Desai Saksena & Associates

31st May, 2024

Friday Tax Alert

From:

Tax Team of Desai Saksena and Associates
Chartered Accountants

CA Varsha Nanwani (Senior Manager - Taxation)
Vikas Jogle (Manager - International Taxation)
CA Neelu Dusseja (Senior Manager – Indirect Taxation)
CA Neha Patel (Manager - Taxation)
CA Ajay Sachani (Manager - Taxation)
Digvijay Hirwani (Assistant Manager - Taxation)
Alok Sharma (Deputy Manager - Indirect Taxation)

Contacts:

If you have any questions or would like to have additional information on the topics covered in this alert, please email one of the following DSA professionals:

- ✓ CA Varsha Nanwani (Senior Manager – Taxation)
  varsha@dsaca.co.in
- ✓ Vikas Jogle (Assistant Manager – International Taxation)
  vikas@dsaca.co.in
- ✓ CA Neelu Dusseja (Senior Manager – Indirect Taxation)
  neelu@dsaca.co.in
- ✓ CA Neha Patel (Manager - Taxation)
  neha@dsaca.co.in
- ✓ CA Ajay Sachani (Manager – Indirect Taxation)
  ajay@dsaca.co.in
- ✓ Digvijay Hirwani (Assistant Manager - Taxation)
  digvijay@dsaca.co.in
- ✓ Alok Sharma (Deputy Manager – Indirect Taxation)
  sharma.alok12@gmail.com

No additions invoking section 69B if expenditure was held disallowable u/s 40A(3) & not for unexplained expenditure: ITAT

The assessee was engaged in the manufacturing of fabrics and readymade garments. A survey under section 133A of the Income Tax Act ("the Act") was conducted at the business premises of the assessee wherein the assessee surrendered an amount on account of excess stock over and above its normal business income, discrepancy in cost of building and on account of disallowance under section 40A(3) of the Act which provides that any expenditure incurred by an assessee in respect of which a payment or aggregate of payments made to a person in a day exceeds ₹ 10,000 in cash, will not be allowed as a deduction while computing the income chargeable under the head Profits and gains of business or profession.

Subsequently, the assessee filed its return of income by declaring total income, including the surrendered income. The Assessing Officer (AO) contended that the surrendered income on account of cash expenditure was chargeable under section 69B the Act and to be taxed as per the provisions of section 115BBE of the Act whereby the income found to be undisclosed or unexplained during the course of an assessment, is taxed at a flat rate of 60%, along with applicable surcharge and cess.

Aggrieved by the order, the assessee preferred an appeal to the CIT(A). The CIT(A) confirmed the AO's additions, and the matter reached the Amritsar Tribunal.

The Tribunal held that there was no finding that cash expenditure had been found and that it had not been accounted for. In such a situation, it was not understood as to how the deeming provisions can be invoked.

Where the expenditure has been held disallowable in terms of section 40A(3) of the Act, which means that certain expenditure has been incurred, accounted for in books of accounts and is incurred in cash in violation of section 40A(3) of the Act, the question of unexplained expenditure or unaccounted expenditure doesn't arise for consideration. Hence, the action of the AO in invoking the deeming provisions in this regard was set aside. *[Gurinder Makkar vs DCIT - [2024] 162 taxmann.com 731 (Chandigarh - Trib.)]*

Factual error in date of notice invalidates assessment as it was claimed to be served before that date: ITAT

The assessee filed its return of income for the relevant assessment year. Subsequently, the Assessing Officer (AO) issued a notice under section 148 of the Act after recording the reasons for reopening the assessment. The notice was dated 27-03-2017. However, AO claimed that it was issued on 15.03.2017 and served upon the assessee on 20.03.2017 by way of affixture through the inspector without the presence or signature of two independent witnesses of the neighbourhood and, consequently, AO passed the assessment order.

The assessee contended that the notice cannot be issued and served a week before the mentioned date on the notice. Further, there was a gross violation of the procedure in the service of the notice by way of affixture as laid down under section 282 read with rule 12, 17 and rule 19 of Order (v) of Civil Procedure Code, 1908.

The assessee challenged the assessment order before CIT(A) that the assessment order passed by AO was bad in law, but the CIT(A) affirmed the AO's order. The assessee challenged the same before the Tribunal.
The Tribunal held that the date mentioned on the notice issued under section 148 of the Act was 27-03-2017. However, the AO has stated that the notice was issued on 15.03.2017 and served upon the assessee on 20.03.2017. In our view, it is beyond human probabilities to issue and serve notice a week before a date mentioned in the alleged notice issued under section 148 of the Act. Such factual mistakes and errors in the dates mentioned on the notice and that of the date of issue and date of service discussed in the assessment order rendered the basic foundation of the assessment erroneous and *void ab-initio*.

Further, an affixture report shows that there was no independent local person as a witness and there was no evidence that anyone identified the place as belonging to the assessee before such affixture. This led to gross violation of procedure in service of notice by way of affixture as laid down under section 282 read with rule 12, 17 and 19 of Order V of Civil Procedure Code, 1908 as the notice under section 148 of the Act was served through affixture has been witnessed by TA and Inspector of the office and not by two independent witnesses as required under the law.

It had been found to be a flagrant violation of rule 17 of Order (v) of the Code, which lays down a procedure to serve notice by affixture. Hence, it was held by the Tribunal that the requirements of the Code of Civil Procedure had not been fulfilled. Therefore, the reopening assessment completed in pursuance to the alleged notice under section 148 of the Act was held to be not valid and the assessment order was quashed as *void ab initio*. *[Mandeep Malli vs. ACIT - [2024] 162 taxmann.com 637 (Amritsar - Trib.)]*

Mere mentioning of assessee's name in panchnama of another company doesn't authorize AO to issue notice u/s 153A: HC

Assessee was a company engaged in real estate development. A search and seizure operation was conducted against another person under section 132 of the Act. While preparing the panchnama for the search operation, the assessee's name was also added and the Assessing Officer (AO) issued a notice under section 153A of the Act. Subsequently, AO concluded the assessment and raised a demand.

Aggrieved by the order, the assessee filed a writ petition before the Punjab & Haryana High Court. The High Court held that the panchnama would be a document that has to be prepared recording articles, material and objects that may be seized as incriminating documents when searching premises. Mentioning any company's name in the panchnama would only reflect that documents relating to that company were found during the search at the premises. A panchnama, therefore, cannot be treated to mean authorization issued to the authorities under Section 132 of the Act.

If any incriminating articles/documents/objects or any material relating to the assessee was recovered during the search of premises, which is found to be sufficient for reassessment by the AO, he was required to follow the procedure laid down under Section 153C.

In the instant case, the panchnama prepared at the office of another person only reflects the name of the assessee. Since it cannot be concluded that there was authorization to conduct a search against assessee under Section 132., the proceedings initiated under Section 153A, including the notice issued to the assessee, were held to be unjustified and without jurisdiction. *[Misty Meadows Private Limited vs. Union of India - [2024] 162 taxmann.com 702 (Punjab & Haryana)]*.

Mumbai ITAT adjudicates ALP determination for provision of financial guarantee and performance guarantee as well as issuance of letter of comfort; holds that issuance of letter of comfort does not constitute an international transaction

The taxpayer is engaged in civil construction, real estate, trading of construction materials and construction-related services. In AY 2014-15, the taxpayer issued a performance guarantee, financial guarantee and letter of comfort to banks on behalf of its Associated Enterprises (AEs).

During the course of Transfer Pricing (TP) proceedings, the Transfer Pricing Officer (TPO) determined the Arm's Length Price (ALP) of commission for the issuance of a letter of comfort at 0.75%, and for the provision of performance guarantee as well as a financial guarantee at 1.50%.

The taxpayer had challenged the aforesaid TP adjustments before the Commissioner of Income Tax (Appeals) [CITA(A)]. The CIT(A) partially upheld the adjustments, thereby restricting the ALP from issuing letter of comfort to 0.20% and the provision of a financial guarantee to 0.50%. CIT(A) deleted the addition for provision of performance guarantee as it had expired during the AY under consideration.

The taxpayer as well as the Department preferred to appeal against the CIT(A)'s order before the Hon'ble Tax Tribunal, wherein the bone of contention was whether or not an issuance of letter of comfort constituted an international transaction.

The taxpayer asserted that a letter of comfort did not constitute an international transaction as Explanation 'c' to Section 92B of the Act does not include letter of comfort under the definition of International Transaction and even the Safe Harbour Rules explicitly define "corporate guarantee" and exclude letter of comfort from the definition therein.

The Department's stance was that letter of comfort creates a financial liability on the taxpayer to make good any default on the part of the AE, to the extent of the taxpayer's equity holding in its AE.

The Hon'ble Mumbai ITAT held that:

- ✓ Several decisions of the Jurisdictional High Court have established that a letter of comfort provided by the taxpayer on behalf of its AE does not constitute an international transaction, hence obviating the need for determining its ALP.
- ✓ Since the performance guarantee had expired, its ALP was not to be determined, affirming the deletion of TP adjustment by the CIT(A).
- ✓ Provision of financial guarantee is an international transaction, yet neither the taxpayer nor the tax authorities had followed the methodology for determining the ALP as prescribed in the Act. The Hon'ble Mumbai ITAT remanded the matter back to the TPO for determination of ALP as per one of the prescribed methods, also stating that ALP determination of an international transaction needs to be carried out for every taxpayer for each AY and ALP determined in another case or for another AY in the taxpayer's case cannot be a detrimental factor thereto. *[Citation: Shapoorji Pallonji and Company Private Limited [TS-147-ITAT-2024(Mum)-TP]*