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## DIRECT TAX UPDATE

### SUMMARY OF JUDGEMENT

#### I. Transfer Pricing case laws:

##### 1. **First Blue Home Finance Ltd. Vs. DCIT (ITA No. 3072/Del/2013)**

Receipt of share application money by the assessee from the Associated Enterprise for a price less than the book value of the shares cannot be regarded as a "deemed loan" by the assessee to the AE and notional interest cannot be imputed thereon.

##### 2. **Infogain India Pvt. Ltd. Vs. DCIT (ITA No. 6134/Del/2012)**

Circumstances in which the Profit Split Method ("PSM") has to be preferred over the Transactional Net Margin Method ("TNMM") for determining the Arm's Length Price ("ALP").

#### II. Domestic case laws:

##### 1. **CIT Vs. Smt. Datta Mahendra Shah (ITA No. 1601 of 2013)**

Gains from sale of shares could be assessed as short-term capital on satisfying the test laid down by CBDT vide its instructions.

**2. Hoshiarpur Improvement Trust Vs. ITO (ITA No. 200/Asr/ 2010)**

Fulfilment of object of general public utility should be seen in broader sense for the definition of the charitable purposes under section 2(15) of the Act

**3.M/s. Parinee Developers Pvt Ltd. Vs. ACIT (ITA No. 6772/M/2013)**

Penalty should not be imposed merely because the income has been offered to tax in a later year and not in the current year.

**4. Venus Financial Services Ltd. Vs. Assistant Commissioner of Income Tax (ITA No. 5335/Del/2012)**

The expression "full value of consideration" used in section 48 of the Income-tax Act, 1961 ("the Act") does not have any reference to market value. Thus, the AO cannot ignore the price agreed between two parties and disallow the claim of capital loss.

**Transfer Pricing case laws:**

**1. First Blue Home Finance Ltd. Vs. DCIT (ITA No. 3072/Del/2013)**

Receipt of share application money by the assessee from the Associated Enterprise for a price less than the book value of the shares cannot be regarded as a "deemed loan" by the assessee to the AE and notional interest cannot be imputed thereon.

**Facts of the case:**

The assessee, a 100% Indian subsidiary of BHW Holding AG (BHW Germany), received Rs. 53,30,96,400 towards "Receipt of share application money" and demonstrated the international transaction of 'Receipt of share application' at ALP by following the Comparable Uncontrolled Price (CUP) method as the most appropriate method. The Transfer Pricing Officer ("TPO") observed that the book value of each share of the assessee company at the beginning of the year stood at Rs. 11.98 whereas, the assessee was found to have received share application money against such shares from its AEs at the rate of Rs. 10 per share.

The TPO held it as a transaction of 'transfer of assets of the company' to its AEs in the guise of issue of share capital and treated the same as deemed loan and made an adjustment of interest.

On appeal, the Commissioner (Appeals) upheld the TP adjustment. Assailing the said order passed by CIT(A), the assessee filed appeal before the Hon'ble Tribunal.

#### **Decision of the Hon'ble Tribunal:**

The Hon'ble Tribunal while deciding in favour of assessee held as under:

- An income is chargeable to tax, if it is either of a revenue character or of a capital nature having been specifically included in the ambit of income under the Act.
- The definition of income does not specifically include within its purview any capital receipt arising on issue of share capital.
- Thus it follows that the issue of shares at par or premium is a transaction on capital account, which does not affect the computation of total income of a company.

Thus, adjustment in form notional interest on deemed loan cannot be made merely because the assessee received share application money from the AE for a price which is less than the book value of the shares.

## **2. Infogain India Pvt. Ltd. Vs. DCIT (ITA No. 6134/Del/2012)**

**Circumstances in which the Profit Split Method ("PSM") has to be preferred over the Transactional Net Margin Method ("TNMM") for determining the Arm's Length Price ("ALP").**

### **Facts of the case:**

The assessee was engaged in the business of software development. The assessee adopted Profit Split Method (PSM) as the most appropriate method for the financial year 2007-08 relevant to the assessment year under consideration. In view of the fact that it transitioned from a back end software services company of its AE to being fully responsible for the execution and delivery of software services to the end customers, the TPO claimed that TNMM was the most appropriate method and made adjustments accordingly.

The assessee filed an appeal before the Dispute Resolution Panel ("DRP") wherein, DRP upheld the order of the TPO. Aggrieved by the order, the assessee filed an appeal before the Hon'ble Tribunal.

### **Decision of the Hon'ble Tribunal:**

The Hon'ble Tribunal while deciding in favour of the assessee held as under:

- PSM may be applicable in case where transaction involved transfer of unique, intangibles or any multiple transactions

interrelated international transactions which cannot be evaluated separately for determining the ALP of any one transaction.

- A perusal of the function of the assessee company reveals that the international transactions are highly integrated and interrelated and both the entities are contributing significantly to the value chain of provision of software services to the end customers.
- The assessee assigned weights to each activity keeping in view the relative importance in the entire value chain.

**Thus, the PSM is the most appropriate method for determination of ALP as the assessee as well as its AE had significant contribution to the transaction.**

#### **Domestic Case Laws:**

##### **1. CIT Vs. Smt. Datta Mahendra Shah (ITA No. 1601 of 2013)**

**Gains from sale of shares could be assessed as short-term capital on satisfying the test laid down by CBDT vide its instructions.**

#### **Facts of the case:**

The assessee is a senior citizen having income on account of capital gains, business income and income from other sources. During the year, the assessee claimed short term capital gains of Rs. 9.25 crores. The Assessing Officer ("AO") was of the view that the amount claimed as short term capital gains was in fact business income as assessee dealt with the shares of more than 60 companies during the year.

The assessee filed an appeal before the Commissioner of Income tax (Appeals) [CIT(A)], wherein CIT(A) decided in favour of assessee.

Aggrieved by the order of CIT(A), the Revenue preferred an appeal before the Hon'ble Tribunal wherein the Hon'ble Tribunal upheld the order of [CIT(A)]. Assailing the said order, the revenue filed an appeal before the Hon'ble Bombay High Court.

**Decision of the Hon'ble Bombay High Court:**

The Hon'ble Bombay High Court while deciding in favour of Assessee held as under:

The CIT (A) and Tribunal rightly concluded that compliance on the part of the assessee was done in accordance to Instruction No.1827 dated 31 August 1989 issued by the Central Board of Direct Taxes ("CBDT") which lays down tests for distinguishing the shares held as stock-in-trade and shares held as an investment.

**Thus, based on Instruction No. 1827 issued by CBDT, the income earned by assessee is treated as short term capital gains.**

**2. Hoshiarpur Improvement Trust Vs. ITO (ITA No. 200/Asr/ 2010)**

**Fulfilment of object of general public utility should be seen in broader sense for the definition of the charitable purposes under section 2(15)**

**Facts of the case:**

The assessee trust is set up, under the Punjab Towns Improvement Act 1922, (PTIA, in short) by the Government of Punjab and that the principal objective of the trust was to bring about improvement in the town. The Assessing Officer, however, required the assessee

to explain as to how the work done by the assessee trust, registered as pursuing objects of 'general public utility', qualifies to be eligible for exemption under section 2(15). The assessee submitted that it is a non-profit organization, owned and controlled by the State Government formed for the development of urban areas hence entitled for exemption under section 11 and 12 of the Act.

The AO referred to the tests laid down in **Lok Shikshan Trust Vs CIT [(1975) 101 ITR 234 (SC)]** and concluded that income earned by assessee cannot be treated as exempt.

The assessee filed an appeal before the Commissioner of Income tax (Appeals) [CIT(A)] wherein, CIT(A) upheld the order of the AO by stating that assessee trust does not get any grant from the State Government which shows that first it makes profits from land deals and then use the income so earned for the public causes stated. Aggrieved by the said order, the assessee filed appeal before the Hon'ble Tribunal.

#### **Decision of the Hon'ble Tribunal:**

The Hon'ble Tribunal while deciding in favour of the assessee held as under:

- An object of general public utility does not necessarily require that the activities or the beneficiaries must be funded or subsidized by the State.
- As long as broader public cause is served, whether by the State funding or by efficient regulation of the affairs, it is an object of general public utility.
- It is also important to bear in mind that costs of proper development of area are also costs incidental to the plots and units sold by the assessee and, therefore, these two things should not be seen in isolation.

Thus, the object of general public utility of the assessee was considered to be covered under the definition of charitable purpose u/s 2(15) and the benefit u/s 11 had been allowed for the entire income.

**3. M/s. Parinee Developers Pvt Ltd. Vs. ACIT (ITA No. 6772/M/2013)**

**Penalty should not be levied on a declared income irrespective of the year of disclosure.**

**Facts of the case:**

The assessee sold 1,51,520 sq ft of commercial area for a sum of Rs. 736.55 Crs, but the said area was not completed by the time relevant to the Assessment Year ("AY") under consideration. Basing on the method of accounting followed i.e. percentage completion method, the assessee offered sum of Rs. 239.27 Crs) for the year under consideration as the completed area works out to 42.92%. However, assessee reversed the sale to the extent of 36,038 sq ft amounting to Rs. 179.03 Crs for some reasons / developments. This amount of sales was not shown by the assessee in the AY 2009-2010 basing on the percentage completion method. However, the said amount was reflected in the return for the AY 2010-2011 based on the principle of pay as you earn.

The AO levied the penalty on this sum of sales of Rs. 179.03 Crs which is otherwise offered to tax in the AY 2010-2011.

The assessee filed an appeal before the Commissioner of Income tax (Appeals) [CIT(A)] wherein, CIT(A) upheld the order of the AO. Assailing the said order, the assessee filed an appeal before the Hon'ble Tribunal.



### **Decision of the Hon'ble Tribunal:**

The Hon'ble Tribunal while deciding in favour of the assessee held as under:

- This is the case of preponement of income, which is otherwise undisputedly offered to tax in the later year in order to end litigation with the Department.
- Since, it is already offered in the return of income for the AY 2010-2011, there is neither failure on the part of the assessee in matter of disclosure of particulars nor furnishing of any inaccurate particulars.
- When there is no tax loss to the Department and the only issue is year of taxability but when the tax rates are the same on facts, it is a settled proposition in law that the Department should not disturb the assessment of income offered in the subsequent assessment years.

**Thus, penalty should not be imposed merely because the income has been offered to tax in a later year and not in the current year.**

#### **4. Venus Financial Services Ltd. Vs. ACIT (ITA No. 5335/Del/2012)**

**The expression "full value of consideration" used in section 48 of the Act does not have any reference to market value; thereby, the AO cannot ignore the price agreed between two parties and disallow the claim of capital loss.**

#### **Facts of the case:**

The assessee was engaged in the business of investments and purchase/sale of land and immovable property. Apart from business loss, the assessee had also disclosed loss from capital gain transaction of selling shares of three unlisted company in the return of income. The Assessing Officer accordingly disallowed the claim

of long term capital loss of assessee in respect of shares of one company since the shares were sold at Rs. 0.10 per share whereas, the company whose shares were being sold showed the value of same at Rs. 3.50 per share.

The assessee filed an appeal before the Commissioner of Income tax (Appeals) [CIT(A)] wherein CIT(A) upheld the order of the AO. Assailing the said order, the assessee filed an appeal before the Hon'ble Tribunal.

#### **Decision of the Hon'ble Tribunal:**

The Hon'ble Tribunal while deciding in favour of the assessee held as under:

- The AO had disallowed the loss ignoring the documents filed by the assessee during the course of assessment proceedings and the valuation report of independent valuer who had determined the value of shares by applying NAV Method, which is well accepted method under the provisions of the Act.
- The AO has overlooked that the shares were duly transferred in the name of other party and the consideration was received by cheque.
- The long term capital gain or loss is to be computed in the manner laid down in section 48 of the Act wherein expression used is "full value of consideration received or accrued".

**Thus, the AO cannot ignore the price agreed between the parties for computation of capital gain/(loss) and disallow the claim of capital loss.**

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