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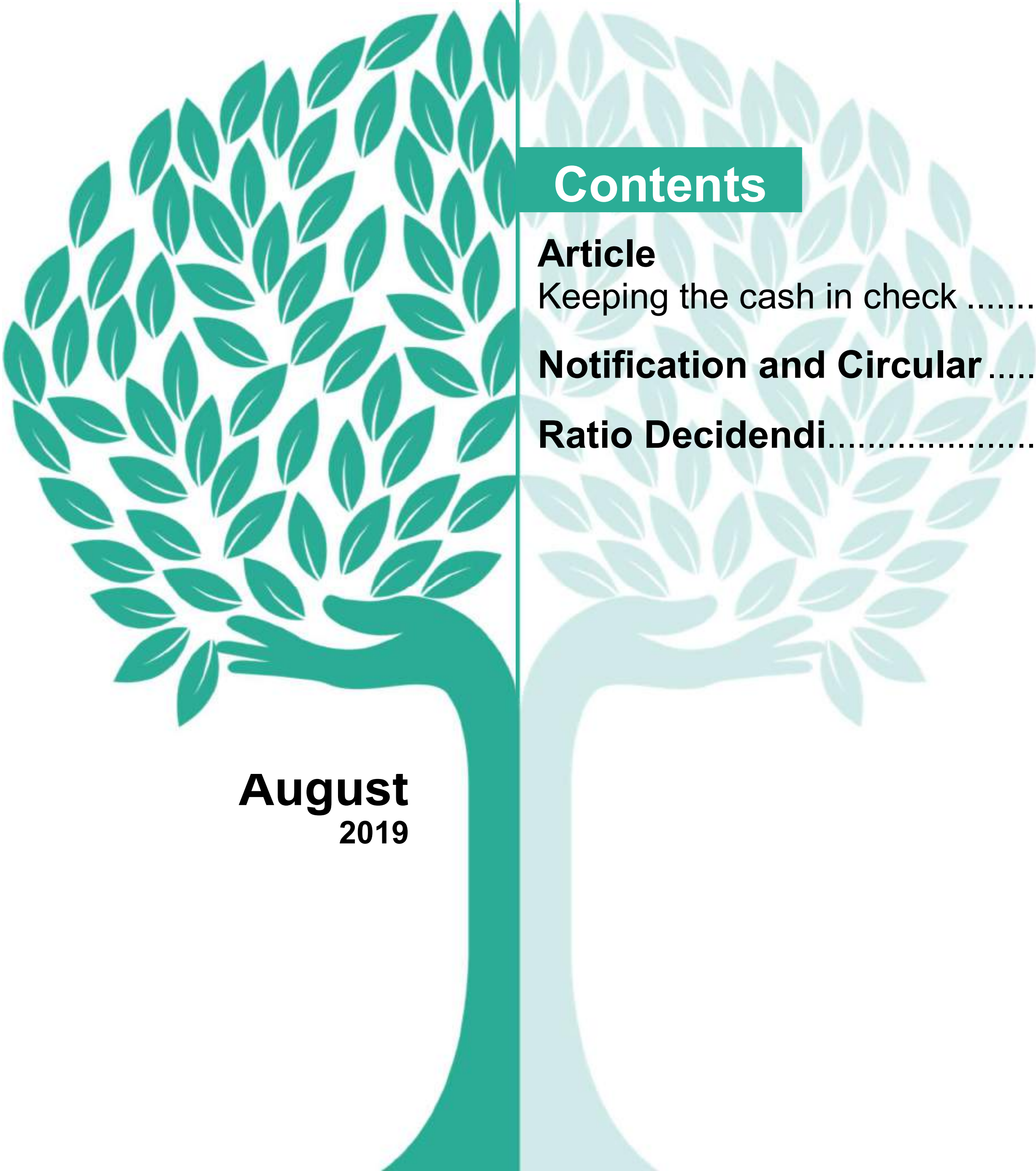

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Article

Keeping the cash in check

By **Shashank Sharma**

The Government of the present day, continuing from its previous tenure, has placed emphasis on harnessing the power of information technology in improving the governance in the country. One of the prime examples of the Government's E-Governance Policy would be the introduction of E-assessment under the provisions of the Income-tax Act, 1961 ('the Act').

Similarly, in the recently announced Budget, the Government has re-emphasized on the use of information technology for undertaking monetary transactions as opposed to cash transactions, by introducing a new section in the Act viz., Section 194N. The said section provides that a banking company, a co-operative society (in the business of banking) or a post office, shall be liable to withhold tax at the rate of 2% on withdrawal in cash, of an amount which is in excess of Rs. 1 crore in a financial year. The implication of the section would arise over any form of cash withdrawal, be it cash withdrawal from a debit card or cash withdrawal by way of a demand draft/cheque.

The measures taken by the Government via the Finance Bill, 2019, would prove to be another step in promoting a less cash economy. Earlier the Finance Act, 2017 had introduced Section 269ST, which placed a restriction on acceptance of cash equal to or more than Rs. 2 Lakh for any transaction. Therefore, by introducing Section 194N, the Government is further discouraging people from undertaking cash transactions.

However, comparison of the proposed section with the Banking Cash Transaction Tax ('BCTT') would be inappropriate as the said BCTT was introduced as a separate levy via a separate chapter in the Finance Act, therefore, acting as a separate code in itself, as opposed to being a new section in the Act. Further, the BCTT was levied on cash withdrawal, cash purchase of instruments like bank draft and on receipt of cash on maturity or otherwise of the term deposit, whereas the present section is applicable only on withdrawal of cash.

Another objective that can be attributed to the introduction of the new section is to keep a check on large cash withdrawals. The newly introduced section would thus go on to act as a deterrent to transactions in the real estate sector, where the component of cash is still quite high.

However, the Government may face resistance, as well as criticism, over the introduction of the said section from certain parts of the country where the banking system is either not fully developed, or though developed, lacks operational efficiency. As per reports, one such instance is that of the Indian Tea Association which has asked the Government to exempt it from the applicability of the said section. The reason for seeking such exemption being that there are inadequate banking facilities in the tea growing areas and accordingly, the workers are generally paid in cash.

Therefore, in this regard questions may be raised over this step of the Government in a scenario where the country has a large unorganized sector, which, perhaps, suffered a major setback from the demonetisation carried out in 2016 and is still struggling to be back on the track of recovery.

Apart from the above highlighted operational difficulties, the provision, if it were to be incorporated in the statute book in the form in which it was introduced, it would have also posed a challenge to the banks who are burdened with the task of deducting appropriate tax. This was on account of the ambiguity in the language used in the proposed section.

It is clear from a reading of the section that if a person has accounts in multiple banks, then the limit of Rs. 1 crore per annum is to be applied by each bank separately. For instance, if a person withdraws Rs.75 lakhs from one bank and Rs.60 Lakhs from the second bank, then either of the banks will not be required to withhold any tax under Section 194N. It is also quite logical because the obligation of withholding cast under the section is on the bank, which will only have access to cash withdrawals made by a person from accounts maintained with it.

What was not clear earlier was as to how this limit will be applied if a person maintains multiple accounts with the same bank. Let us say a person withdraws Rs. 75 lakhs from one account and Rs. 60 lakhs from the second account. Though the aggregate amount of cash withdrawals in a year exceeds Rs.1 crore, withdrawals from each account considered separately is still below the limit.

The use of the phrase 'an account' in the section initially introduced, suggested that the monetary limit shall apply qua each account. Therefore, going by such interpretation of the section, it shall mean that if a payee has multiple bank accounts with a single bank, then in that case the monetary limit shall be in respect of each account and not aggregate of all the bank accounts. Basis this one may have argued that adopting the above interpretation would go on to defeat the very purpose for which the section has been introduced. For instance, if a payee has 4 bank accounts with a bank, then virtually he can withdraw cash to the extent of Rs. 4 Crore in a year without attracting tax deduction.

However, the amendment vide the Finance (No. 2) Bill, clarified that the limit would apply qua the bank i.e. it will have to be seen in respect of all the bank accounts maintained by a person with a bank.

Nevertheless, question regarding the validity of the provision would still persist, as, a sum in the nature of income tax is being withheld, on the withdrawal of the money, placed in a bank which may or may not have the character of income. Also, whether the step of the Government will discourage people from bringing money in the banking stream is something which will have to be seen apart from the operational challenges that may arise.

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Notification and Circular

Quoting of Document Identification Number (DIN) in communication to assesses and others

The CBDT has issued Circular No. 19/2019, dated 14-8-2019 directing that a computer-generated Document Identification Number (DIN) will have to be mentioned in notices, assessments proceedings, investigations, verification of information, correspondence regarding exemption, penalty and so on. In exception circumstances like operational difficulty, technical problems, functionality to issue communication not being available in the system, officer being unavailable, PAN not being known, etc., such communication may be issued manually but the reason for not-mentioning of DIN must also be mentioned in the communication. Also, such communication has to be regularised within 15 days of issuance in case of technical glitches, officer's non-availability or delay in PAN migration. This direction will apply to all communications issued by the department on or after 1-10-2019. Further, the circular also directs that in case of pending assessment where notices have been issued manually, the same shall be uploaded by 31-10-2019.

Monetary limits for appeal by department

The monetary limits for filing of appeal by the department at ITAT, High Court and Supreme Court have been enhanced by CBDT Circular 17/2019, dated 8-8-2019. The CBDT has now fixed the limit as Rs. 50,00,000/- for appeal before ITAT, Rs. 1 crore for appeal before the High Court and Rs. 2 crore for appeal before the Supreme Court. The earlier Circular No.3/2018, dated 11.7.2018 has been modified to this effect. Also, it has been clarified that in case of composite orders involving more than one assessment year, appeal will be filed only for those years in which the appeal threshold is crossed.

Relief for start-ups from proceedings on account of premium received on subscription

Circular 16/2019, dated 7-8-2019 provides relief from assessment of companies as regards applicability of Section 56(2)(vii)(b) wherein start-ups which were subsequently recognised in terms of the DPIIT Notification dated 19-2-2019 were also being proceeded against by issuing notice under Section 143(2)/147 of the Income Tax Act. The Circular lays down that where a start-up has been recognised and the proceedings are only in respect of Section 56(2)(vii)(b) regarding consideration received, the contention of the recognised start-up will be summarily accepted. In case multiple issues are involved, the issue of share premium will not be pursued and other issues will be taken up after obtaining permission from the supervisory authority. Also, where a case is selected for scrutiny involving other issues besides applicability of Section 56(2)(vii)(b), it will be proceeded with only after obtaining permission from supervisory authority.

India notifies the provisions of the Multilateral Convention

India had ratified the Multilateral Convention (the convention or MLC) to Implement Tax Treaty related Measure to Prevent Base Erosion and Profit Shifting and deposited the instrument of ratification on 25-6-2019. By way of Notification No. 57/2019 dated 9-8-2019, the provisions of the convention have been notified and they will enter into force on 1-10-2019. The MLC is an endeavour by the signatory nations to address in a coordinated manner, the abuse of treaty provisions and profit shifting methods adopted by enterprises. Instead of numerous bi-lateral negotiations the countries have agreed on certain common provisions, worded in identical manner so that the existing treaties can be amended in a uniform manner and with lesser effort. As per the notification, India had listed 93 countries including Japan, France, Germany, UK, Malaysia and Singapore, with whom it has a treaty (Covered Tax Agreement or CTA) and also provided the list of reservations/ options it has chosen from the model suggested by the MTC. Some of the significant provisions are

1. ***Dual residency:*** India has adopted the position as regards dual residency that Article 4 of the MTC provides, that residence of a person other than an individual would be determined with regards to place of effective management and in the absence of agreement the person shall not be entitled to benefits under the Treaty except to the extent as agreed upon by the competent authorities of the countries.

2. ***Preamble:*** Article 6 of the MTC which sets out the intention of the nations to eliminate double taxation without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance including treaty shopping arrangements would be included in the Treaties. India has not made any reservation for non-inclusion of the Preamble.

3. ***Prevention of treaty abuse:*** Article 7 of the MTC provides that where obtaining a benefit under treaty was one of the principal purposes of any arrangement or transaction (the Principal Purpose Test) then, the benefit would not be granted unless it is proved that such benefit could be granted in accordance with the purpose and the object of the CTA. India has accepted the application of this clause as an interim measure and would endeavour to add to or replace the same with a bilaterally negotiated text. India has notified 36 CTA including the Treaty with UK in which such provisions exist.

4. ***Simplified Limitation of Benefits (SLOB) clause:*** India has opted for application of the SLOB clause which provides for extending of benefits under the CTA to 'qualified person' defined with certain conditions like active conduct of business or holding of certain percentage of beneficial interest of a qualified person. India has provided a list of 9 CTA including those with Sri Lanka and USA, which already contain similar provisions.

5. ***Artificial avoidance of PE status through commissionaire arrangements and specific activity exemptions:*** Article 12 and 13 of the MTC provide that a person acting on behalf of an enterprise habitually concluding contracts or playing the principal role leading to conclusion of contracts which are routinely concluded without material modification by the enterprise would be deemed to constitute a PE of the enterprise. This Article seeks to address the situation wherein because a person lacked the authority to conclude contracts, such person did not constitute a PE. India has notified the list of CTA including Australia, Japan, Netherlands in which such or similar clause is incorporated. Also, a person acting as an independent agent would not constitute a PE.

   Article 13 of the MTC is regarding specific exemption to certain activities which will not be deemed to constitute a permanent establishment. Activities which are preparatory or auxiliary in nature are covered under this exemption. India has chosen Option A in this Article wherein certain activities specifically listed in the CTA would not constitute a PE whether or not the exception is contingent on the activity being of a preparatory or auxiliary character, the maintenance of a fixed place solely for the purpose of carrying on these activities or a combination of these activities which are however of preparatory or auxiliary character.

6. ***Arbitration:*** India has opted to not include the provisions relating to mandatory binding arbitration to resolve issues or contentions raised by a person who considers that the provisions of the CTA have not been applied correctly.

Ratio Decidendi

Trust implementing welfare scheme of government is not engaged in charitable activity

The assessee trust was established for carrying out charitable activities and implemented various welfare schemes of the government which had been awarded to other trusts. The assessee trust received funds for the said activity from other trusts and also received consideration for the implementation. However, its registration under Section 12AA of the Income Tax Act was cancelled stating that it was not engaged in any charitable activity. The assessee argued that it did not have any profit motive and participation in welfare activities would qualify as charitable activity. The ITAT however, held that the assessee was engaged in business activity as a sub-contractor for other trusts and was not entitled to registration under Section 12AA. [*CIT v. Annadan Trust* - (2019) 307 CTR (Ker) 448]

Salary paid in advance to CEO by non-resident and reimbursed by Indian entity, is not income of non-resident

At issue was the taxability of reimbursement to the non-resident AE (assessee) of salary paid to the CEO of Indian AE. The revenue authorities claimed that the sum was taxable in the hands of the non-resident AE as Fees for Technical Services (FTS) and in terms of the India France DTAA, the assessee had made available technical skill and knowledge to the Indian AE. On analysing the provisions of the Act, the ITAT held that Explanation 2 to Section 9(1)(vii) which states that income of a recipient which is chargeable under the head income from salary would not be FTS, should be tested in the hands of the real recipient and not the literal recipient. In the instant case, the salary was received by the CEO who offered both the sums received from Indian AE as well as a portion received directly from the non-resident AE to tax as salary. On facts, the income arose on account of the employer-employee relationship between the Indian AE and the CEO. Also, in order for the sum to be taxable as FTS, the services should have been rendered by the CEO on behalf of the non-resident AE but in the fact of the case, it was rendered by the CEO in his own right. Distinguishing the ruling in *Centrica* [(2014) 364 ITR 336 (Delhi)], the ITAT stated that in order to be taxable as income, the sum must accrue to the non-resident and in the instance case, no money was received by the non-resident in its own right. Hence, the ITAT held that the sum cannot be taxable as FTS in the hands of the assessee. [*Faurecia Automotive Holding v. DCIT* - ITA 784/Pun/2015, Order dated 8-7-2019, ITAT, Pune]

Interest (notional) which is part of purchase price is business income

The assessee have offered NIL income for taxation in the return filed by the representative assessee on sale of bullion. As per the terms agreed between the assessee and its buyer in India, a Letter of Credit was issued from India and the same was discounted by the assessee at its bank in Australia. The LC charges and discounting charges were identical and hence no income was offered to tax. The revenue department contended that the notional interest charges on LC which was taxable as interest in the hands of the assessee though it admitted that the interest did not arise on account of a debt. The assessee argued that the amount did not partake the character of interest and was its business income and in order to tax the income under Article 11 of the India Australia DTAA, the revenue authorities had to establish that such income was taxable as per Indian laws. The Tribunal agreed with the assessee that where interest is part of the cost of bullion itself, the same cannot be taxed under the residual head of income from other sources. [*AGR Matthey of Western Australia v. ADIT* - ITA 1341/Del/2010, Order dated 5-8-2019, ITAT, Delhi]

Costs incurred to provide services contracted for is an expense even if reimbursed by AE

In a recent case, the assessee was a company providing marketing support services to its AE in UK. Therein, the AO made an adjustment of Rs. 26,10,163/- under Section 92CA of the Income Tax Act on the recommendation of the TPO. Against the said order, the assessee preferred an appeal before the CIT(A). However, the CIT(A) instead of providing relief to the assessee further reduced the profit margin of the assessee from 10% to 6% by including the marketing expenses incurred by the assessee on behalf of its AE to its total cost while calculating the profit level indicator. In doing so, the CIT(A) rejected the argument of the assessee that it was simply acting as a pass-through entity which was being reimbursed on a cost-to-cost basis for the third-party cost incurred by it for its AE. Aggrieved by the order of the CIT(A), the assessee preferred an appeal before the Delhi Bench of the ITAT.

The ITAT upheld the Order of the CIT(A) by observing that the Marketing Services Agreement between the assessee and its AE clearly showed that the performance of the marketing support services was the responsibility of the assessee, and the same could either be performed by the assessee itself or through some third parties. Thus, the UK AE was not dealing with the third parties through the assessee but rather the third parties were being engaged by the assessee to fulfil its contractual obligations, since it lacked the adequate manpower to do so. It also rejected the contention of the assessee that it was simply acting as a conduit and acting on behalf of its AE. [*Trip Advisor Travel India Pvt. Ltd. v.* DCIT - ITA No. 1422/Del/2017, ITAT Delhi]

Business expenditure – Allowability to be judged from mindset of assessee

Observing that the way professionals promote themselves is fast changing, ITAT, Delhi has held that scholarship provided by an assessee to the Indian students in a foreign university is a revenue expenditure allowable under Section 37(1) of the Income Tax Act. The Tribunal observed that such expenditure is to increase visibility and social status and was not capital in nature and not a gift. It also held that the assessee knows better as to what kind of expenditure he should incur for furtherance of his business and that the AO should put himself in assessees shoes and then decide as to whether the expenditure incurred by the assessee is necessary or not for the business of the assessee.

Tribunal in this regard rejected the department's view that giving scholarships to the students cannot be a factor which will lead to building the overall persona of the assessee contributing to the professional stature of the assessee. It was also held that there was a nexus between the expenditure incurred and the professional services rendered by the assessee. [*Harish Narinder Salve v. ACIT* – Order dated 13-8-2019 in ITA No. 2285 and 2392 /Del/2016, ITAT New Delhi]

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