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An e-newsletter from **Lakshmikumaran & Sridharan**, India

July 2022 / Issue–94

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July
2022

Article

Deduction under 10AA – Benefit available even after sunset date?

By **Karanjot Singh and Parvathy Kartha**

Introduction

Special Economic Zones ('**SEZ**') were introduced with an intent to drive economic growth along with quality infrastructure complemented by attractive fiscal package. Initially introduced in the form of SEZ Policy in 2000, the scheme was subsequently formalised in the form of SEZ Act, 2005 ('**SEZ Act**'). SEZ has, in today's world, become a very familiar terminology to the larger public/ layman as a result of growing interest of the public in tax debates and economic development of the country.

The SEZ Act[1] confers various exemptions/ benefits on SEZ developers and entrepreneurs under various tax laws. One such benefit provided is under Section 10AA of the Income Tax Act,1961 ('**IT Act**'). Section 10AA of the IT Act entitles every person being an entrepreneur[2] of a SEZ unit to claim deduction of the profits and gains derived from export of services or articles or things manufactured or produced through such unit subject to certain conditions as prescribed therein. The deduction is available in respect of units wherein, *inter-alia,* the manufacture or production activity had commenced before 31 March 2021. Certain provisions under the said section relevant for the present discussion have been summarised herewith:

[1] Section 26 and 27 of the SEZ Act

[2] Entrepreneur has been defined under Section 2(j) of the SEZ Act to mean a person who has been granted a letter of approval by the Development Commissioner under Section 15(9) of the SEZ Act.

- In case any unit entitled for deduction is transferred to another undertaking before expiry of the ten-year period during which deduction is available, in a scheme of amalgamation/de-merger, deduction shall be allowed to the successor unit as if the amalgamation/de-merger had not taken place.
- The deduction is not available to any unit which is formed by:
  a. splitting up, or reconstruction, of a business already in existence; or
  b. transfer to a new business, or machinery or plant previously used for any purpose.

It may be noted that the aforesaid conditions are applicable only for setting up of a new unit. In other words, the aforesaid prohibitions are not attracted in cases where an existing unit claiming deduction under Section 10AA of the IT Act expands its business by way of acquiring another unit/ purchase of used plant and machinery.

Although, the sunset date for setting-up new units in SEZ to claim income-tax deduction has lapsed, many taxpayers who had set-up units before the cut-off date and had commenced the manufacturing or production activities are still claiming deduction under the provision. It is also possible that certain taxpayers may acquire new units by way of amalgamation and demerger and commence claiming deduction (for the balance period) after the sunset date.

Section 10AA seeks to grant deduction in respect of eligible units to the taxpayers who are

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in compliance with the provisions of SEZ Act. Seen from that perspective, the deduction should be available to the person who is the owner of SEZ unit. Thus, assuming that the successor actually continues with the business of the eligible unit, acquisition of eligible unit by way of demerger/ merger with the intent of claiming deduction under Section 10AA is in line with the legislative intent.

There may be other cases where a taxpayer merges two eligible unit for business and corporate synergies. Such a case may have the effect of altering the eligible period of deduction under Section 10AA. Assuming that the business re-structuring is *bona fide*, and that the taxpayer has added substantial value to the newer unit, it can be argued that grant of benefit in such cases is in line with the SEZ and Income-tax laws.

Before elaborating this aspect, the relevant provisions under the SEZ laws have been summarised herewith:

- Every SEZ is under the administrative control of a Development Commissioner, and he shall be the overall in-charge of the SEZ[3]. Additionally, approval committees are also constituted for every SEZ which is chaired by the development commissioner. The LOA is issued by the development commissioner[4] basis approval accorded by the approval committee[5].
- The approval committee may approve proposals for diversification, enhancement of capacity of production, change in the items of manufacture or service activity subject to adherence to requirements as mentioned therein.

Thus, the expansion of SEZ units and claim of deduction for enhanced capacity is contemplated in the SEZ laws. Such expansion could be done by outright purchase of assets or through corporate re-structuring. The aforesaid discussion can be explained by way of the following example:

An assessee having a unit in a SEZ, say unit A having a production capacity of 50 units, exhausts the deduction under Section 10AA of the IT Act. With an intent to take benefit of synergies, the assessee acquires another unit in the same SEZ say unit B consequent to de-merger from another entity. The assessee seeks approval for both the units under the same proposal wherein one LOA is granted. Unit B prior to the de-merger had a production capacity of say 100 units. Post de-merger, the assessee adds plant and machinery (which was earlier being used in unit A) to unit B and the total output of Unit B increases to 200 units. It may be possible that the availability of deduction under Section 10AA is one of the motives of de-merger, but it can still be argued that the deduction should be available in respect of all 200 units. This is because the assessee post de-merger has continued the business of unit B and has made substantial expansion to the said unit. Accordingly, the deduction should be available to the assessee both for the original as well as the increased production capacity.

In the aforesaid illustration, essentially, an entrepreneur may be able to claim deduction in respect of supplies effected using assets which were earlier used in Unit A and subsequently in Unit B beyond the stipulated period of 10 years. Such a practice, it can be argued, is not a façade provided the assessee is able to substantiate that the assets of Unit A have been actually integrated with Unit B and thereby resulting increased production capacity of the Unit B.

[3] Rule 20 of SEZ Rules, 2006 read with Section 11 & 12 of SEZ Act, 2005
[4] Rule 19 of SEZ Rules, 2006
[5] Section 13 read with Section 14 of the SEZ Act, 2005

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Thus, essentially, this would be a case involving mere expansion of Unit B.

It goes without saying that guising the business of an existing unit for which the ten-year deduction has been availed in another eligible unit may be seen as abuse of provisions of Section 10AA and may result in invocation of GAAR provision. In a case where the taxpayers merely shift the business of one unit to another unit without adding any value to the subsequent unit, the deduction should be denied to the assessee.

Considering that the availability of deduction boils down to the conduct, the taxpayers may be required to demonstrate genuineness of business re-organisation involving merger/de-merger of eligible units. Factors such as integration of assets, manpower employed, production capacity etc. may be looked into by the tax officer to examine the eligibility to claim deduction post the business re-structuring process.

Amongst others, maintenance of separate books of accounts *qua* the unit and ensuring substantial investment in the new unit would help the assessee in proving the genuineness of the merger/ demerger and thereby claiming the deduction.

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Notifications and Circulars

Virtual Digital Assets (‘VDA’) clarified

Scope of the VDA

The definition of VDA contained in Section 2(47A) of the Income-tax Act, 1961 (‘**Act**’) empowers Central Government to exclude any digital asset from the definition of VDA. *Vide* Notification No. 74/2022, following virtual digital assets have been excluded from the definition of VDA:

- Gift card or vouchers, being a record that may be used to obtain goods or services or a discount on goods or services:
- Mileage points, reward points or loyalty card, being a record given without direct monetary consideration under an award, reward, benefit, loyalty, incentive, rebate or promotional program that may be used or redeemed only to obtain goods or services or a discount on goods or services.
- Subscription to websites or platforms or application

The definition of VDA includes a Non-Fungible Token (‘**NFT**’) as may be notified by the Central Government. *Vide* Notification No. 75/2022, the Central Government has specified NFT as a token which qualifies to be a VDA. However, it

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does not include NFT whose transfer results in legally enforceable transfer of underlying tangible asset.

Tax withholding under Section 194S on transfer of VDA

- Section 194S is effective from 1 July 2022. Where sum is paid or credited before 1 July 2022, then Section 194S will not apply. However, for the purpose of calculation of threshold limits of INR 50,000/10,000, the amount shall be reckoned from 1 April 2022.
- Once tax is deducted under Section 194S, Section 194Q shall not apply.
- In case where consideration is in kind, the buyer is required to ensure that tax required to be deducted in respect of such transaction has been paid by the seller. Thus, the buyer is required to release the consideration only after seller provides proof of payment of such tax.
- In case where VDA is exchanged with another VDA, both buyers and sellers are required to pay tax in respect to transfer of VDA and show the evidence to other so that VDAs can then be exchanged.

Vide Circular No. 13 of 2022, Central Government has issued certain guidelines with respect to tax withholding on transfer of VDA through an Exchange. Key highlights of the circular are as under:

- Tax may be deducted by the Exchange only which is crediting or making payment to the seller.
- In case Exchange is crediting or making payment to the broker (not being the seller of VDA), the obligation to withhold tax lies on both the Exchange and the broker. However, subject to a written agreement between the broker and the Exchange, the broker alone may withhold tax in such situation.
- In case where VDA being sold is owned by the Exchange, then the buyer or his broker would not be required to withhold tax if the following conditions are satisfied:
- Exchange enters into a written agreement with the buyer or his broker that the Exchange would be paying the tax on or before the quarterly due date.
- Exchange would report all such transactions in its quarterly tax withholding statements (i.e., Form 26QF[6])on or before the prescribed due dates.
- Exchange includes all these transactions in its return of income.
- Where the consideration for transfer of VDA is in kind, then the buyer and seller would not be independently required to deduct tax under Section 194S of the IT Act if the Exchange after entering into a written contractual agreement with the buyers/sellers deducts and pays tax under Section 194S to the credit of the CG.
- The tax is required to be deducted on the net consideration after excluding GST/charges levied by the deductor for rendering service.
- Payment gateways are exempted from application of Section 194S provided the seller/Exchange, as the case may be, has deducted tax under Section 194S.

Vide Notification No. 67/2022, it is stated that tax withheld under Section 194S is required to be deposited in challan cum statement in Form No. 26QE within 30 days from the end of month in which the tax was withheld. Within 15 days of due date of furnishing Form No. 26QE, the deductor is required to furnish certificate in Form No. 16E to the payee.

[6] Notified by Notification No. 73/2022.

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Mutual Agreement Procedure (MAP) guidance updated – Interplay with *Vivad se Vishwas*

MAP guidance has been updated to provide that the Competent Authorities (CA) of other countries/specified territories may accept MAP applications from their taxpayers being Associated Enterprises (AE) of Indian resident taxpayer who has settled transfer pricing adjustments on international transactions with their AEs under Vivad se Vishwas Act. The CAs may notify the CA of India and thereafter the latter will allow access to MAP. However, the result of the Vivad se Vishwas, cannot be deviated. Instead, a correlative relief would be requested from treaty partners. CAs of India shall not provide access to MAP to a non-resident taxpayer who has himself opted for VsV on the same issue.

A new part is added to MAP guidance to list down responsibility of applicants for true disclosure and providing up-to-date information. If the provisions of the MAP guidance are in conflict with any other domestic legislations, rules DTAAs, etc., then the domestic rules, legislations, DTAAs etc. will prevail.

Tax benefits under Sovereign Gold Bond Scheme, 2022-23[7]

Through Notification G.S.R. 454(E) [F.NO.4(6)-B(W&M)/2022], the Central Government has introduced the Sovereign Gold Bond Scheme, 2022-23. The scheme specifies that capital gains arising on redemption of bonds to an individual will be exempt. Further, indexation benefits will be provided for the long-term capital gains arising to any person on transfer of bond. However, interest income received on gold bonds will be taxable.

[7] Captured only through the perspective of IT Act.

Tolerance range notified for calculating Arm's Length Price ('ALP') for A.Y. 2022-23

Notification No. 70/2022 provides for a tolerance range of 1% for wholesale trading and 3% in all other cases for computation of ALP for AY 2022-23. The term wholesale trading has been defined to mean an international transaction or specified domestic transaction of trading in goods which fulfils the following conditions:

- Purchase cost of finished goods is 80% or more of the total cost pertaining to such trading activities; and
- Average monthly closing inventory of such goods is 10% or less of sales pertaining to such trading activities.

No tax withholding on lease rentals paid for leasing of aircrafts to lessors in International Financial Services Centre (IFSC)

Notification No. 65 of 2022 has been notified by the Central Government stating that no tax withholding will be required under Section 194-I of the IT Act on payment of lease rent or supplemental lease rent for leasing an aircraft, made by a lessee to a lessor being unit located in IFSC. It is stipulated that the lessor is required to intimate in Form 1 the details of the years for which the lessor opts for claiming deduction under Section 80LA of the Act. The exemption will be available only for the years for which deduction under Section 80LA is being claimed. Further, the lessee needs to furnish details of all the payments made by him to the lessor on which tax was not deducted in quarterly withholding tax statements. The term aircraft means an aircraft, a helicopter, or an engine of an aircraft or a helicopter, or any part thereof.

The Notification comes into force from 1 July 2022 and it has Form No. 1 attached with it.

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Ratio Decidendi

Reimbursement paid by Indian entity to overseas entity towards salaries of employees seconded to Indian entity is not Fees for Included Services, absent satisfaction of make-available clause

The petitioner company provides information technology solutions and support services for e-commerce industry. During the course of its business, the petitioner had paid reimbursements on cost-to-cost basis to Walmart Inc., Delaware, USA (**'Walmart'**) for AY 2020-21, towards salaries paid by the Walmart to expatriate employees seconded to the assessee. This transaction arose from the Inter-Company Master Service Agreement (**'Agreement'**) entered into between Flipkart Singapore and Walmart for secondment of employees and provision of services. As per this Agreement either of the parties to the Agreement or its affiliates could use the seconded employees. Further, the party placing the secondees would invoice the compensation and wage cost of secondees incurred in the home country. Walmart seconded 4 employees to the petitioner who would work for the petitioner's benefit. The salaries for such seconded employees were paid by Walmart for administrative convenience and the petitioner later reimbursed Walmart for the same. The petitioner filed an application u/s 195(2) of the Act, requesting for issuance of 'nil-tax deduction at source' certificate with respect to these payments towards reimbursements. The Income-tax Department ('**ITD**') rejected this application *vide* order ('**195(2) Order**') and directed the petitioner to deduct tax at source ('**TDS**') at the applicable rates. Aggrieved, the petitioner filed a writ petition before the Karnataka High Court ('**HC**') challenging the aforesaid order and seeking direction to the ITD to issue a nil-TDS certificate u/s 195(2).

The HC dealt with the issue whether the petitioner had to deduct TDS u/s 195(2), IT Act read with Article 12(4) of the DTAA? Article 12, *inter alia,* deals with taxation of FIS arising in one State and paid to the other State's resident and Article 12(4) provides the definition of FIS. The HC relied on Section 90(2), IT Act and the Supreme Court judgement in *Engineering Analysis Centre of Excellence Private Limited* v. *Commissioner* [2021 432 ITR 471 (SC)] to hold that definition of FIS in Article 12(4), DTAA being more beneficial for the petitioner with respect to its tax-withholding liability, is to be considered in the present case instead of the less beneficial corresponding FTS provisions of the IT Act. The HC referred to the Agreement to hold that in spite of the secondees having the necessary experience/skill/training to complete the concerned services, the secondment in the present case does not fulfil the make-available condition and thus no FIS arise.

In connection with the above question, the HC also dealt with the aspect of whether the petitioner is the employer of the secondees during the secondment period. The HC noted that petitioner issues the appointment letters to the secondees, who also report to the petitioner and the petitioner has the power to terminate the services of the secondees. Thus, the HC, for the limited purpose of Section 195, observed that the petitioner could be concluded to be the employer of the secondees during the secondment period. Further, Walmart's power to decide on the employees' continuance after the secondment

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will not make any difference as it relates to a service condition post the period of secondment and does not alter relation between Assessee and the employees.

The HC also observed that the SC decision in the case of *Commissioner* v. *Northern Operating Systems* (Civil Appeal No. 2289-2293/2021), is in the context of service tax. The precise question before the SC was whether supply of manpower was a taxable service provided by foreign company to Indian company. However, the question before the HC in present case is whether secondment of employees is FIS, which is 'made available' to the Indian Company. Any conclusion on an interpretation of secondment in the Agreement to determine who the employer is and the nature of payment by itself would have no conclusive bearing on whether the payment made is for 'FIS' in light of the further requirement of 'make available'.

The HC also referred to its observation in *Director of Income Tax (International Tax)* v. *Abbey Business Services India (P.) Ltd.* [(2020) 122 Taxman.Com 174] that 'a secondment agreement constitutes an independent contract of services in respect of employment with assessee.'

Consequently, the HC set aside the 195(2) Order and directed the ITD to issue a Nil-TDS certificate under Section 195(2) of the IT Act. [*Flipkart Internet Private Limited* v. *Deputy Commissioner of Income Tax (International Taxation)* - TS-503-HC-2022(KAR)]

Reference to TPO made after expiry of assessment time limit is bad in law – Assessee not barred by estoppel to challenge such time-barred reference and subsequent proceedings

The appellant had filed its return of income on 30 November 2006 for the AY 2006-2007. The Assessing Officer ('**AO**'), after receiving approval by communication dated 18 November 2008 from Commissioner of Income Tax (**'CIT'**), referred the appellant's case on 17 February 2009 to the Transfer Pricing Officer ('**TPO**') under Section 92CA of the IT Act for computation of arm's length price for certain international transactions entered into by the appellant. Notably, the time limit for passing the Assessment Order, in cases where TP reference is not made, was 21 months from the end of the relevant AY i.e., 31 December 2008. Draft assessment order was passed by the AO on 31 December 2009 ('**Draft Order**'). The appellant raised objections with the Dispute Resolution Panel (**'DRP'**), including regarding expiry of limitation period for making reference to the TPO. The appellant's objections were rejected by the DRP *vide* order dated 24 September 2010 ('**DRP Oder**'). The appellant filed a writ petition and subsequently, an intra-court appeal with the Madras High Court on the issue whether reference to the TPO was time-barred. The HC analysed various IT Act provisions on assessment timelines and judicial precedents to observe that:

a. As per the language of Section 153(1) and the scheme of the Act, the reference to the TPO must be made *during the course of the assessment proceedings* and before the expiry of limitation to pass the assessment order, which is 21 months from the end of the relevant AY (i.e., till 31 December 2008), as per Section 153, as it stood at the relevant time.

b. When one proviso specifies a time-limit and other proviso extends it in specific circumstances, then the two provisos cannot be considered independent of each other and have to be read together. The 1st and 2nd provisos to Section 153(1), as it stood at the relevant time, provide 21 months' time period to complete assessment. During this 21 months' time period, if a reference to the

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TPO is made and is pending, then the time limit to complete assessment gets extended by further 12 months. *Such extension is provided only if the necessary condition (i.e., of making a reference to the TPO) is fulfilled during the 21 months' normal time limit of completing assessment proceedings*. Further this extension is provided only upon making of a valid 'reference' to TPO and not merely on getting an 'approval' from the Commissioner to make such a reference to the TPO.

c. If a reference to the TPO is not made within the 21 months' time limit, then such reference cannot be made subsequently.

d. The various time limits to be followed by the TPO, AO, assessee and DRP during the assessment proceedings, are triggered only when the reference to the TPO is made. In the present case, the reference was made after expiry of the 21 months' time limit, i.e., on 17 February 2009. Further the DRP Order and the final assessment order by the AO were also not passed within the prescribed time limits.

e. With respect to the ITD's contention of the appellant being estopped from initiating objections against the assessment proceedings, the HC held that this question of limitation being a legal plea, can be raised at any point of the proceedings since it goes to the root of the relevant authority's jurisdiction and there cannot be waiver of statutory right. The appellant had specifically raised the objection on limitation before the DRP. Further, the appellant was unaware of the actual date of reference when it had furnished its documents and objections before the TPO. There is no estoppel in taxing laws.

The HC thus held that since the reference to the TPO is bad in law, being time-barred, any proceedings in furtherance of the same are also bad in law. [*Virtusa Consulting Services Pvt. Ltd.* v. *DRP/JCIT/ACIT* - TS-474-HC-2022(MAD)]

Actual sale consideration when to be considered instead of stamp duty value, under Section 50C – ITAT also allows exemption under Section 54F; rejects addition of notional rent and rejects application of Section 50 on capital gains from sale of building incapable of depreciation

Four issues were dealt by the ITAT in the present case -

Issue 1: Adoption of stamp duty value by the AO as deemed consideration under Section 50C:

The appellant sold a property consisting of land and buildings for Rs. 8,81,00,000 (Rs. 6,55,07,063 was the value of land and INR 2,18,50,441 was the value of buildings). The stamp duty valuation of the property (land and buildings) was INR 11,19,40,441 (INR 9,90,99,000 was the value of land and INR 1,28,41,441 was the value for buildings). For computing capital gains u/s 50C(1), IT Act, the AO adopted the higher values for the land and the buildings, i.e., the stamp duty value of land at INR 9,90,99,000 and sale value of buildings as stated by the appellant at INR 2,18,50,441, which totalled to INR 12,09,49,441 (exceeding the total stamp value of both the land and the buildings). The CIT(A) upheld the AO's adoption of stamp duty value for computation of capital gains under Section 50C. However, the CIT(A), as a limited relief, held that for the buildings too, the AO should have adopted the stamp duty value for computing capital gains under Section 50C. On appeal, while the ITAT agreed that there cannot be double standards in adopting the stamp duty value of the land and not of the buildings, it directed the AO to consider the actual sale

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consideration for computing capital gains for the following reasons:

a. during the assessment proceedings, the appellant had objected to adoption of stamp duty value by giving full particulars of the fair market value of the property. The appellant filed detailed submissions with evidence showing that market price of the concerned property was much lesser than the price notified by the Government for stamp-duty purposes since the said property were old and unmaintained house property in a bad condition which was not fit for living.

b. as per Section 50C(2), IT Act, any objection raised by the assessee against application of Section 50C(1) must be referred by the AO to the valuation officer for determination of fair market value of the property.

c. in the instant case, the AO violated the procedure prescribed under Section 50C(2) without discussing any reasons for the same. Further, there was no finding or allegation that the appellant received any excess amount over the actual sale consideration as stated in the deeds.

Issue 2: Allowability of exemption u/s 54F, IT Act:

The appellant purchased a new house property within the prescribed time limit and claimed exemption from long term capital gains under Section 54F. The AO denied the exemption on the ground that the appellant owned seven residential houses (i.e. more than one) on the date of transfer of the concerned property/capital asset. The CIT(A) ruled in favor the appellant, observing that all conditions have been met for claiming exemption under Section 54F. The CIT(A) held that the aforesaid houses are not capital asset, as defined under Section 2(14), IT Act and cannot be considered as residential houses owned by the appellant on the date of transfer, as given under the proviso to Section 54F(1). In this regard, the CIT(A) specifically observed that:

a. the appellant regularly maintained a separate trading account for its trading business in real estate which is a part of the audited financials.

b. as per the trading accounts and audited financials of FY 2012-13 till FY 2016-17, the seven residential houses are reflected as stock-in trade of the appellant's trading business.

c. aforesaid houses are 40-50 years old, unusable, with no electricity or water connection, unfit for habitation (either residential or commercial) unless subjected to major renovations.

d. Appellant has incurred expenses and sold some houses in earlier years. However, the appellant was unable to sell the aforesaid 7 houses, despite best efforts, due to which they are kept as stock-in-trade.

e. The appellant purchased new residential property within the time line prescribed u/s 54F.

f. The AO has not refuted the aforesaid contentions/submissions of the appellant. Further, the AO also considered the aforesaid houses as trading properties when he computed notional rent arising from the same (i.e., Issue no. 3).

The ITAT upheld the decision of CIT(A) on this count, in favor of the appellant.

Issue 3: Computation of notional rent on old and unsuable house properties:

On the aforesaid seven residential houses, the AO, after relying on the Delhi HC's decision in *CIT* v. *Ansal Housing Finance & Leasing Co Ltd.* [2013] 354 ITR 180 (Delhi)] had made additions under the head 'income from house property' to

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the appellant's taxable income by computing notional rent on these house properties. The CIT(A) upheld this addition. The ITAT, however, ruled in the appellant's favor by distinguishing the aforesaid Delhi HC decision on facts and noting that:

a. The aforesaid 7 properties were held as stock-in trade by the appellant

b. The said house properties are old, dilapidated and unfit for habitation. In this regard, the appellant had produced certain evidence during assessment proceedings which were not at all dealt with in the report of the Inspector who was appointed by the AO to inspect these properties. This proves that the appellant's submissions on the state of the properties are valid.

c. In the *Ansal Housing (supra)* decision, the concerned buildings were new, ready to use for habitation while this is not true for the instant case.

Issue 4: whether Section 50, IT Act is applicable on capital gains from sale of buildings?:

The appellant also had land and buildings at SEZ Jodhpur which were used for business upto the end of FY 2011-12, after which the said business was discontinued. From 1 April 2012, the said buildings, being not used for the purpose of business, were considered as incapable of being depreciable assets. In compliance with Section 50, IT Act, in the year that these assets were discarded as business assets, the written down value of the same, as on 1 April 2012 was excluded from the block of assets and was separately shown in the balance sheet. The land and buildings were then treated as investment assets by the appellant from AY 2013-14 onwards. Further, no depreciation was charged with respect to such buildings from AY 13-14 onwards. More than 3 years later, in FY 16-17, the appellant sold the land and buildings of the discontinued business and contended that the capitals gains arising from the sale of buildings in SEZ Jodhpur were long term capital gains. The AO invoked Section 50 to assess capital gains on these buildings as short-term capital gains, *inter alia*, observing that the said buildings continue to be depreciable assets on the date of sale because once an asset has been treated as being a part of a block of assets, it will continue to be treated so, regardless of its disposal or the manner of disposal. The nature of the building will not be altered by the fact that the no depreciation was claimed on the same by the appellant and that no business operations were carried out therefrom. The CIT(A) upheld the AO's decision.

The ITAT accepted the appellant's submissions and held that Section 50 is not applicable to the instant case because once the buildings became incapable of being termed as business assets, they stopped being a part of the block of assets, after the value of the same were reduced from the value of the block of assets. Further, even if Section 50 is to be applied here, the AO should have reduced the full consideration value from the written down value of the complete block (i.e., all the building in both Jodhpur and Jaipur), however, the AO only reduced the written down value of the buildings in Jodhpur and not Jaipur. Thus, the ITAT noted that there was a lacuna in application of Section 50 to the instant case by the ITD. [*DCIT* v. *Goverdhan Prasad Singhal* - TS-487-ITAT-2022(JPR)]

Re-assessment proceedings initiated during pendency of CIRP when valid

The petitioner companies had voluntarily filed applications for the Corporate Insolvency Resolution Process (**'CIRP'**) under Section 10 of the Insolvency and Bankruptcy Code, 2016 (**'IBC'**) on 28 February 2018 before the National Company Law Tribunal, Mumbai (**'NCLT'**) and these applications were admitted by the NCLT in

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March 2018. Subsequently, in March 2018 itself, the Revenue initiated reassessment proceedings for various AYs in the petitioners' cases by issuing notices under Section 148 of the IT Act. Further, the objections filed by the petitioners against the aforesaid reopening of various completed assessments were also rejected by the Department by various orders.

Consequently, the petitioners challenged the aforesaid notices and orders by filing writ petitions on 26 December 2018 before the Madras HC. *Vide* interim orders dated 27 December 2018, the HC allowed the department to continue with the assessments but directed it to keep the assessments in a sealed cover. On 9 June 2020, the NCLT approved the resolution plan in the petitioners' case.

The Madras HC, after considering the Supreme Court decision in *Ghanashyam Mishra & Sons (P) Ltd.* v. *Edelweiss Asset Reconstruction Co. Ltd.* [(2021) 9 SCC 657] held that:

a. A resolution plan, upon getting approved by the adjudicating authority, is binding on the corporate debtor, its employees, creditors, members, and other stakeholders involved in the said plan.

b. In the present case, while the impugned notices u/s 148 were issued in March 2018, the resolution plan, which was submitted on behalf of the petitioners on 21 May 2019, did not address to any concessions from the ITD. The approved resolution plan also did not deal with any tax dues under the IT Act.

c. Additionally, at the time of approval of the resolution plan, the reassessment proceedings under Section 148 of the IT Act were yet to be crystallised/finalised.

d. The objections filed by the petitions against the initiation of reassessment proceedings were also not in accordance with the insolvency proceedings voluntarily initiated by the petitioners.

e. Since the impugned notices under Section 148 were issued after the petitioners had already voluntarily initiated insolvency proceedings, the petitioners should have ensured that the ITD had proper notice of the insolvency proceedings and should have obtained the necessary concessions from the ITD in the resolution plan.

f. Importantly, the NCLT also did not consider the ITD's claims while approving the resolution plan.

Thus, on facts of the case, the HC dismissed the writ petitions by holding that the aforesaid insolvency proceedings and the approved resolution plans cannot infringe ITD's right to initiate reassessment u/s 148 of the IT Act and consequently pass an assessment order. [*Dishnet Wireless Ltd.* v. *ACIT* - [2022] 139 taxmann.com 493 (Madras)]

Depreciation on goodwill, arising out of acquisition of businesses as going concerns in a slump sale before 1 April 2021 is allowable

During AY 2015-16, the assessee company had claimed depreciation @ 25% on goodwill arisen on account of acquisition of a proprietary concern and a limited company on slump sale basis. The AO held that the assessee couldn't substantiate its claim of paying huge amounts for goodwill of the aforesaid two concerns and also could not produce any basis or evidence for determination of the value of goodwill. Thus, the AO held the aforesaid transaction as being a sham and a colorable device to claim higher depreciation. The AO applied Explanation 3 of Section 43(1) of the IT Act and reduced the goodwill amount from the value of intangible assets. The CIT(A) upheld the AO's disallowance of depreciation. Aggrieved, the assessee approached the ITAT,

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Bengaluru, which made the following observations:

a. The fifth proviso (presently the sixth proviso) to Section 32(1), *inter alia*, restricts the aggregate deduction claimed by the predecessor and successor in case of succession referred to in Section 47(xiv). Section 47(xiv) does not apply to the instant case because:

   - All assets and liabilities of the proprietary concern were not transferred to the assessee, as required. Only the assets which were part of the undertaking were transferred.
   - Assessee paid consideration to the seller through banking channels and there was no consideration by way of allotment of shares in the assessee company.
   - Sellers paid taxed on the consideration received as capital gains.

   Since Section 47(xiv) does not apply to the aforesaid transaction, hence fifth (presently, the sixth) proviso to Section 32(1) also would not be applicable. Further, the fifth (presently, the sixth) proviso applies only where assets already existed in the predecessor's books and on which the predecessor was claiming depreciation before the transfer. It does not apply on assets which are recognised only by the successor pursuant to the slump purchase.

b. Application of Explanation 3 to Section 43 of the IT Act by the AO is erroneous since this provision applies only in the cases where the concerned assets were used, at any time by any other person for his business/profession. In the instant case, the concerned asset is the goodwill arising due to transfer of business. This goodwill appeared in the transferee assessee's books and never appeared in the seller's books. This asset was never used by any other person, as required in Explanation 3 to Section 43. Thus, this provision is not applicable to the assessee's case.

c. The goodwill in the present case was a commercial or business right under the category of an intangible asset and was allowed to be depreciated under Section 32 of the IT Act.

d. A reading of the various amendments introduced by the Finance Act, 2021 due to which depreciation on goodwill was disallowed with effect from 1 April 2021, i.e., from AY 2021-22 onwards, shows that the legislative intent behind these amendments was not to disallow depreciation on goodwill prior to coming into effect of these amendments.

e. The Revenue department accepted the capital gains offered for taxation for AY 2015-16 by the MD who sold the goodwill to the assessee and thus the same transaction cannot be doubted in the hands of the purchaser assessee.

Further, the AO has not established that the main purpose of the aforesaid transaction was to reduce the assessee's income-tax liability by claiming extra depreciation on increased cost. [*I&B Seeds Pvt Ltd.* v. *DCIT* - TS-509-ITAT-2022(Bang)]

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