JUDICIAL UPDATE FOR MAY 2024 EXAMINATION

S. No.	Case Law	
1.	***Mahle Anand Filter Systems Pvt. Ltd. v. ACIT [2023] 456 ITR 29 (SC)***	
	Issue	**Analysis and decision**
	Can foregoing a security deposit to settle a dispute be considered a revenue expenditure?	When the assessee sought to vacate certain leased premises, disputes arose, and to end the dispute with the lessor, the assessee agreed not to claim the security deposit of ₹ 5.8 crores. The Apex Court affirmed the decision of the High Court which held that the amount of ₹ 5.8 crores could not be treated as revenue expenditure merely because it was paid in the course of a dispute. It is evident that the character of the amount was of a capital nature and remained so although assessee decided to forgo ₹ 5.8 crores (the security deposit).
2.	***CIT v. KBD Sugars and Distilleries Ltd. [2023] 454 ITR 800 (SC)***	
	Issue	**Relevant provision of law, analysis and decision**
	Can a resulting entity set off and carry forward the losses of the dysfunctional unit of demerged entity?	**Relevant Provision of Law:** Clause (vi) of section 2(19AA) lays down a condition that demerger in relation to companies means the transfer, pursuant to a scheme of arrangement under section 230 to 232 of the Companies Act, 2013 by a demerged company of its one or more undertakings to any resulting company in such a manner that the transfer of the undertaking is on a going concern basis. **Assessing Officer's Contentions:** The Assessing Officer contented that the assessee was ineligible to the benefit of brought forward loss under section 72A(4) for the reason that the demerged company was dysfunctional since 1999 and, therefore, does not qualify to be a 'going concern'. Since the undertaking not being a 'going concern', the condition laid down in sub-clause (vi) of section 2(19AA) for demerger stands violated. **Analysis and Decision**: The Tribunal opined that the words used 'on a going concern basis' in sub-clause (vi) of section 2 (19AA) only means that the transfer should be based on a 'going concern', and it does not mean that the undertaking being transferred should be a 'going concern' as on the date of transfer. The 'scheme of demerger', which stands approved by the High Courts and the jurisdictional Court, clearly establishes the fact that the transfer of the undertaking is indeed on a 'going concern basis'. The assets, liabilities, employees, debts, obligations, rights, etc., of the undertaking, immediately prior to the demerger, stand entirely vested with the assessee upon 'demerger'. This amounts to 'transfer of the undertaking on a going concern basis'. A simple reading of the same makes it very clear that the assessee is eligible for the benefits under section 72A(4). The Act does not state that the undertaking being demerged ought to be a going concern at the time of demerger. It only states

		that the undertaking being demerged should stand transferred in a manner similar to the manner in which a 'going concern' is transferred. Accordingly, the High Court held that if a unit were running and profitable, the same would not be available for demerger. It would be incongruous to construe sub-clause (vi) of section 2(19AA) to mean a running unit. The scheme of demerger had been approved by the High Courts. Therefore, the assessee was entitled to set off the brought forward losses under section 72A(4). The Apex Court affirmed the decision of the High Court.
3.	***Secunderabad Club v. CIT [2023] 457 ITR 263 (SC)***	
	Issue	**Facts, Analysis and decision**
	Does the principle of mutuality apply to interest income derived from fixed deposits made with the banks by the clubs if such banks are members of the club?	**Facts of the case:** The assessee-club deposited surplus funds as term deposits with various banks (who were the club members). It claimed interest earned on said deposits as exempt from income-tax applying the principle of mutuality. **Analysis:** The principle of mutuality works on the triple test, namely- (i) Complete identity between the contributors and participators; (ii) Action of the participators and contributors must be in furtherance of the mandate of the associations or the Clubs. The mandate of the Club is a question of fact that has to be determined from the Memorandum or Articles of Association, Rules of Membership, Rules of the Organization, etc., and must be construed broadly. (iii) There must be no scope for profiteering by the contributors from a fund made by them, which could only be expended or returned to themselves. Applying the above principles to the facts of the case, it was observed that in relation to transactions, namely, the deposit of surplus funds earned by the club, in banks which are members of the club, the principle of mutuality applies till the stage of deposit of funds and would lose its application, once the funds are deposited as fixed deposit in the banks. This is because the funds would be exposed to commercial banking operations, which means that the deposits could be used for lending to third parties and earning a higher interest thereon by paying a lower interest rate on the fixed deposits to the club. The bank utilising the funds of the club deposited in fixed deposit receipts for their banking business would completely rupture the "privity of mutuality", and as a result, the element of complete identity between the contributors and participators would be lost. Consequently, the first condition for the claim of mutuality is not satisfied. If the surplus fund is not applied for the common purpose of the club or towards the benefit of the members of the club directly but is invested with a third party who has the right to utilise the said funds, subject to payment of interest on it and repayment of the principal when desired by the club, then, in such an event, the club loses its control over the said funds. Furthermore, as the bank utilises the fixed deposit amounts for its banking business, the club's identity with the funds is compromised. The bank's ability to derive profits by lending the amount at a higher interest rate,

		while paying a lower rate of interest on the fixed deposit made by the club, further disrupts the essential identicality between contributors and participators in the mutual relationship. Conversely, when a club provides its facilities to members who contribute to its income, the principle of mutuality applies due to the identity between contributors and participants. However, where the same facilities are offered to non-members or the public to generate additional income, it transforms into a commercial transaction, and the principle of mutuality no longer applies. For the triple test to apply to the different and varied transactions of the club, it is necessary to lift the veil and discern the nature of each transaction: whether there is third-party intervention, which is the reason for earning the income, or it is an income generated between the members and the club, as such, i.e., only between the members of the club. When the transactions of the club are viewed in the aforesaid prism, then, in each of the transactions, whether the principle of mutuality would apply has to be discerned. **<u>Decision:</u>** Accordingly, the Supreme Court held that the interest income earned on fixed deposits made with the banks by the appellant club has to be treated like any other income from other sources within the meaning of section 2(24). Conversely, if any income is earned by the club through its assets and resources from persons who are not members of the club, such income would also not be covered under the principle of mutuality. It would be liable to be taxed under the provisions of the Income-tax Act.
4.	***CIT (International Taxation) v. Air India Ltd. [2023] 456 ITR 139 (SC)***	
	Issue	**Facts, Analysis and Decision**
	Can the provisions of section 206AA, which prescribe a higher rate of tax deduction at source in case of non-furnishing of PAN, override the Double Taxation Avoidance Agreement (DTAA) that specify a lower rate of tax?	**Facts of the case:** Assessee had taken an engine on lease under an agreement with a foreign company (lessor), a tax resident of the Netherlands, having no permanent establishment (PE) in India. The foreign company also does not have PAN in India. The assessee company deducted tax at source @10% on lease rental as per provisions contained under DTAA between India and the Netherlands. However, revenue contended that in the absence of furnishing of PAN, the assessee was under an obligation to deduct tax at a higher rate of 20% following the provisions of section 206AA. **Analysis and Decision:** The High Court noted that section 90(2) provides that the provisions of the DTAAs would override the provisions of the Act in cases where the provisions of DTAAs are more beneficial to the assessee. Even the charging sections 4 and 5 of the Act, which deal with the principle of ascertainment of total income under the Act, are also subordinate to the principle enshrined in section 90(2). Thus, in so far as the applicability of the scope/rate of taxation with respect to the impugned payments made to the non-residents is concerned, no fault can be found with the rate of taxation invoked by the assessee based on the DTAAs, which

		prescribed for a beneficial rate of taxation. The provisions of tax withholding, i.e., section 195 of the Act, would apply only to sums that are otherwise chargeable to tax under the Act. The provisions of DTAAs, along with sections 4, 5, 9, 90 & 91 of the Act, are relevant while applying the provisions of tax deduction at source. Therefore, section 206AA of the Act cannot be understood to override charging sections 4 and 5 of the Act. Accordingly, the High Court upheld the Tribunal's ruling which held that where the tax has been deducted on the strength of the beneficial provisions of DTAAs, the provisions of section 206AA cannot be invoked to insist on the tax deduction @ 20%, having regard to the overriding nature of the provisions of section 90(2). The Supreme Court upheld the decision of the High Court, resulting in the dismissal of the SLP filed by the Revenue.
5.	***CIT v. Industrial Development Bank of India Ltd. [2023] 454 ITR 811 (SC)***	
	Issue	**Relevant Provision, Analysis and Decision**
	Does the limitation period for exercising the powers under section 263 reckoned from date of passing of the original assessment order rather than the date of reassessment order for the issues covered under the original assessment but not covered in the reassessment proceedings?	**Relevant provision of law**: Section 263 provides that where the Principal Chief Commissioner, Chief Commissioner, Principal Commissioner or Commissioner of Income-tax considers that an order passed by the Assessing Officer or Transfer Pricing Officer is erroneous in so far as prejudicial to the interests of the Revenue, he may pass a revisionary order. The order for revision shall be made within a period of two years from the end of the financial year in which the order sought to be revised was passed. **Analysis:** As observed and held by the Court in the earlier decisions, once an order of assessment is re-opened, the previous order of assessment will be held to be set aside. The whole proceedings would start afresh, but the same would not mean that even when the subject matter of reassessment is distinct and different, the entire proceedings would be deemed re-opened. It means that only in a case where the issues before the Commissioner at the time of exercising powers under section 263 relate to the subject matter of reassessment would the limitation start from the date of the reassessment order. However, if the subject matter of the reassessment is distinct and different, in that case, the relevant date for the purpose of determining the period of limitation for exercising powers under section 263 would be the date of the original Assessment Order. **Decision:** Accordingly, the Supreme Court held that the issues before the Commissioner while exercising the powers under section 263 related back to the original assessment order which were not covered in the reassessment proceedings and, therefore, the limitation would start from the original assessment order and not from the reassessment order.