

IN THE INCOME TAX APPELLATE TRIBUNAL
'B' BENCH : BANGALORE
BEFORE SHRI CHANDRA POOJARI, ACCOUNTANT MEMBER
AND
SMT. BEENA PILLAI, JUDICIAL MEMBER

ITA No.696/Bang/2018
Assessment Year : 2013-14

M/s Muneer Enterprises, Mine Owners, Upstairs, Muneer Cars, Bellary Road, Hospet-583 201.	Vs.	The Asst. Commissioner of Income-Tax, Circle-1, Bellary.
PAN - AAGFM 6500 R		
APPELLANT		RESPONDENT

Assessee by	:	Shri Shiv Prasad Reddy, ITP
Revenue by	:	Shri Priyadarshi Mishra, Addl. CIT (DR)

Date of Hearing	:	04-02-2021
Date of Pronouncement	:	09-03-2021

ORDER

PER BEENA PILLAI, JUDICIAL MEMBER

Present appeal has been filed by assessee against order dated 29/12/2017 passed by learnt CIT (A), Gulbarga for assessment year 2013-14 on following grounds of appeal:

- “1. The learned Commissioner of Income-tax(Appeals), Gulbarga is not justified in rejecting the claim for expenditure amounting to Rs.51,20,653/- being contribution to SPV a special fund created at the directions of Apex Court.*
- 2. The learned Commissioner of Income-tax(Appeals), Gulbarga is not justified in treating the expenditure towards contribution to SPV as an expenditure not allowable under explanation 1 to section 37(1) of IT Act 1961.*

3. *The Commissioner of Income-tax (Appeals), Gulbarga ought to have appreciated the fact that the very purpose of contribution is at the direction of Apex court which is solely and exclusively for the purpose of business carried on by the assessee.*

4. *The Commissioner of Income-tax (Appeals), Gulbarga ought to have appreciated with the written representations made during the course of appeal hearing, wherein a detailed write up made as to how the contribution to SPV qualifies as an expenditure allowable under explanation 1 to section 37(1) of IT Act 1961.*

5. *The learned Commissioner of Income-tax(Appeals), Gulbarga has failed to appreciate the cases relied on by the Assessing officers was clearly distinguished vide our written submission Dt. 30.12.2017.*

6. *Any other grounds that may be urged at the time of appeal may kindly be treated as grounds of appeal.”*

Brief facts of the case are as under:

2. The Assessee is a partnership firm engaged in the business of extraction, processing and manufacturing of iron ore for sale. The assessee owns mining lease No. 2339/2151 measuring 36.42 ha classified under category B. It has been stated that the only issue that arises out of the impugned order is disallowance of 15% of sale proceeds of iron ore deducted and retained by the monitoring committee towards special purpose vehicle in respect of category B mines.

3. During the year under consideration assessee debited to the P&L account sum of Rs. 51, 20, 653/-being 15% of the sale proceeds of Rs.3,41,37,680/-is under the head social welfare-government fund. The Ld. AO disallowed the said SPV deduction by observing as under:

“2.1.8. The mines operated by the Appellant-assessee are as 'B' category mines. The relevant extracts from the report of the CEC showing the categorisation of mines of the as 'B' is enclosed herewith as Annexure-A. The Appellant is listed in serial No.5 in respect of its mining lease in No.2339/2151 categorised as 'B'.

2.1.9. During the subject assessment year, the assessee-Firm had debited to P 8 L account an amount of Rs.51,20,653/-, being sae proceeds of Rs.3,41,37,688/-, under the head 'Social Welfare - Govt. Fund'. The learned AO disallowed the said SPV deduction in the impugned assessment order.

Observations of the learned AO.

2.1.10. The learned AO disallowed the said amount (10%/15% Of the sale proceeds) referring to the decision of the Hon'ble Supreme Court in WP(C) No.562 of 2009 order dated, 18-04-2013

Holding that the observations of the Hon'ble Supreme Court have clearly indicated that the amount of sale proceeds deducted & retained towards the SPV are penal in nature attracting Explanation- 1 u/s 37(1). The learned AC has also observed that the amounts in question represented income accruing to the assessee during the assessment year and accordingly there was no diversion of income overriding title. The learned AC relied on the decision of the Supreme Court in the case of CIT vs. K.C.P. Limited (SC) 421. The learned AG also placed relied on the following :

(i). C. Padmanabha Chattiyar & Sons vs. CIT182 HR 1, 5 (Mad.)

(ii). Reform Flour Mills Pvt. Ltd., vs. CIT 132 ITR 184, 196 (Cal)

(iii). CIT vs. A Krishnaswamy Mudaliar & Others 53 ITR 122 (SC).

Observations of the learned CIT(A).

2.1.11. The learned CIT(A) has dismissed the appeal holding that the amount retained was penalty in nature and as such, cannot be allowed as expenditure u/s 37(1)."

4. Aggrieved by the order of Ld. AO, assessee preferred appeal before the Ld.CIT (A).

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

6. At the outset the Ld.AR submitted that the issue of 15% of sale proceeds remitted to SPV account a stands covered by following decisions of coordinate bench of this Tribunal:

(i). M/s. Veerabhadrappa Sangappa & Co., in ITA No.1 054/Bang/2019 order dated, 08-12-2020.

(ii) M/s. Ramgad Minerals & Mining Ltd. in ITA Nos.1270 & 1271/Bang/2019 order dated, 04-11-2020)"

7. The Ld.AR submitted that a clarification was issued by the Department of mines on 08/03/2019, wherein it has been

clarified that transfer of 10% of sale value shall continue to be transferred to SPV even after conducting auction of these leases. He placed reliance on the said clarification placed at page 328-330 of paper book. It was thus submitted that it is a recurring expenditure incurred by assessee and is allowable as business expenditure.

8. On the contrary the Ld.CIT.DR placed reliance on orders passed by authorities below.

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

10. In present appeal, only issue raised for our consideration is in respect of 15% contribution made to SPV. First of all, we summarise objections of Ld.AO as in respect of SPV expenses as under:-

(a) This is one of the objections of the Ld.AO that the SPV Expenses is not allowable because it is compensation and penal in nature for contravention of law as observed by him in para 4.4 of the assessment order.

(b) Second objection of the Ld.AO is contained in para 4.7 of the assessment order and as per the same, this is the objection of Ld.AO that the said SPV is nothing but CSR Expenses only and therefore not allowable.

(c) Third objection of Ld.AO is also contained in para 4.7 of the assessment order that, said SPV is not allowable u/s 37 (1) as it

was not incurred by the assessee wholly and exclusively for the purpose of business.

11. The Ld.AO observed that, these SPV were deducted pursuant to directions of *Hon'ble Supreme Court (supra)* by order dated 18/04/2013, wherein, it was directed that, sum so paid towards SPV charges should be exhaustively and exclusively used to undertake socio economic and infrastructure development, afforestation, soil and biodiversity conservation for ensuring inclusive growth of the area surrounding mining leases.

12. The Ld.AO further observed that these payments are nothing but appropriation of profits earned by assessee that cannot be said to have incurred for purpose of business or earning profits. Accordingly, entire amount adjusted towards SPV was disallowed by the Ld.AO. The Ld.AO was of opinion that, entire sale proceeds as per E auction bid Sheets/invoices were to be assessed as trading receipts. The amount retained by CEC/monitoring committee as per directions of *Hon'ble Supreme Court*, on behalf of assessee for SPV purposes, was on account of damages and loss caused to environment due to contravention of law, and therefore cannot be allowed as deduction out of sale proceeds, even after accrual of such liability. Ld.AO was of opinion that, even in Category 'A' mines, there was marginal illegality found by CEC, because of which 10% of contribution was attributed out of sale proceeds to the SPV.

13. On careful reading of decision of *Hon'ble Supreme Court* dated 18/04/2013, it is clear that 15% contribution to SPV account was guarantee payment for implementing of R & R plan, which would be deducted from sale proceeds. This was one of the conditions for resuming mining operations under Categories 'B'.

We refer to and rely on observations by *Hon'ble Supreme Court* in case of *CIT vs Sitaldas Tirathdas reported in (1961) 41 ITR 367*. *Hon'ble Supreme Court* laying down following principal referred to various rulings that illustrated aspects of diversion of income by overriding title.

“These are the cases which have considered the problem from various angles. Some of them appear to have applied the principle correctly and some, not. But we do not propose to examine the correctness of the decisions in the light of the facts in them. In our opinion, the true test is whether the amount sought to be deducted, in truth, never reached the assessee as its income. Obligations, no doubt, there are in every case, but it is the nature of the obligation which is the decisive fact. There is a difference between an amount which a person is obliged to pay out of his income and an amount which by the nature of the obligation cannot be said to be a part of the income of the assessee. Whereby the obligation income is diverted before it reaches the assessee, it is deductible but where the income is required to be applied to discharge an obligation after such income reaches the assessee the same consequence in law does not follow. It is the first kind of payment which can truly be excused and not the second. The second payment is merely an obligation to pay another portion of one's own income which has been received and essence applied. The first is a case in which the income never reaches the assessee, who, even if he were

to collect it, does so, not as part of his income but for and on behalf of the person to whom it was payable.”

Emphasis Supplied

14. In the present facts of the case, we note that 15% of sale proceeds was payable to SPV account, after it accrued to assessee, and the fact that, assessee was obliged to part with such portion of income, by virtue of directions of *Hon'ble Supreme Court*, as a precondition to resume mining operations under Category 'B'. At this juncture we also emphasise that, but for the intervention by *Hon'ble Supreme Court*, assessee would not have contributed 15% to SPV account for implementation of reclamation and rehabilitation scheme on its own, as there was no statutory requirement to do so under relevant statutes that regulate mining activities.

15. *Hon'ble Supreme Court* has been very clear regarding the types of payments that needs to be recovered from lessee's under Category 'B', from the sale proceeds as well as otherwise. All the payments forms part of R&R plan for recouping and rehabilitating the environment. Certain payments are one time payment and some others are recurring depending upon the sale of iron ore sold in the name of each licensee or depending on the need for rehabilitation.

16. In our view contributing 15% to SPV account on account of Category 'B', would be application of income, and therefore should be considered as expenditure incurred for carrying out its

business activity. This we hold so, for the reason that, contributions determined by *Hon'ble Supreme Court* are in the nature of guarantee payment necessary for resuming mining activity. We also note that, alleged sum in these grounds are for implementation of R&R Plans in respective sanctioned lease area held by assessee, where illegal mining activities or which were used for illegal overburden dumps, roads, offices etc., beyond sanctioned lease area were carried out. Here, we also note that, *Hon'ble Supreme Court* directed CEC to refund any leftover guarantee money, after completion of implementation of R& R plan, subject to satisfaction of CEC and approval *by Hon'ble Supreme Court*. For this peculiar reason amount so contributed towards SPV being 15% of sale proceeds, under Category B, cannot be treated as penal in nature. We, therefore, reject observations of authorities below that, such sum having contributed by assessee fall within ambit of explanation to section 37 (1) of the Act.

17. The decisions relied upon by Ld. CIT (A) has also been perused by us. We note that those decisions deal with expenses which are in the nature of penalty. In the present situation, contribution towards SPV is a requirement to be incurred to carry continue its business activities. In our view, these payments in present facts do not fall within the category of penalty.

18. We note that identical issue has been considered and decided in the light of observations by *Hon'ble Supreme Court* in

case of referred by the Ld.AR mentioned herein above. For sake of convenience we reproduce the observations of this *Tribunal* in case of *Veerbhadrappa Sangappa (supra)* as under:

8.12.3. *On careful reading of decision of Hon'ble Supreme Court dated 18/04/2013, it is clear that 10%/15% contribution to SPV account was guarantee payment for implementing of R & R plan, which would be deducted from sale proceeds. This was one of the conditions for resuming mining operations under Categories 'A' and 'B' respectively. In this background, we once again refer to and rely on observations by Hon'ble Supreme Court in case of CIT vs Sitaldas Tirathdas (supra). Hon'ble Supreme Court laying down following principal referred to various rulings that illustrated aspects of diversion of income by overriding title.*

"These are the cases which have considered the problem from various angles. Some of them appear to have applied the principle correctly and some, not. But we do not propose to examine the correctness of the decisions in the light of the facts in them. In our opinion, the true test is whether the amount sought to be deducted, in truth, never reached the assessee as its income. Obligations, no doubt, there are in every case, but it is the nature of the obligation which is the decisive fact. There is a difference between an amount which a person is obliged to pay out of his income and an amount which by the nature of the obligation cannot be said to be a part of the income of the assessee. Whereby the obligation income is diverted before it reaches the assessee, it is deductible but where the income is required to be applied to discharge an obligation after such income reaches the assessee the same consequence in law does not follow. It is the first kind of payment which can truly be excused and not the second. The second payment is merely an obligation to pay another portion of one's own income which has been received and essence applied. The first is a case in which the income never reaches the assessee, who, even if he were to collect it, does so, not as part of his income but for and on behalf of the person to whom it was payable."

Emphasis Supplied

8.12.4. *Applying, thin line of difference interpreted by Hon'ble Supreme Court to present facts, we are of the opinion that, contribution to SPV account, cannot be considered to be diversion of income. This is because, we have already held while deciding ground 2.1 and 2.2 hereinabove, that entire sale proceeds accrued to assessee, and it is only due to direction of Hon'ble Supreme Court that such amount was contributed to SPV account, for which assessee was to authorise CEC/MC in relevant paragraph 11(III) refer to and relied by Ld.CIT DR.*

8.12.5. *In the present facts of the case, we note that 10%/15% of sale proceeds was payable to SPV account, after it accrued to assessee, and*

the fact that, assessee was obliged to part with such portion of income, by virtue of directions of Hon'ble Supreme Court, as a precondition to resume mining operations under Category 'A and 'B'. At this juncture we also emphasise that, but for the intervention by Hon'ble Supreme Court, assessee would not have contributed 10%/15% to SPV account for implementation of reclamation and rehabilitation scheme on its own, as there was no statutory requirement to do so under relevant statutes that regulate mining activities.

8.12.6. *In our view contributing 10%/15% to SPV account on account of Category 'A'/ 'B' respectively, would be application of income, and therefore should be considered as expenditure incurred for carrying out its business activity. This we hold so, for the reason that, contributions determined by Hon'ble Supreme Court are in the nature of guarantee payment necessary for resuming mining activity. We also note that, alleged sum in these grounds are for implementation of R&R Plans in respective sanctioned lease areas held by assessee, where illegal mining activities or which were used for illegal overburden dumps, roads, offices etc., beyond sanctioned lease area were carried out. Here, we also note that, Hon'ble Supreme Court directed CEC to refund any leftover guarantee money, after completion of implementation of R&R plan, subject to satisfaction of CEC and approval by Hon'ble Supreme Court. For this peculiar reason amount so contributed towards SPV being 10%/15% of sale proceeds, under category A/B, cannot be treated as penal in nature. We, therefore, reject observations of authorities below that, such sum having contributed by assessee do not fall within ambit of explanation to section 37 (1) of the Act.*

8.12.7. *Based on above discussions and analysis, we are of opinion that contribution to SPV being 10%/15% of sale proceeds, under category A/B, is to be allowable expenditure for year under consideration."*

19. Facts leading to the disallowance is in the present case is similar and identical to the facts in the case of Veerbhadrappa Sangappa & Co. (Supra), we note that same is the view taken by Co-ordinate Bench in case of M/s Ramgad Minerals & Mining Ltd. (Supra).

20. Respectfully following the view taken in above decisions and based on the above discussions and analysis, we are of the opinion that 15% contribution to SPV retained by the monitoring

committee on behalf of assessee deserves to be treated as business expenditure for the year under consideration.

Accordingly grounds raised by assessee stands allowed.

In the result appeal filed by assessee stands allowed.

Order pronounced in the open court on 9th March, 2021

Sd/-
(CHANDRA POOJARI)
Accountant Member
Bangalore,
Dated, the 9th March, 2021.
/Vms/

Sd/-
(BEENA PILLAI)
Judicial Member

Copy to:

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2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT, Bangalore
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By order

Assistant Registrar, ITAT, Bangalore