

IN THE INCOME TAX APPELLATE TRIBUNAL  
DELHI BENCHES: 'F', NEW DELHI

BEFORE SMT. BEENA A PILLAI, JUDICIAL MEMBER  
AND Dr. B.R.R. KUMAR, ACCOUNTANT MEMBER

ITA No. 5481/Del/2014  
AY: 2011-12

Punjab National Bank The Chief Manager-PNB HO: Finance Division 5, Sansad Marg New Delhi 110 001  PAN:AAACP0165G	vs.	The ACIT, Range-14 C.R. Building New Delhi
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**(Appellant)**

**(Respondent)**

**Appellant by :** Sh. Karan Khanna, Adv.

**Department by :** Smt. Sulekha Verma, CIT, D.R.

**Date of Hearing :** 02/01/2019

**Date of Pronouncement:** 03/01/2019

**ORDER**

**PER BEENA A PILLAI, JUDICIAL MEMBER**

Present appeal has been filed by assessee against order dated 27/07/2014 passed by Ld.CIT(A)-XVII, Delhi for Assessment Year (A.Y.) 2011-12 on following grounds of appeal:

*"1. That the order is against the law and facts of the case.*

*2. That on the facts and circumstances of the case and provisions of the law, the Ld.CIT(A) was not justified in sustaining the action of A.O. in disallowing an expenditure of Rs.17,18,46,500/-to have been made under rule 8D(iii) and Section 14A of the Act. No expenditure is attributable to exempt income. It is prayed that the additions being unwarranted be deleted.*

*3. That on the facts and circumstances of the case and provisions of the law, the Ld.CIT(A) was not justified in sustaining the action of A.O. in disallowing an expenditure of Rs.3,67,157/- on the grounds that the expenditure is of penal nature. The expenditure is a business expenditure. It is prayed that the additions being unwarranted be deleted.*

*4. That on the facts and circumstances of the case and provisions of the law, the Ld.CIT(A) was not justified in sustaining the action of A.O. in not allowing the deduction towards leave encashment of Rs.141,60,00,000/- claimed during the course of assessment proceedings. It is prayed to allow the deduction towards leave encashment.*

*5. That the above grounds of appeal are independent and without prejudice to one another.*

*Your appellant craves leave to add, alter, amend or delete any of grounds of appeal at the time of hearing."*

**2. Brief facts of the case:** Assessee filed its return of income on 30/09/11 declaring total income of Rs.57,96,13,45,146/-. Return was processed under section 143(1) of the Act and, case was selected for scrutiny. Accordingly notice under section 143(2) of the Act, along with a notice under section 142 (1) of the Act along with questionnaire was issued to assessee. In response to statutory

notices, representative of assessee appeared before Ld.AO and filed necessary details as called for.

**2.1.** Ld.AO upon verification of annual accounts observed that assessee made investments, resulting in income, which was exempt, amounting to Rs.2,66,71,13,393/- as dividend and other tax free income. Ld.AO was of the opinion that provisions of section 14 A read with Rule 8D was applicable in case of assessee. During assessment proceedings, assessee was called upon to submit as to why disallowance under section 14 A should not be made. The Ld.AO, after considering submissions of assessee was of opinion that assessee was keeping common and consolidated accounts for income earning activities. He was of the opinion that assessee was having common infrastructure and common personnel for earning income under various heads. Thus assessee was using its administrative, managerial and infrastructural setup for earning income, which does not form part of total income under the Act. He thus rejected claim of assessee regarding expenditure in relation to income which does not form part of total income, and made addition amounting to Rs.1,71,77,09,500/-.

**2.2.** Another issue observed by Ld.AO was in respect of deduction for provision of leave encashment amounting to Rs.1,24,61,00,000/-. Ld.AO was of the opinion that provision was not claimed as expenditure, as per section 43B (f) of the Act and hence assessee was not entitled to any deduction to that extent. Further a sum of Rs.3,67,157/- was disallowed as according to Ld.A.O. it was penal in nature.

3. Aggrieved by order of Ld.AO, assessee preferred appeal before Ld.CIT (A) who allowed claim of assessee under section 14 A read with Rule 8D(ii) but confirmed disallowance under Rule 8D(iii). As regards disallowance under section 36(1)(vii) of the Act, the same was confirmed by following decision of his predecessor for preceding Assessment Years.

4. Aggrieved by order of Ld. CIT (A), assessee is in appeal before us now.

5. **Ground No. 1** is general in nature therefore do not require any adjudication.

6. **Ground No. 2** relates to disallowance conformed by Ld. CIT (A) under rule 8D (iii) of Income Tax Rules, 1963.

6.1. At the outset, Ld.Counsel submitted that, this issue stands squarely covered by following observation by *Hon'ble Supreme Court* in case of *Maxopp Investments vs CIT* reported in (2018) 91 *taxman.com* 154, in favour of assessee:

*"36. There is yet another aspect which still needs to be looked into. What happens when the shares are held as 'stock-in-trade' and not as 'investment, particularly, by the banks? On this specific aspect, CBDT has issued circular No. 18/2015 dated November 02, 2015.*

*37. This Circular has already been reproduced in Para 19 above. This Circular takes note of the judgment of this Court in Nawanshahar case wherein it is held that investment made by a banking concern are part of the business or banking. Therefore, the income arises from such investment is attributable to business of banking falling under the head 'profits and gains of business and profession'. On that basis, the Circular contains the decision of the Board that no appeal would be filed on this ground by the officers of the Department and if the appeals are already filed, they should be withdrawn. A reading of this circular would make it clear that the*

issue was as to whether income by way of interest on securities shall be chargeable to income tax under the head 'income from other sources' or it is to fall under the head 'profits and gains of business and profession'. The Board, going by the decision of this Court in Nawanshahar case, clarified that it has to be treated as income falling under the head 'profits and gains of business and profession'. The Board also went to the extent of saying that this would not be limited only to co-operative societies/Banks claiming deduction under Section 80P(2)(a)(i) of the Act but would also be applicable to all banks/commercial banks, to which Banking Regulation Act, 1949 applies.

**38.** From this, Punjab and Haryana High Court pointed out that this circular carves out a distinction between 'stock-in-trade' and 'investment' and provides that if the motive behind purchase and sale of shares is to earn profit, then the same would be treated as trading profit and if the object is to derive income by way of dividend then the profit would be said to have accrued from investment. To this extent, the High Court may be correct. At the same time, we do not agree with the test of dominant intention applied by the Punjab and Haryana High Court, which we have already discarded. In that event, the question is as to on what basis those cases are to be decided where the shares of other companies are purchased by the assesseees as 'stock-in-trade' and not as 'investment' We proceed to discuss this aspect hereinafter.

**39.** In those cases, where shares are held as stock-in-trade, the main purpose is to trade in those shares and earn profits therefrom. However, we are not concerned with those profits which would naturally be treated as 'income' under the head 'profits and gains from business and profession'. What happens is that, in the process, when the shares are held as 'stock-in-trade', certain dividend is also earned, though incidentally, which is also an income. However, by virtue of Section 10 (34) of the Act, this dividend income is not to be included in the total income and is exempt from tax. This triggers the applicability of Section 14A of the Act which is based on the theory of apportionment of expenditure between taxable and non-taxable income as held in Walfort Share & Stock Brokers (P.) Ltd. case. Therefore, to that extent, depending upon the facts of each case, the

expenditure incurred in acquiring those shares will have to be apportioned.

**40.** We note from the facts in the State Bank of Patiala cases that the AO, while passing the assessment order, had already restricted the disallowance to the amount which was claimed as exempt income by applying the formula contained in Rule 8D of the Rules and holding that section 14A of the Act would be applicable. In spite of this exercise of apportionment of expenditure carried out by the AO, CIT A) disallowed the entire deduction of expenditure. That view of the CIT A) was clearly untenable and rightly set aside by the ITAT. Therefore, on facts, the Punjab and Haryana High Court has arrived at a correct conclusion by affirming the view of the ITAT, though we are not subscribing to the theory of dominant intention applied by the High Court. It is to be kept in mind that in those cases where shares are held as 'stock-in-trade', it becomes a business activity of the assessee to deal in those shares as a business proposition. Whether dividend is earned or not becomes immaterial. In fact, it would be a quirk of fate that when the investee company declared dividend, those shares are held by the assessee, though the assessee has to ultimately trade those shares by selling them to earn profits. The situation here is, therefore, different from the case like Maxopp investment Ltd. where the assessee would continue to hold those shares as it wants to retain control over the investee company. In that case, whenever dividend is declared by the investee company that would necessarily be earned by the assessee and the assessee alone. Therefore, even at the time of investing into those shares, the assessee knows that it may generate dividend income as well and as and when such dividend income is generated that would be earned by the assessee. In contrast, where the shares are held as stock-in-trade, this may not be necessarily a situation. The main purpose is to liquidate those shares whenever the share price goes up in order to earn profits. In the result, the appeals filed by the Revenue challenging the judgment of the Punjab and Haryana High Court in State Bank of Patiala also fail, though law in this respect has been clarified hereinabove."

**6.2.** On the contrary Ld.Sr.DR placed reliance upon the orders passed by authorities below and following decisions:

- Godrej and Boyce manufacturing Co Ltd vs. DCIT reported in (2017) 81 Taxmann.com 111 (SC);
- India Bulls financial services Ltd vs. DCIT reported in (2016) 76 Taxmann.com 268 (Del);
- Punjab tractors Ltd vs. CIT reported in (2017) 78 Taxmann.com 65 (P&H).

7. We have perused the submissions advanced by both sides in the light of records placed before us.

8. It is observed that decisions relied upon by Ld.Sr.DR has been passed prior to decision of *Hon'ble Supreme Court* in the case of *Maxopp Investment vs CIT (supra)*. Further *Hon'ble Supreme Court* in the case of *Maxopp Investment vs CIT (supra)*, has rendered a clear finding in respect of banking institutions which is peculiar.

Present assessee before us is also a Bank, where shares were held as stock-in-trade and therefore it becomes business activity of assessee. In our opinion specific observation *Hon'ble Supreme Court* in the case of *Maxopp Investment vs CIT (supra)*, reproduced hereinabove are squarely applicable to facts of present case. Respectfully following the view taken by *Hon'ble Supreme Court* in the case of *Maxxop Investment vs CIT (supra)*, we allow this ground raised by assessee and hold that these were not investments made by assessee in order to fall within the ambit of Rule 8D (iii) of Income tax Rules 1963.

**8.1. Accordingly the ground raised by assessee stands allowed.**

9. Ground no.3 relates to disallowance of expenditure of Rs.3,67,157/- being penal in nature.

9.1. Ld.Counsel submitted that Clause 17(e)(ii) of the Tax Audit Report read with Schedule IX indicates expenditure amounting to Rs.3,67,157/- is debited in P&L account, which is of penal nature. Vide notice u/s 142(1) of the I.T. Act, 1961 dated 26.09.2013, assessee was called upon to justify why expenditure of penal nature debited to P&L account should not be disallowed and added to total income. Admittedly the assessee did not submit any answer in this regard. Ld. A.O. thus disallowed the expenditure.

9.2. On appeal Ld.CIT(A) held as under.

*" 11. AO stated that as per the audit report the expenditure of Rs.3,67,157/- was of penal nature. No reply was submitted by the assessee to explain this expenditure which was disallowed by the AO. In my view, the payments are of penal nature and cannot be allowed as a deduction. The addition of Rs.3,67,157/- is sustained. The ground of appeal is ruled against the assessee."*

10. Before us Ld.AR could not establish by way of evidence anything contrary to the view taken by authorities below. Further, Ld.AR is also not refuting the fact that the payment is not an expenditure which was penal in nature. Under such circumstances we have no option but to uphold the view of Id.CiT9A).

**10.1.** Accordingly this ground raised by assessee stands dismissed.

**11. Ground No. 4** is in respect of claim of leave encashment claimed by assessee amounting to Rs.1,24,61,00,000/- during the year under consideration.

**11.1.** Ld.Counsel submitted that section 43B (f) of the Act do not cover any claim regarding leave encashment and therefore no disallowance could be made. He submitted that *Hon'ble Calcutta High Court* in case of *Exide Industries Ltd vs. Union of India* reported in *292 ITR 470* had struck down constitutional validity of section 43B (f) of the Act being arbitrary, unconstitutional and *de hors* the facts of decision in case of *Bharat Earth Movers* reported in *245 ITR 428*.

**11.2.** On contrary, Ld.Sr.DR placed reliance upon orders passed by authorities below and submitted that, certain deductions could be allowed, only on actual payment. He placed reliance upon decision of coordinate Bench in the case of *Nainital Almora Kshetriya Bank* in *ITA No. 4240/Del/2012, ITA No. 5234/Del/2012 and ITA No. 5312/Del/2013 for Assessment Years 2008-09, , 2009-10 and 2010-11*. Further Ld.Sr.DR submitted that decision relied upon by Ld.Counsel passed by *Hon'ble Calcutta High Court* has been stayed by *Hon'ble Supreme Court* vide order dated 08/05/09.

**12.** We have perused submissions advanced by both sides in light of records placed before us.

**12.1.** Controversy of section 43B (f) of the Act is that, *Hon'ble Calcutta High Court* held constitutional validity of section 43B (f) of the Act being arbitrary, unconstitutional and *de hors* facts of decision in case of *Bharat Earth Movers* reported in *245 ITR 428*, and that decision of *Hon'ble Calcutta High Court* has been now stayed by *Hon'ble Supreme Court* vide order dated 08/05/09. Even otherwise leave encashment is allowable on payment basis only.

**13.** We therefore direct Ld.AO to allow claim of assessee in the year in which it has been paid and to disallow in the year of provision. We accordingly set aside Ground No. 4 back to Ld.AO with a direction to disallow the claim, in the year of provision and to allow claim in the year of payment. Ld. AO is directed not to levy any interest and penalty in the year of disallowance.

**13.1. Accordingly this ground is partly allowed for statistical purposes.**

**14. In the result appeal filed assessee stands partly allowed.**

Order pronounced in the Open Court on 03/01/2019.

Sd/-

( B.R.R. KUMAR)  
ACCOUNTANT MEMBER

Sd/-

(BEENA A PILLAI)  
JUDICIAL MEMBER

Dt. 03/01/2019

\*Gmv

Copy forwarded to: -

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT

- TRUE COPY -

By Order,

**ASSISTANT REGISTRAR**  
ITAT Delhi Benches

	Date
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Date of dispatch of Order.	