that the TPA's are liable to deduct tax from the payments made to the hospital u/s 194-J of the Act and upheld the addition made by the AO.

The appeal was further filed by the assessee before the Tribunal, who vide the impugned order held that assessee was required to deduct TDS u/s 194J of the Act on payments made by it to the hospitals. The appeal was filed before the Hon'ble High court.

Ruling

The Hon'ble Karnataka High Court held that TPA services are incidental or ancillary services, which are connected with carrying on Medical Profession are included in the term Professional Services for the purpose of Section194J. The words "in the course of carrying on" are used with the intention to include incidental, ancillary, adjunct or allied services connected with or relatable to medical services. Thus, the sweep and scope of Explanation (a) to Section 194J is not restricted only to payments made to medical or other professionals but services rendered in the course of carrying on the stipulated profession. It is pertinent to note that payments are made to the hospitals and not personally by the payer to the individual doctors or professionals. The medical services are rendered in the course of carrying on the medical profession.

Therefore, the payments in the hands of the recipient, is determinative of deductibility of tax at source, however, the payments in the hands of hospital cannot be treated to be business income as the payments are received in the course of carrying on the

medical profession. Hence, payments made by TPAs to the hospitals fall under the purview of section 194J and shall be liable for deduction of tax at source. Accordingly, the appeal of the assessee was disposed of.

Source: HC, Karnataka in TTK Healthcare TPA Pvt Ltd vs. DCIT (TDS), Bangalore; ITA No. 303 of 2013, dated Oct 12, 2020

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Disallowance of expenditure incurred to earn exempted income u/s 14A of the Income Tax Act cannot exceed such exempt income

Facts

The assessee earned "dividend income" from the investments made by it, which is exempt from income tax for the AY 2011-12 but the ld. Assessing Authority vide order disallowed the expenditure which is ex facie illegal and impermissible. He also submits that the expenditure incurred to earn the exempted income in the form of Dividend was really not incurred by the Bank during the year but the said computation of expenses was made as per the direction of Assessing Authority in terms of Rule 8D of the Rules with a clear submission made by the assessee that no expenditure deserves to be disallowed in the hands of assessee u/s 14A of the Act r/w Rule 8D of the Rules but ignoring such factual submissions as well as the provisions of law, the assessing authority disallowed the sum and the Appellate Authorities also casually upheld the said findings. The Revenue urged before the Court that though the disallowance in excess of the dividend income earned by the assessee may not be justified, but the assessee himself has computed the figures in terms of Rule 8D and had supplied the same to the assessing authority and therefore the assessing authority was justified in disallowing the same.

Ruling

The Hon'ble Madras High Court held that the disallowance of expenditure incurred to earn exempted income cannot exceed the exempted income itself and neither the Assessee nor the Revenue are entitled to take a deviated view of the matter. The negative figure of disallowance cannot amount to hypothetical taxable income in the hands of the assessee. The disallowance of expenditure incurred to earn exempted income has to be a smaller part of such income and should have a reasonable proportion to the exempted income earned by the assessee in that year, which can be computed as per Rule 8D only after recording the satisfaction by the Assessing Authority that the apportionment of such disallowable expenditure u/s 14A made by the assessee or his claim that no expenditure was incurred is validly rejected by the Assessing Authority by recording reasonable and cogent reasons conveyed to assessee and after giving opportunity of hearing to the assessee in this regard.

Accordingly, the appeal was disposed of by answering the question of law in favor of the assessee and against the Revenue and by holding that the disallowance under Rule 8D of the IT Rules r/w section 14A of the Act can never exceed the exempted income earned by the assessee during the particular AY and further, without recording the satisfaction by the Assessing Authority that the apportionment of such disallowable expenditure made by the assessee with respect to the exempted income is not acceptable for reasons to be assigned the

Assessing Authority, he cannot resort to the computation method under Rule 8D of the Income Tax Rules, 1962.

Source: HC, Madras in M/s Marg Ltd. vs. CIT, Chennai

ITA No. 41 to 43 & 220 of 2017, dated Oct 1, 2020

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ITAT RULINGS

Depreciation is granted towards admission fees and processing charges paid for membership in stock exchange

Facts

The assessee is a Pvt. Ltd. Company engaged in stock exchange operations. During the relevant AY, the assessee had made payment to MCX-SX Stock Exchange towards admission fees and processing charges. Assessee had claimed it as a deduction. In the assessment order completed u/s 143(3) of the Income-tax Act,1961, the Ld. AO however disallowed the admission fees expenditure and held it to be a capital expenditure.

Aggrieved by the same, the assessee filed an appeal to the first appellate authority and submitted that the amount paid as admission fees in a stock exchange is only a permission to do trading in shares and no capital asset is acquired by the assessee. Therefore, it was submitted that the expenditure incurred as admission fees is to be allowed as a revenue expenditure. Alternatively, it was contended that if expenditure is to be treated as a capital expenditure, depreciation on the same is to be granted. The CIT(A) after referring to the precedence on the issue held that the expenditure being admission fees paid to a stock exchange is a capital expenditure. The CIT(A) however allowed the alternative claim of the assessee and granted depreciation on it. The assessee being aggrieved by the order of the CIT(A) filed an appeal before the Tribunal.

Ruling

The Tribunal relied upon the judgement of the Hon'ble Apex Court in case of *Techno Shares and Stocks Ltd vs. CIT* that the membership of stock exchange is business or commercial right conferred by the rules of exchange. The membership right is said to be owned by the member and used for the purpose of business. It was similar to a license or franchise and is to be treated as an intangible asset. The Hon'ble Apex Court, held that the owner used the said asset for the purpose of business and was entitled to depreciation on the same, on examining the nature and character of membership card, which enabled the assessee to trade on the floor or as a broker of the stock exchange. The membership was a business or a commercial right in the nature of license u/s 32(1)(ii) of the Act and was a right or a license owned by the assessee used by him as an asset, i.e. a capital asset.

Therefore, the CIT(A) has rightly treated the admission fee as a membership of the stock exchange capital asset and allowed alternative plea of assessee that depreciation is to be granted on the same. Hence, the order of CIT(A) was upheld and the appeal filed by the assessee was dismissed.

Source: ITAT, Bangalore in BGSE Financials Ltd. vs. DCIT, Bengaluru

ITA No. 3130 of 2018, dated Oct 6, 2020

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Service Charges collected by the Banks/Gateways cannot be considered as commission paid and provisions of section 194H are not applicable

Facts

The assessee company is in the business of developing and running online game on its own web portal, filed its return of income for AY 2015-16 pursuant to which the case was selected for scrutiny under CASS. During the course of assessment proceedings u/s 143(3), the AO observed that the assessee had debited an amount under the head "payment to Gateways". The assessee explained the same and stated that TDS was not deducted from the said payments. It was submitted that the said amount represents aggregate of the service charges retained by the Gateways from the amounts paid by the customers for enabling them to play online games in the portal of the company. He submitted that the terms and conditions under which the Gateway has rendered services to the customers were invariably recorded in the agreements between the company and the respective Gateways, which establish that the company, on the one hand, and Gateways on the other hand, were independent parties in their respective fields and, therefore, there was no necessity of deducting any TDS u/s 194H of the Act. the assessee preferred an appeal before the CIT(A), who deleted the disallowance made by the AO u/s 40(a)(ia) of the Act, and against the relief granted by the CIT(A), the revenue filed an appeal before the Hon'ble Tribunal.

Ruling

The Hon'ble Tribunal held that the "sale made on the basis of a credit card" is the transaction of the merchant establishment and that the credit company only facilitates the electronic payment for a certain charge and the commission retained by the credit card company is therefore in the nature of normal banking charges and not in the nature of commission/brokerage for acting on behalf of the merchant establishment. The service charges collected by the Banks/Gateways cannot be considered as commission paid by the assessee and, therefore, provisions of section 194H are not applicable. Further, it is also noticed that the Gateways have offered the income to tax in their hands in their respective returns of income. Resultantly, the appeal of the revenue was dismissed.

Source: ITAT, Hyderabad in ACIT vs. Head Infotech India Pvt. Ltd. ITA No. 2372 of 2018, dated Oct 1, 2020

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Unexplained Agriculture Income shall be treated as Unexplained Cash credit u/s 68 of the Income Tax Act

Facts

The assessee's case was selected for limited scrutiny for the reason that high cash shown in balance sheet as compared to preceding year and return of income filed after the due date. During the AY under consideration, the assessee derived income from his proprietorship firm besides, the assessee also had agricultural income and income from other sources namely interest. The assessee was asked to explain the high cash shown in the balance sheet, In response to which the assessee had submitted before the AO that the increase in cash balance was mainly due to receipt of cash from agricultural income and sale of school books during the Month of March which were usually paid by the customers in cash. The assessee was further asked to give details and substantiate

agricultural income by producing all evidentiary documents relating to alleged cultivation of land. In response, the assessee produced a certificate issued by the Anchal (ward) office, Lal ganj Vaishali, Bihar and land holding certificate. The AO rejected the contention of the assessee and held that mere statement of land purchase/holding is not sufficient. There was unsupported claim of cultivating the land and assessee did not demonstrate that he was doing agricultural activities and there was no evidence that assessee had obtained agricultural income. Therefore, the AO made an addition u/s 68 of the Act on the said unexplained Agriculture Income. Aggrieved by the order of the AO, the assessee carried the matter in appeal before the ld. CIT(A) who confirmed the order passed by the AO. Aggrieved by which the assessee filed an appeal before the Tribunal.

Ruling

The Tribunal held that the assessee in this case has claimed to have received agriculture income, therefore, the onus to prove the said receipt as exempt being agricultural income is on the assessee. The assessee failed to produce evidences other than the certificate issued by the Anchal Adhikari, Government of Bihar, Lalganj (Vaishali) and land holding certificate, the AO noted that the assessee did not produce any evidences to show that there was agricultural activity carried out in the land. The AO as well as the CIT(A) did not accept the claim of the assessee since he failed to prove the income is from agriculture activities, mere possession of land is no proof of earning agricultural income. Thus, the assessee failed to substantiate his claim. Hence, the view of the authorities was legally tenable and therefore, the order of the ld. CIT(A) is confirmed and the appeal filed by the assessee was accordingly dismissed.

Source: ITAT, Kolkata in Rajnarayan Prasad Singh vs. ACIT Circle, Shillong

ITA No. 142 of 2019, dated Oct 1, 2020

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CIRCULARS & NOTIFICATIONS

CBDT notifies Income Tax 22nd Amendment Rules, 2020

Central Board of Direct Taxes amends Rule 5, Form 3CD, 3CEB & Form ITR 6 and inserted rule 21AG, 21AH, Form 10 IE and Form 10 IF as the following:

1. In Rule 5(1) of the Income Tax Rules, 1962, it has been substituted that u/s 32(1)(iii) in respect of depreciation of any block of assets entitled to more than 40% shall be restricted to 40% only on the WDV of such block of assets in case of:
    I. A domestic company exercising option of concessional rate of taxes u/s 115BA(4) or 115BAA(5) or 115BAB(7); or
    II. An Individual/HUF exercising option of new and option income tax regime u/s 115BAC(5); or
    III. A Co-operative Society resident in India which has exercised option of paying taxes @ 22% u/s 115BAD(5);

The above rule is subject to conditions as stated in the notification.

2. Rule 21AG is inserted to specify that an individual/HUF exercising option u/s 115BAC(5) for any PY to the AY on or after April 1, 2021 shall file Form 10-IE electronically either under a DSC or EVC. Further, PDGIT(Systems) or DGIT(Systems) shall specify the procedure for filing Form 10-IE.

3. Rule 21AH is inserted to specify that a Co-operative Society exercising option u/s 115BAD(5) for any PY to the AY on or after April 1, 2021 shall file Form 10-IF electronically either under DSC or EVC. Further, PDGIT(Systems) or DGIT(Systems) shall specify the procedure for filing Form 10-IF.
4. The changes made in Form 3CD/3CEB and format of Form 10-IE & 10-IF can be checked here.

Source: Notification No. 82/2020 dated Oct 1, 2020.

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CBDT amends the manner of Investment in Provident Fund u/r Rule 67 of the Income Tax Rules, 1962 and notifies 23rd Amendment Rules, 2020

Rule 67(2) of the Income Tax Rules 1962 pertains to the manner of investment of all moneys contributed to a provident fund (whether by the employer or by the employees) after the October31, 1974, or transferred after that date from the individual A/c of an employee in any recognized PF maintained by his former employer or accruing after that date by way of interest or otherwise to the fund may be deposited in a Post Office Savings Bank A/c in India and to the extent such moneys as are not so deposited.

Therefore, CBDT allowed investments of the aforesaid funds in Securities having Single Rate 'A' or above. Earlier Investment were allowed in Securities having cibil Rate of 'AA' and above. This shall come into force from April 1, 2021 and therefore, shall be effective from AY 2021-22 onwards.

Source: Notification No. 84/2020 dated Oct 22, 2020.

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ITAT RULINGS

Questioning benefits to assessee on availing services is outside the scope of transfer pricing, where evidences to corroborate income submitted

Facts

Assessee was engaged in two segments wherein first is trading and second is manufacturing. Assessee has availed management support services from its AEs, which were reimbursed on cost to cost basis. As far as availment of management services were concerned, the case of the assessee was that the entities of Danisco group had the expertise available within the group and the cost of availment of such services were allocated to the entities on cost to cost basis applying suitable allocation key. The services were rendered pursuant to the arrangement between the assessees and its AEs through common pool. The case of the assessee is that the services were actually rendered and there was no duplication of services.

Ruling

Paperbook. In the present set of facts, the assessee has filed extensive evidences with regard to availment of services and it is not the jurisdiction of the TPO to question whether such availment of services is to be made by the assessee for better management of its business. The assessee company is part of an international group and to maintain its international standards such availment of services from the group entities, in order to maintain international standards for carrying on its business, is a business decision and such decision of the businessman cannot be questioned. The Assessing Officer/TPO also cannot sit in judgement as to what benefits are derived by the assessee from availment of such services.

Where the assessee was availing specialized services which were provided by the AEs from common pool and the evidences in this regard have been filed by the assessee and where the services were charged on cost to cost basis, there is no merit in the order of the Assessing Officer in questioning the availment of services and the benefit derived by the assessee. Under law the benefit, if any, arises to the assessee or not cannot be questioned. Hence, the payment made by the assessee being cost to cost reimbursement of the services availed from common pool is duly allowable as a business expenditure in the hands of the assessee. TPO has exceeded his jurisdiction in holding the value of the said international transaction at NIL.

Source: ITAT, Delhi in Danisco India Pvt. Ltd vs. DCIT
ITA No. 2846 of 2016, dated Oct 7, 2020

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Profit motive is not relevant in a government enterprise; to be excluded from list of comparables

Facts

Assessee is engaged in providing support services to its AE in nature of marketing and other support services and is reimbursed on cost plus basis for rendering said services to its AE. Assessee had applied

Transactional Net Margin Method for benchmarking its international transaction for Provision of Ancillary Management Support Services to its AE being most appropriate method and had computed its margin at 10.28% by applying OP/OC as PLI. Assessee in transfer pricing study report had selected six comparable companies as functionally comparable. However, TPO applied filters selected by assessee but also used additional filters and drew list of nine comparables as finally selected to benchmark international transaction. Being aggrieved by inclusion of A, G and T, the assessee preferred the present appeal before the tribunal.

Ruling

Referring to the decision of the Delhi High Court in Philip Morris in ITA No. 1468 of 2018, the tribunal held that A was not good comparable of concerns providing business support services, on the ground that in case of Government enterprises, profit motive is not relevant consideration and the Government company worked for public undertakings. G had been held to be not comparables by the Delhi High Court in Philips Morris (supra) itself on the ground that the company was established by the Government to provide Ancillary Management Support Services to Government Departments or their agencies. Assessee is also engaged in providing marketing and Ancillary Management Support Services to its AE; hence the concerns, A & G being Government concerns are not comparable and need to be excluded from the final list of comparables. Delhi High Court in Philip Morris had directed the exclusion of T as no segmental information was available in respect of the different segments operated by the company. Accordingly, T was not to be included in final list of comparables as well.

Source: ITAT, Delhi in Intercontinental Hotels Group India Pvt. Ltd vs. DCIT; ITA No. 4035 of 2016, dated Oct 14, 2020

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The right to use granted through licensing of a software does fall within the meaning of "Royalty" as provided for in the domestic law or the DTAA

Facts

Assessee is a company incorporated in Sweden and is engaged in the business of sale of software products and rendering information technology services. The business of the assesseee includes software materialization, marketing and support of the software material Qlikview for which it enjoys all intellectual property rights such as patent, trademark and copy rights. The assessee has entered into an agreement with its subsidiary QlikTech India Private Ltd. for onward sale of shrink wrapped software to the end users/customers in India as per the distribution / license agreement. As per the said agreement QlikIndia will promote and resell QlikTech products to the end users within the prescribed territory in accordance with the terms and conditions set forth in the agreement. The AO in the draft assessment order passed on 15th December 2016 held that the entire receipts amounting to Rs. 7,01,62,491/- from sale of software products is taxable as royalty under Article 12 of the India-Sweden Double Taxation Avoidance Agreement and u/s 9(1)(vi) of the Act. The assessee did not file any objection before the DRP but communicated that it would prefer an appeal before the Ld. CIT(A). The AO accordingly passed the draft assessment order on 27thJanuary 2017 computing the tax @ 10% on gross receipts amounting to Rs. 7,01,62,491/- as per the DTAA.

Ruling

The right to use granted through licensing of a software does riot fall within the meaning of "Royalty" as provided for in the domestic law or the DTAA. Any consideration for the same is not taxable as Royally under section 9(1)(vi) or the relevant DTAA. Thus, what has been transferred by the appellant is neither the copyright in the software

nor the use of the copyright in the software, but what is transferred is the right to use the copyrighted material or article which is clearly distinct from the rights in a copyright. The right that is transferred is not a right to use the copyright but is only limited, to the right to use the copyrighted material and the same does not give rise to any royalty income. The Tribunal held that consideration received by the assessee for sale of software cannot be treated as royalty under the provision of section 9(1)(vi) of the Act as well as Article 12 of the India-Sweden DTAA and that the sale of software products by the assessee to its Indian distributors for further sale to end users is not in the nature of transfer of "copyright" and therefore not taxable in the hands of the assessee as "royalty" under the provision of section 9 (1)(vi) of the Act as well as Article 12 of the India-Sweden DTAA.

Source: ITAT, Delhi in Quiktech International AB Co Quicktech India Pvy. Ltd. vs. DCIT; ITA No. 1185 of 2019, dated Oct 20, 2020

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