Nangia Andersen LLP

Tax Rulings Compendium

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Section 79 of the Indian Income-tax Act, 1961 ('the Act') – Carry forward and set-off of losses

Change in shareholding of ultimate parent company, no trigger for denying set-off of brought forward losses [ITA Nos. 2939 & 2940/Del./2018]

- WSP CIL, a private limited company incorporated in India is a wholly owned subsidiary of WSP Cyprus, which is held by the ultimate holding company, WSP UK. During AY 2013-14, there was a reorganization, wherein WSP UK was made the intermediate holding company and WSP Canada, the ultimate holding company.

- Revenue disallowed set-off of brought forward losses pertaining to AY 2012-13, in AY 2013-14 & 2014-15 stating that since there has been change in the shareholding in ultimate holding company, the losses pertaining to the year before such change, could not be set-off.

- CIT(A) deleted the additions, stating that throughout, the holding company was WSP Cyprus and the change in ultimate holding company from WSP UK to WSP Canada does not affect the shareholding of the assessee.

- ITAT notes that in the year of incurrence of loss *i.e.,* AY 2012-13 and as on the date of the previous year relevant to AY 2013-14 & 2014-15, there was no change in the shareholding pattern of the assessee. Observes that WSP Cyprus being the immediate holding company continued to hold 99.9% of the shares of assessee.

- ITAT states that it is a well settled proposition that registered shareholder is to be considered the beneficial owner of shares, unless such shares are held in the capacity of a nominee/ agent/ trustee of the real owner, follows the rationale in Delhi HC ruling in Yum Restaurants.

Key takeaways: *As per the discussed ruling, in the case of multilayer group structure, the intermediate holding company or ultimate holding cannot be said to be holding shares in the company where the subsidiary of such intermediate holding company or ultimate holding is the shareholder.*

Section 50B of the Act – Computation of capital gains in case of slump sale

Transfer of technical know-how in slump sale cannot be equated to goodwill transfer [ITA No. 568/2015]

- ITAT held that the transaction is transfer of technical know-how and profit on sale of technical know- how cannot be brought to tax as capital gains u/s 45 as assessee could not substantiate the expenses incurred for its acquisition/ development, applies SC ruling in B C Srinivasa Shetty.

- ITAT also rejects revenue's attempt to equate transfer of 'Technical know-how' with 'Goodwill', remarks "the only way to bring to tax sale consideration received on transfer of "Technical know- how" is to call it "goodwill".

- HC accepts ITAT's findings that at no point of time the Revenue doubted the fact that the assessee transferred technical know-how. HC also observes that even though goodwill is a self-generated asset and therefore its costs of acquisition cannot be determined, by reason of amendment to the provisions of Sec.55(2)(a) of the Act by the Finance Act, 1987 w.e.f. 1.4.1989, the cost of acquisition of 'Goodwill' is nil and therefore it is possible to compute capital gain on transfer of goodwill. Such an approach cannot be adopted if the capital asset transferred is ''Technical know-how".

- HC also considers ITAT's consideration that if the assessee has treated the cost/ expenses relating to acquisition/ improvement/ development of intangible non-depreciable assets in the revenue field, the gains arising as a result of sale thereof will have to be necessarily treated to be in the nature of revenue either u/s 28 or u/s 56 and not as capital gains and notes that since the Revenue could not give any specific finding for taxing the said consideration, opines that in such circumstance "the finding of the assessing officer ('AO') that the transfer of know-how was transfer of goodwill is wholly unsustainable."

- As regards the non-compete fees, HC notes that the fee was payment for sharing customer database and sharing of trained employees and not attributable to transfer of any assets or right and "the mere fact that the receipt is not attributable to non-compete covenant, it cannot be automatically concluded that the receipt was either from business or income of an activity recurring in nature", relies on Bombay HC ruling in Mahindra & Mahindra.

Key takeaways: *This ruling fortifies the position taken by many taxpayers that a receipt which is arising out of transfer of a capital asset shall not be taxable where the cost cannot be ascertained, and the computation mechanism fails as laid out in SC ruling – B C Srinivasa Shetty. While the Act has been amended over the previous years to specifically consider cost as NIL under section 55(2)(a) of the Act in select cases to provide for taxability, there still exists conflicting views in cases of assets which are not covered in section 55(2)(a) of the Act.*

Section 237 r.w.s. 90(2) of the Act - Refunds

Interest on IT Refund to foreign company taxable under Article 11 of India-USA DTAA and not as business profits [ITA No. 5895/Del/2017]

- Assessee, a tax resident of USA, had received interest income on income tax refund. The AO held that the interest income received by the assessee on account of income tax refund is taxable at the maximum marginal rate of 40%, by treating it as the business income of the permanent establishment ('PE').
- Assessee contended it is entitled to benefits of the tax treaty between India and USA and hence the interest received on income-tax refund was chargeable in terms of Article 11 (Interest) of the India-USA tax treaty at the rate of 15%, as the interest income is not effectively connected with the business of the PE, basis the asset-test or activity-test.
- Delhi ITAT perused the provisions of section 90(2) of the act and ruled in favour of the Assessee, held that interest on income-tax refund is taxable at 15% under Article 11 of India-USA tax treaty and not at 40% applicable to foreign companies.

Key takeaways: *Revenue's contention that interest income is effectively connected to the PE and hence taxable as business income is overruled as refund is not effectively connected to the PE of the taxpayer and that the provisions of section 90(2) to the extent beneficial to the assessee shall be applied.*

Refund cannot be withheld on unreasonable grounds [W.P.(C) 8411/2020 & CM No.38352/2021]

- Revenue withheld refund of Rs.349 Cr. u/s. 241A on the basis that the assessee may have to bear tax liability in the range of Rs.500 Cr. as and when an assessment order is framed for AY 2018-19.

- The anticipated tax liability of Rs.500 Cr. was founded on three counts:
  - **Addition arising from ALP adjustments**
    Delhi High Court observed that addition on account of ALP adjustment cannot give rise to any tax liability as the Assessee has executed an APA in December 2019 and also refers to TPO order whereby no adverse inference is drawn in respect of ALP of assessee's international transaction.
  - **Disallowance of Marked to Market (MTM) forex losses**
    High Court observed that the revenue has not made any estimation as to what is the foreign exchange fluctuation that is likely to be disallowed and revenue has only stated the fact that MTM losses of Rs.11 Cr. were disallowed during AY 2016-17.
  - **Addition for unearned revenue**
    Revenue has estimated a likely addition of Rs.1050 Cr. High Court observed that assessee has been following a consistent accounting policy of recognizing unearned revenue in each financial year and offering it for tax as and when services are rendered and/or goods are sold.

- High Court held that the estimate made by the Revenue that there is a likelihood of assessee having to bear a tax liability of Rs.500 Cr. is not rational and on cogent grounds.

- High Court also noted that the assessee's net worth is nearly Rs.1873 Cr and opined that it is not as if the assessee does not have necessary financial wherewithal to defray the estimated tax liability, if it arises. Hence, High Court directed Revenue to issue refund to the assessee.

Key takeaways: *Tax refund cannot be denied without proper justification and when it is evident that such refund is not likely to adversely affect the revenue. In a similar case of withholding refund u/s 141A of the Act, in the case of Tata Teleservices Ltd., Delhi HC has directed revenue to refund Rs.72 Cr. along with interest or justify withholding of refund. The matter is listed for hearing on April 7, 2022.*

Divergent rulings post CBDT's Circular 3/2022 on Most Favoured Nation (MFN) clause

CBDT Circular on MFN clause transgresses Sec.90(1), neither binding on ITAT nor retrospective –[ITA No.202/PUN/2021 Pune Tribunal]

- Assessee is a company incorporated in Spain. Assessee rendered technical services to an Indian company and offered the income to tax at the rate of 10% instead of 20% rate as provided in India- Spain tax treaty pursuant to most-favored-nation (MFN) clause read with Article 12 of India-Portugal DTAA.

- AO held that the tax rate of 10% applied by the assessee under Portuguese tax treaty could not be applied because section 90(1) specifically requires the issuance of necessary Notification by the Government of India.

- ITAT took cognizance of the CBDT Circular No.3/2022 dated 03-02-2022 providing clarification and laying down certain pre-requisites for deriving the benefit of the MFN clause in the Protocol to India's tax treaties with certain countries and held that once tax treaty is notified all its integral parts, including Protocol, gets automatically notified and there remains no need to again notify the individual limbs of the tax treaty.

- Also observed that though the CBDT has mandated issuance of separate notification for import of treaty benefit, it overlooks the plain language of Section 90(1) in juxtaposition to treaty which treats MFN clause as integral part of agreement.

- ITAT also observes that the CBDT Circular is binding on the tax authority and not on the assessee or the tribunal or other appellate authorities and notwithstanding the above, Circular cannot be applied to the period prior to the date of its issuance (i.e., tax year 2015-16 in the present case) as it is detrimental to the taxpayer for taking benefit conferred by the tax treaty.

Key takeaways: *The ITAT has disregarded the circular and held that no notification needs to be issued to claim MFN clause, as the MFN clause is part of protocol which is integral to the tax treaty. Hence, there is no requirement of issuing separate or piecemeal notifications.*

The issue is pending before the Supreme Court in the case of Steria India Ltd (India- France DTAA) and Concentrix services (India- Netherlands DTAA). The judgment of the Supreme Court will put to rest the conflict on the claim of benefit provided by the MFN clause of the DTAA. While India is yet to notify any DTAA for the purpose of the MFN clause, this judgement will come as a relief to taxpayers who are currently claiming the benefit of MFN Clause.

Business support services are not taxable as FTS in view of the MFN clause under the India-Belgium tax treaty [ITA No. 1358/DEL/2015]

- Assessee, a tax resident of Belgium, has entered into an agreement with an Indian company for the provision of business support services, such as marketing, sales, finance, administration and other services. Such services were provided by the assessee from outside India.

- The AO observed that the support services provided by the assessee were both managerial & consultancy services including technical consulting services. Referring to Article 12 of the India- Belgium tax treaty, AO formed a belief that these services are taxable as FTS both under the tax treaty and under the provisions of Section 9(1)(vii) of the Income-tax Act, 1961.

- Assessee contended that the Protocol to the India - Belgium tax treaty provides for taxation of FTS in accordance with the provisions of tax treaty between India and a member of OECD entered into after 01.01.1990, where such provisions provide for a lower rate or restrictive scope of taxation on Royalties/FTS.

- The DRP upheld the order of the AO.

- The Tribunal held that the business support services are not taxable as FTS under the tax treaty applying the MFN Clause. By virtue of the MFN clause, the restricted scope *i.e.,* make available clause under the India-Portugal tax treaty, will apply to the India-Belgium tax treaty and since the services provided by the assessee did not make available technology, skill, know-how, etc., to Indian company, the same cannot be treated as FTS.

Key takeaways: *The ruling has affirmed that where a tax treaty provides a protocol for taxation of FTS in accordance with the provisions of a tax treaty between India and a member of the OECD, if such provision provides for a lower rate or restrictive scope of taxation, then such benefit can be availed.*

Section 32 of the Act - Depreciation on goodwill for assessment years prior to the Amendment brought by Finance Act 2021

Disapproves overlooking of Smifs Securities & prior year's ITAT ruling in draft order of Mylan Labs [W.P.No. 26279 of 2021]

- Revenue passed draft assessment order u/s 144C for AY 18-19 disallowing depreciation of Rs. 1,247 crores completely overlooking ITAT’s decision in assessee’s own case for AY 2014-15 and also Supreme Court’s ruling in the case of Smifs Securities.

- Assessee preferred a writ petition against the draft assessment order wherein Revenue contended that it had not accepted ITAT’s ruling and the appeal against ITAT order in assessee’s case for earlier years was pending before the HC. Thus, issue of disallowance of depreciation on goodwill had not attained finality for prior years in assessee’s own case.

- HC disposes of assessee’s writ petition holding Revenue’s approach as problematic. Clarifies that no opinion has been expressed on merits for the disallowance and DRP shall consider the objections raised by the assessee more particularly, about the ITAT ruling and SC ruling in Smifs Securities.

- Referring to section 144C of the Act, HC observes that the object behind the constitution of DRP appears to be “to ensure that the assessment proceedings are kept within the bounds of law while adhering to the principles of natural justice”.

- Remarks that Revenue's view that the ITAT order is not acceptable to the Revenue and thus the issue had not reached finality is "highly objectionable" and clarifies that unless there is a stay, decision of the jurisdictional ITAT is binding on all income tax authorities within its jurisdiction. Relies on SC ruling in Kamalakshi Finance Corporation Ltd. wherein reiterating the principles of judicial discipline, it was held that the orders of the higher appellate authorities should be followed unreservedly by the subordinate authorities. Also, remarks that if this healthy rule is not followed, the result will only be undue harassment to the assessee and chaos in administration of the tax laws.

- On distinguishing SC ruling in Smifs securities, HC opined that it is not open to the AO to try to evade from the binding effect of a Supreme Court decision by trying to find out distinguishing features.

- **Another recent ruling passed by ITAT – allows depreciation on goodwill acquired in amalgamation, follows Smifs Securities [IT(TP)A No. 2511/Bang/2019]** – Holds goodwill acquired as a capital right on amalgamation to be eligible for depreciation. Proviso to section 32 of the Act is inapplicable as it is not a case where the amalgamating company had goodwill as an asset and that goodwill arose in the hands of the assessee for the first time. Relies on SC's ruling in Smifs Securities & opines that depreciation claimed by the assessee on goodwill acquired, deserves to be allowed and directs Revenue to compute depreciation in accordance with the principles laid down in the case of Smifs Securities.

Key takeaways: *Finance Act, 2021 w.e.f. 1.04.2021 has held that goodwill will not be considered as a depreciable asset. Pursuant to this amendment, there have been cases where Revenue has denied depreciation on goodwill which arose in assessment years prior to the amendment. This ruling affirms that depreciation can be claimed on goodwill for the period prior to the amendment which is effective from AY 2021-22 only.*

Rulings pursuant to dispute in interplay of Equalization Levy ('EL') and Royalty/ FTS

In a dispute over interplay of EL & Royalty/FTS, Court direct withholding at 8% on Google's receipts as interim measure [W.P.(C) 215/2022 – Delhi HC

- The petitioner is a Singapore based company, engaged in the business of providing "cloud services" in India. The petitioner filed a writ petition challenging withholding tax certificate issued u/s 195(2) directing the Indian entity, to deduct tax @ 10% on payments made to the Assessee holding that the assessee's income will attract a withholding tax at the rate of 10% as per the India-Singapore tax treaty.

- The petitioner contested that the sale of cloud services would attract equalization levy and the foreign company has paid tax at 2% on the payment made. The petitioner argued that no withholding tax obligation on the Indian entity making the payment since once equalization levy is paid, as per the Act, there is no further liability.

- The High Court held that an Indian entity making a payment to a foreign taxpayer was permitted to withhold tax at the rate of 8% instead of 10% as provided under the applicable tax treaty because the payment was already subject to the 2% "equalization levy".

Key takeaways: *Equalization levy is leviable at 2% on sale of goods and services that take place through non-resident e-commerce operators, who do not have a business presence in India. Finance Act of 2021 clarified that the equalization levy will not apply if payments are taxable as royalties or fees for technical services in India.*

There is no clarification issued in the case of re-characterization of income by the revenue. Courts will have to decide on a case-to-case basis whether the payments will attract withholding tax or equalization levy. Sumo Logic, Mastercard Asia Pacific Pte are also litigating against alleged re-characterization of its income by the revenue.

Article 23 of the India - Singapore tax treaty

Guarantee commission is not a business income for oil drilling company; Credit of taxes withheld in Singapore can be claimed as FTC [ITA. Nos. 8154 AND 8155/Del/2019

- The assessee is engaged in the business of providing offshore drilling services to oil companies in India. It provided performance guarantee in respect of a derivative contract entered into by its joint venture partner (JV partner). Assessee received a commission for performance guarantee on which tax was deducted by the buyer.
- The AO and CIT(A) disallowed the FTC claimed by the assessee holding that the commission was not taxable in Singapore in the absence of assessee's permanent establishment (PE) in Singapore.
- The AO and CIT(A) held that the provision of performance guarantee to the JV partner was for strategic purpose in the course of business activity and since the assessee company did not have any PE in Singapore under Article 7, therefore Singapore Tax Authorities could not have withheld the tax as entire income is taxable in India. The AO and CIT (A) also referred to various other decisions of the ITAT to arrive at this conclusion.
- ITAT noted that assessee's main business was providing offshore drilling services and exploration in India and the assessee was not in the business of providing bank guarantee or performance guarantee to be taxed as a business income under Article 7 of the tax treaty. Hence, it is to be taxed as per the residuary Article 23 of the tax treaty and entitled to foreign tax credit. Moreover, as per section 12(6) of the Singapore Income Tax Act, the income in question is taxable in Singapore even if the assessee has no PE in Singapore.

Key takeaways: *A mere difference in the interpretation of a treaty provision between the source and resident country cannot result in denial of tax credit. Where taxes have been deducted in the source country treating the payments as taxable, due credit for the same need to be granted in the resident country.*

Form of subsidy is irrelevant for bifurcation into capital or revenue receipt, where incentive is provided for promotion of industries in a state

Recalls earlier order, holds sales-tax remission to Tata Chemicals not taxable; Fertilizer subsidy eligible for Sec. 80-IB deduction [ITA No. 2439/Mum/2011

- Hindustan Lever Chemicals Ltd. was amalgamated with assessee company and pursuant to amalgamation, assessee filed its revised return for AY 2003-04 where it did not claim deduction under Section 80-IB but made a disclosure for claiming the deduction at the time of assessment.
- CIT(A) upheld revenue's order disallowing the deduction of fertilizer subsidy and sales tax remission.
- ITAT in its earlier order held that the fertilizer concession received by the assessee was a part of sale proceeds which could not be excluded while working the profit under Section 80-IB and also that the sales tax remission had direct nexus with activities of the industrial undertaking, thus, restored the matter for fresh adjudication.
- ITAT, pursuant to recall of its earlier order, refers to the West Bengal Incentive Scheme, 1999 wherein the assessee opted for remission of the sales tax on finished goods over deferment of sales tax and observes that the scheme was formulated for promotion of industries in the state. Relies on SC ruling in Ponni Sugar to hold the same to be a capital receipt not chargeable to tax.
- On the matter of fertilizer subsidy, ITAT finds that the assessee produced the fertilizers under the retention pricing scheme wherein the government decided the maximum retail price and the difference between cost less maximum retail price is paid to the assessee by way of a subsidy as the manufacturers sell the fertilizers at or below the indicated maximum retail price to the farmers.
- ITAT holds that the fertilizer subsidy received by the assessee is income derived from the business of the industrial undertaking and eligible for deduction under Section 80-IB, notes that same is covered by the SC ruling in Meghalaya Steel wherein it was held that subsidies that are inseparably connected with the profitable conduct of the business are incomes derived from the business.

Key takeaways: *When an assessee is incentivized for promotion of an industry, the incentive is of capital nature, not chargeable to tax. Subsidies which are connected with the conduct of the business, shall be taxable as income derived from business (in the instant case, the assessee is eligible for deduction u/s 80IB, hence subsidy derived from business is claimed as a deduction u/s 80IB).*

Settlement award on dispute of Intellectual Property Rights (IPR) assignment is a business income where the assessee continues to exploit the IPR owned independently

Income arising on IPR assignment pursuant to settlement agreement to be taxable as 'business income' and not capital gains [ITA No.2546/Bang/2019

- Assessee Company had entered into an agreement with an entity, whereby assessee would contribute the source code of fully developed WCDMA protocol stack (background IPR/ independently owned IPR) and also jointly develop layers 2-4 of protocol stack software, for 3G standard in China (IPR).

- Pursuant to arbitration award received by assessee, the parties involved entered into a settlement agreement to put an end to disputes whereby the entity paid a sum to the assessee for assignment of joint ownership of independently owned IPR and foreground information, which was offered to tax as LTCG whereas Revenue contended that the sum is taxable as business income. CIT(A) concurred with this finding.

- ITAT held that the assessee did not receive the sum in question for giving up any source of income as the assessee was free to exploit independently owned IPR as well as foreground information and therefore rejected the argument that the sum received is capital receipt for losing a source of income.

Key takeaways: *Where assessee develops software in its course of business and becomes owner of the copyright therein, amount received on its sale is taxable as business income.*

Section 2(14) r.w.s. 2(47) of the Act – Provision relating to capital asset and transfer of a capital asset

Receipt on relinquishment of right to sue arising from arbitral award, non-taxable, under MAT & normal provisions [ITA Nos. 1535/Ahd/2018]

- The assessee entered into an agreement for purchase of land which was under a dispute and paid part consideration, but later learnt that the original owners had sold the land to a cooperative society (original purchaser).
- Assessee had filed objection before competent authority, which led to passing of an arbitral award directing the cooperative society to sell the disputed land to a third party and distribute the amount so realized between original purchaser and the assessee along with the direction for withdrawal of civil suits. Thus, assessee received a consideration for release of its right to sue which eventually was not offered to tax.
- Revenue held that it is taxable as long-term capital gain after allowing deduction towards cost of acquisition and indexation benefit and also enhanced book profits u/s 115JB (Minimum Alternate Tax provisions).
- ITAT opined that the compensation received for release of right to sue being a capital receipt is not chargeable to tax. It also observed that capital receipts are not ordinarily construed as income under rudimentary understanding of accounting and tax laws, therefore not susceptible to tax u/s 115JB.

Key takeaways: *Extinguishment of right to sue is a transfer u/s 2(47) of the Act, but the same not being a capital asset u/s 2(14) of the Act, there does not arise a transfer of a capital asset. Hence the compensation received on release of right to sue is not a taxable capital receipt. In the case of Bhojison Infrastructure Pvt. Ltd, it has been held that amount received as compensation in lieu of right to sue is not chargeable to tax as capital gains.*

Section 37 of the Act – General (Residuary section to claim a business expenditure)

Loss on account of permanent diminution in the value of an investment in a subsidiary company is allowed as a business expenditure [ITA No. 53/2021]

- Assessee claimed business loss on account of permanent diminution in the value of the investment made in the equity shares in one of the subsidiaries in the US.

- The AO disallowed the loss u/s 37 of the Act contending that the expenditure could not be considered as revenue expenditure and that it was not a case of bad debt which could be allowed u/s 36 of the Act.

- The High Court observed that the taxpayer made an investment in its subsidiary company in order to expand its business with a view to earn higher profits. The investment was thus driven by business expediency. Hence it allowed the assessee's claim of permanent diminution in the value of investment in a subsidiary as business expenditure.

Key takeaways: *Loss on diminution in the value of subsidiaries being allowed as a business expenditure has been a contentious issue in the past. In the instant case, it has been held that where investment is made in a subsidiary for the purpose of expansion of business, permanent diminution in the value of the investment shall be allowable as a deductible business expenditure. Similar view was held in the case Maneesh Pharmaceuticals Ltd, Cosmos Industries, etc. The High Court of Karnataka in the case of Ace Designers held that write-off of investment in a wholly owned subsidiary which is set up for the purposes of expansion is an allowable business loss.*

Where share premium computation lacks basis, valuation exercise is 'mechanical', stay application against demand from addition due to issuance of shares at a premium is rejected [ITA No. 120/Mum/2022]

- Although losses of the assessee increased year on year, the assessee issued shares at a huge premium. The valuation firm, which arrived at the share valuation has reserved its opinion on the fairness of the projected financial statements provided by the company.
- In less than a year, despite continued losses incurred by the company, the same valuation firm valued the shares of the company at even higher price.
- Aggrieved by the suspicion of the AO that the money has come from assessee’s fund, and also aggrieved by the action taken under the laws meant for preventing such unscrupulous transactions, assessee carried the matter to CIT(A). The assessee filed a petition, seeking blanket stay on demand during the pendency of the appeal. This petition was rejected, and the assessee was directed to pay 20% of the disputed demand.
- The matter was also rejected in the writ petition filed before the High Court.
- ITAT observed that the net present value of the discounted cash flow, varies significantly in the different certificates issued by the same firm, the entire valuation exercise is degraded to a mechanical calculation. There is no material whatsoever to show the reasonableness of the share premium received vis-à-vis the fair market value of shares and hence declined to interfere in the matter.

Key takeaways: *When the assessee and the valuation firm could not arrive at the reasonableness of the share premium received vis-à-vis the fair market value of shares, such valuation cannot be relied upon.*

Interest accrued on ZCCBs is a deductible expenditure, TDS is applicable on redemption of ZCCBs [ITA Nos.4775 & 4776/Mum/2016 Mumbai ITAT]

- Assessee, engaged in the business of application product, software development services was subjected to disallowance of deduction on account of interest payable on maturity of ZCCBs on the grounds that such expenses were not debited to the profit and loss account, but adjusted out of the share premium account. The assessee claimed the interest payable as deduction only for the purpose of computation of income, and no tax deduction at source was made in respect of the same. On appeal, the CIT(A) upheld the disallowance made by the AO.

- Assessee submitted to the ITAT that proportionate claim of premium on ZCCBs written off during the tenure of ZCCBs which is in the nature of interest is deductible, though the payment shall be made at the end of the period.

- ITAT observed that Assessee debited the amount to share premium, which is permissible under the Companies Act and holds that the interest has actually accrued on ZCCBs and treatment of interest by debiting the share premium account does not make the interest amount contingent.

- ITAT referred to the **Bombay HC ruling in S.M. Holding** and held that since no infraction of law was pointed out, and since the debit to share premium was accepted, it is clear that the Revenue accepted the interest / premium amount as accrued.

- Bombay HC ruling also referred to the **SC ruling in Madras Industrial** and Taparia Tools and holds that the liability on account of debenture redemption premium is liable to be deducted from income and cannot be treated as contingent liability.

- ITAT also relied on the **Mumbai ITAT ruling in Mahindra and Mahindra** to hold that the amount of debenture redemption premium is accrued and thus liable to be deducted.

- As regards, non-deduction of withholding tax, assessee referred to **CBDT Circular No. 4/2004, dt. May 13, 2004,** on deep discount bonds which provides that TDS has to be deducted at the point of redemption. ITAT held that the Bonds are listed on Singapore Stock Exchange and till redemption on maturity, the beneficiary of the premium is not known and absent identification of recipient, TDS deduction could not be given credit for.

Key takeaways: *The ruling brings out the principle that accounting entries are not determinative of the true nature of the transaction. The ITAT highlights that the claim in the Act has to be made as per mercantile system and consistent method of accounting and has to be in compliance with the provisions of the Companies Act.*

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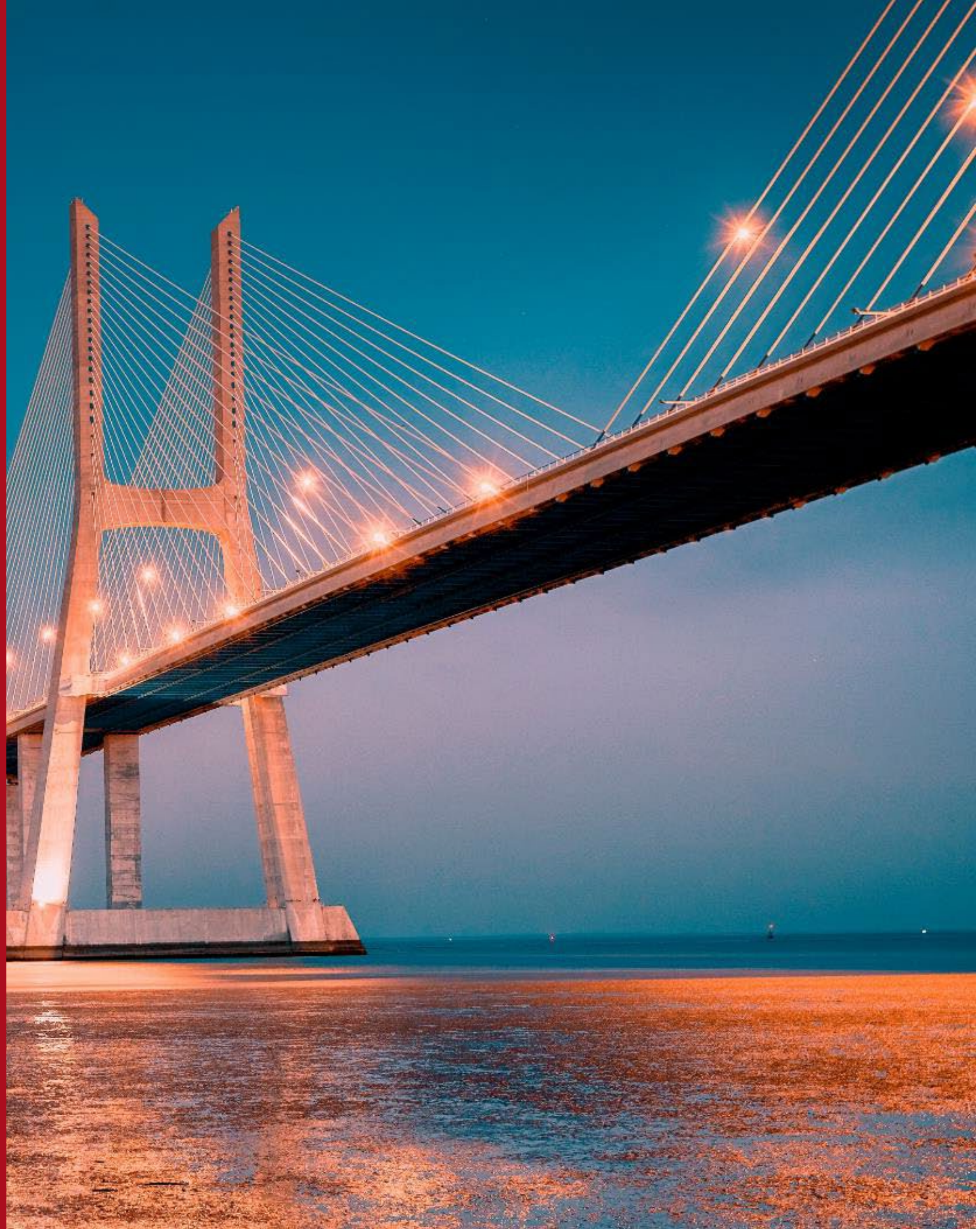

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