

**IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "H", MUMBAI**

BEFORE SHRI VIKAS AWASTHY, HON'BLE JUDICIAL MEMBER

&

SHRI S. RIFAUR RAHMAN, HON'BLE ACCOUNTANT MEMBER

ITA.NO. 120/MUM/2013 (A.Y: 2008-09)

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| Tata Chemicals Ltd 24, HomiMody Street Bombay House, Fort Mumbai- 400001 PAN: AA ACT4059M | v. | ACIT-2(3) Aayakar Bhavan M.K. Road, Mumbai- 400020 |
| (Appellant) | | (Respondent) |

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|--------------------------------------|----------|--------------------------|
| Assessee Represented by | : | Shri Nitesh Joshi |
| Department Represented by | : | Shri Rignesh Das |
| | | |
| Date of Conclusion of Hearing | : | 21.09.2023 |
| Date of Pronouncement | : | 10.11.2023 |

ORDER

PER S. RIFAUR RAHMAN (AM)

1. This appeal is filed by the assessee against the final Assessment Order and directions of the Dispute Resolution Panel – II, Mumbai [hereinafter in short "Ld.DRP"] dated 18.09.2012 for the A.Y.2008-09 passed u/s. 144C(5) of Income-tax Act, 1961 (in short "Act").

2. Assessee has raised the following grounds in its appeal: -

"1. *The learned Assessing Officer erred in adding a sum of Rs.13,54,89,235 in respect of adjustment on following account*

- a) Corporate Guarantee given on behalf of AE's Rs.11,03,74,890.*
- b) Charging of Interest to AE's Rs. 2,09,62,480.*
- c) Deputation of employees to AE's Rs. 41,51,865.*

2. *The learned Assessing Officer erred in disallowing a sum of 5.06 crores u/s 14A of the Act.*

3. *a) The learned Assessing Officer erred in disallowing a sum of Rs. 95,33,434, in respect of payments to various institutions, without appreciating the fact that similar payments have been allowed in the earlier years, by the appellate authorities.*

b) The learned Assessing Officer erred in disallowing a sum of Rs. 2,84,850 in respect of payments to club on which Fringe Benefit tax already in been paid.

4. *The learned Assessing Officer erred in disallowing a sum of Rs.11,35,31,592 paid in respect of subscription towards Brand Equity, observing the same to be non business expenditure.*

5. *The learned Assessing Officer erred in treating the Computer Up gradation expenses as Capital expenditure and thereby adding a sum of Rs.10,68,318 (net of depreciation) to the income of the assessee.*

6. *The learned Assessing Officer erred is refusing the Deduction of Loss on Foreign Exchange Fluctuation of 12.61 crores.*

7. *The learned Assessing Officer erred in disallowing the claim in respect of one fifth of the amount paid on maturity of FCCBs, amounting to Rs.22,29,068, which is claimed in line with the Supreme Court decision in case of Madras Industrial 225 ITR 802 (SC).*

8. *The learned Assessing Officer erred in disallowing the claim for deduction of machinery hire charges of Rs. 2,17,75,428.*

9. *The learned Assessing Officer erred in disallowing the deduction u/s 80(IA) at Rs.35,71,80,349 in respect of the power plant, erroneously observing as under:*

- a. *the assessee has inflated the profit from the said unit by notionally computing profits on sale of steam;*
- b. *the assessee has inflated the profit on sale of power by showing the cost of production at a rate much lower than one as per the Tariff of Gujarat Electricity Board; and*
- c. *claimed deduction u/s 80(IA) in respect of the power plant in spite of the fact that the power generated by the assessee was captively used.*

10. *The learned Assessing Officer erred in disallowing disallowance in respect of post retirement Medical benefit of 5.88 crores u/s 43B without appreciating the facts that 1.75 crores has been debited to the Profit & Loss Account and same was not disallowable U/S 43B.*

11. *The learned Assessing Officer erred in treating the interest from Subsidiaries as income from Other Sources and thereby restricting the deduction u/s 80(IA) without appreciating the facts that said interest has not been claimed for deduction U/s 80(IA)*

12. *The learning Assessing Officer erred in not allowing the deduction in respect of Scientific Research and Development.*

13. *The Learned Assessing Officers erred in treated the sales Tax exemption benefit as Revenue receipts and thereby taxing Rs.17,75,73,424 as income of the assessee.*

14. *The learned Assessing Officers erred in disallowing the sum of 1.59 crores contributed to Patterson Memorial School, Kenya without appreciating the facts that the said amount was paid to an institution which was run for the benefit of the employees of the company/(Subsidiary of the company).*

15. *The learned Assessing Officers erred in disallowing a sum of 2.53 crores in respect of Projects Written off.*

16. *The learned Assessing Officer erred in adding back the provisions for Wealth Tax and doubtful debt which computing the book profit u/ 115JB of the Act.*

17. The appellant craves the leave to add amend, alter, modify or dele any of the above grounds, before or at the time of hearing of the appeal.

3. The assessee has raised several issues in the above grounds of appeal and we shall deal with the above issues raised by the assessee ground wise.

4. With regard to ground No. 1(a) which is in respect of TP adjustment of ₹.11,03,74,890/- on account of no guarantee commission charged on the Corporate Guarantees issued in respect of the loans taken by the AEs, Homefield International Pvt. Ltd. Mauritius, (Mauritius") ("HIPL and Valley Holdings Inc USA). Brief facts relating to the ground as summarized by the Transfer Pricing Officer(TPO) and the conclusion reached are reproduced below: -

"The assessee failed to bring any material on record to prove that the concerned AE was capable of raising a loan all by itself on a standalone basis. The assessee has contended that though the AE did not have any formal credit rating, its "indicative" rating for the year was BBB-. The contention is vague and not supported by any evidence. What is the basis of BBB- rating for the AE has not been demonstrated. The assessee also failed to furnish any evidence in respect of the comparables rates at which the AE could have raised loans on standalone basis had the assessee not provided guarantee to it. It has also furnished a letter dated 12.6.2009 from SBI wherein the bank has indicated a guarantee commission @ 0.5% p.a for loans above Rs 5 Cr. However, such guarantee comes with the "hypothecation of the company's inventory and receivables in favour of the bank". The assessee has conveniently ignored this vital clause for the guarantee. In the instant case, the quote from SBI is not applicable on facts.

The rates quoted by the Allahabad Bank shows that banks and companies are charging rates up to 3% for providing the guarantees. The cost of risk undertaken is not reflected in this rate because these Guarantors secure themselves fully while furnishing the guarantees. These rates are quoted after obtaining adequate security for covering the risk involved in the guarantee. In the present case the assessee has not obtained any security from its AE. It has just provided a blanket guarantee. Therefore the Arm's Length Compensation should be much more than the rate charged by the banks for their commission. Further, the assessee failed to furnish the guarantee agreements and there is no way to find out as to what are the terms and conditions of these guarantees, and in what manner the assessee has secured itself against the risk of these guarantees.

The assessee has also contended that the information provided by Allahabad bank was in respect of the current financial year i.e FY 2011-12 and therefore the said rate of 2.4% per annum cannot be applied. The assessee's contention is factually incorrect. A photocopy of the information received from Allahabad bank was given to the assessee wherein it is clearly mentioned that the information furnished was in respect of AY 2008-09. Further, the information regarding the rates charged by Allahabad bank during AY2007-08 is also available on its website www.allahabadbank.com. Therefore, the assessee's contention is rejected.

Thus, in view of the above discussion, the assessee's contentions are rejected and the rate to be charged for guarantee commission is calculated using the following method:

CUP Approach

Under the CUP approach, the guarantee fee is quantified through a comparison of arm's length guarantee fee rates charged by unrelated third parties providing similar guarantees under similar terms and conditions (i.e. third party comparable rates). This approach identifies what guarantee fee the borrower would have been required to pay if it were to have secured the guarantee through an unrelated third party, such as a bank or a finance company. Under this approach, two variables are estimated: (i) the assets at risk, and (ii) the guarantee fee rate. To estimate an appropriate guarantee fee rate, the borrower's credit worthiness is evaluated by estimating an "implied" credit rating using credit rating guidelines published by a third party credit rating agency. An implied credit rating is a quantitatively derived estimate of an actual credit rating. The borrower's implied credit rating is used to identify comparable guarantee fees charged by third party lenders

to borrowers with similar credit ratings. This approach is most appropriate in cases where the guarantee results in a measurable and material credit enhancement for the borrower and hence lowers the cost of its third party debt. The application of a CUP could either be:

Internal Guarantee CUP

- Take into account guaranteed and un-guaranteed third-party loans.*
- Ensure that the guarantee fee is equal to the spread between the two loans.*

External Guarantee CUP:

- For example, the rates at which the financial institutions are providing guarantee to its constituents.*

In the present case, since the assessee's quote of rate from SBI was found inadequate and rejected, it was considered appropriate that external CUP be applied. In order to apply the CUP, information was gathered from Allahabad bank. The rate charged by the bank is 2.4% p.a for loans above Rs 10 Crores. On the basis of such information the show cause was issued to the assessee.

To benchmark the transaction, it may be seen that the average rate of 2.4 % p.a as calculated above charged by the banks normally includes cash or other security for the guarantee. In this case, since there is nothing on record to prove that the assessee had covered itself with enough security, this rate of 2.4% p.a must also take into account the exchange rate risk, the country specific risk and the AE risk. Therefore, a mark up is to be added to this rate. So a mark up of 0.6 % added to 2.4 % (a total rate of 3%) is held to reflect the third party arm's length rate.

The ALP of this transaction is calculated as under:

Amount of Corporate Guarantee in respect of loan taken by Valley Holdings Inc, USA (loan taken on 26.3.2008) = Rs 1471.41 Crores (as per closing value of USD on 31 march 2008)

Amount of Corporate Guarantee in respect of loan taken by Homefield Pvt Ltd, UK (loan taken on 7.9.2007) = Rs 613.20 Crores (as per closing value of USD on 30th Sept 2007)

Therefore, a rate of 3% is charged on the amount of Rs 1471.41 Crores for 5 days which is Rs 60,46,890/-.

Therefore, a rate of 3% is charged on the amount of Rs 613.20 Crores for 207 days which is Rs 10,43,28,000/-.

Therefore, ALP of the transaction = Rs. 11,03,74,890 /-

Transaction value = NIL

105% of the transaction value = NIL

95% of the transaction value = NIL

As the ALP falls outside the limit of +/- 5% of the transaction value, an adjustment of Rs. 11,03,74,890 /- (difference between Rs. 11,03,74,890 /- and NIL) is made to this international transaction.

Therefore, the quantum of adjustment made is Rs. 11,03,74,890 /-.

6. In view of the above, a total adjustment of Rs. 13,54,89,235 /- is made to the international transaction of the assessee."

5. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the submissions of the assessee Ld. DRP rejected the submission of the assessee and sustained the proposed additions made by the Transfer Pricing Officer / Assessing Officer. The observation of the Ld. DRP is reproduced below: -

"2.3.3. Directions:

We have considered the relevant facts and the submissions of the assessee and also the TPO's order. We find that with retrospective amendment to section 92B w.e.f 1.4.2002 the guarantee commission is now an international transaction and was needed to be benchmarked. However, since the assessee had not done in the benchmarking at any stage the TPO was right in adopting the CUP approach and then benchmarking the transaction. After the retrospective amendment to section 92B, the hon'ble ITAT (Hyd) bench decision in Four Soft Ltd (supra) is not

applicable. It may be mentioned that the hon'ble ITAT in a recent judgement in the case of Mahindra and Mahindra Ltd (ITA No 8597/Mum/2010 for AY 2006-07) has confirmed the adjustment on account of guarantee commission chargeable @3%. We, therefore, uphold the proposed adjustment on the issue of guarantee commission.

6. Aggrieved assessee is in appeal before us raising the above issue. At the time of hearing, Ld. AR of the assessee submitted that the Assessee had provided corporate guarantee in respect of a loan of USD 350 million taken by Valley Holdings Inc., USA for the purposes of financing acquisition of General Chemical Industrial Products Inc in the USA. The said acquisition has been made by the Assessee company through Valley Holdings Inc, as a special purpose vehicle (SPV). By providing such corporate guarantee for loan borrowed by the said company for the purposes of the said acquisition, the Assessee has saved on immediate outflow of funds, where, the interest on the said borrowing has also been borne by the associated enterprise. Valley Holdings Inc. was under an obligation to use the funds only for the purposes of the said acquisition and no other purpose. In these circumstances, the Assessee company was justified in not charging any fee for the corporate guarantee. For this purpose, reliance is placed on Tribunal's order dated 31.03.2023 in the Assessee's own case for the assessment year 2006-07 wherein, this principle has been accepted in

the context of not charging any interest on loan given by the Assessee to the associated enterprise being a SPV for the purposes of making acquisition on its behalf (see flap 24 of the Factual Paper Book - paragraphs 2 to 2.6 at pages 2 to 13 of the said Order). The said order in turn relies upon Tribunal's order in the case of Bennett Coleman & Co. Ltd. v. Dy CIT for assessment years 2009-10 and 2010-11 reported in (2021) 129 taxmann.com 398 and (2021) 129 taxmann.com 397, respectively.

7. Apart from the above, in the financial year relevant to assessment year 2006-07 the Assessee had lent an amount of USD 150 million to Homefield UK Private Limited (being a SPV in the UK) for the purposes of acquisition of Brunner Mond Group in the UK. With a view to enable them to repay back the said loan, they had raised a similar amount of funds through US Private Placement being the 6.44% Guaranteed Senior Notes. In respect of the said 6.44% Guaranteed Senior Notes the Assessee company has given a corporate guarantee. It is submitted that, in this case also, the principle referred to above would equally apply as the investment by the SPV actually represents an acquisition made by the Assessee, where, it cannot expect a fee for the corporate guarantee.

8. Alternatively, as a 100% shareholder of the aforesaid AEs, the Assessee was under an obligation to fund them for making the acquisition. Providing of corporate guarantee in respect of the amount borrowed by the said AES, should be regarded as discharging of shareholder function for which it could not have charged any fee.

9. Ld.AR of the assessee without prejudice to the above proposition, further submitted that, the Ld.TPO wrongly rejected the internal CUP i.e. the rate at which guarantee commission is paid by the Assessee to SBI. In SBI sanction letter indicating guarantee fee of 0.3% was furnished before TPO and provided (SBI sanction letter at page 383 of Transfer Pricing Paper Book). These actual guarantee transactions between SBI and assessee shall be considered as more reliable measure of arm's length guarantee fee in the facts and circumstances of assessee and its subsidiaries, as compared to general card rate data of Allahabad Bank. Thus, internal CUP shall be preferred over external general card rate instances.

10. In support of the above contentions, Ld. AR of the assessee is relied on the following Case Law: -

- i. CIT vs. M/s. Everest Kento Cylinders Ltd. [2013] 34 taxmann.com 19 (Mumbai - Trib) (Refer Para 21)*
- ii. Asian Paints Ltd vs. ACIT [(2014)149 ITD 511 (Mumbai - Trib)] (Refer Para 8)*
- iii. Reliance Industries Limited vs. ACIT [ITA No. 4475/M/2007 & Others pronounced on 13.09.2013] (Refer Para 52.12)*

11. Ld.AR of the assessee submitted that the guarantee commission shall be calculated with reference to outstanding amount of underlying loans for which the guarantee has been given by the assessee. Manugraph India Ltd. v. DCIT 3(2) [ITA No. 4761/Mum/2013 dated 25.03.2015 (Refer para 21).

12. On the other hand, Ld. DR relied on the order of the lower authorities.

13. Considered the rival submissions and material placed on record, we observe that in assessee's own case for the A.Y. 2006-07, the Coordinate Bench in ITA No. 9057/MUM/2010 dated 31.03.2023 held as under: -

"2. The ground No.1 raised by the assessee is with regard to the transfer pricing adjustment on account of low rate of interest charged on advance to M/s. Home Field International P. Ltd (Associated EnterprisesAE).

2.1. We have heard rival submissions and perused the materials available on record. Home Field International Pvt. Ltd. (HIPL) in Mauritius is a 100% subsidiary of the assessee formed with a view

to make investments globally. The assessee was bidding for acquisition of Egyptian Fertilizer Company through HIPL. With a view to fulfil the pre-bid condition of 'Proof of funds letter' from an international banker, the assessee had lent USD 110 million to HIPL to show availability of funds with them. The lending of funds was from 16.05.2005 to 26.06.2005 i.e. for a period of 41 days. Since, the bid was unsuccessful the funds were returned back. The said funds were placed by HIPL as short term fixed deposits with Barclays Bank. Interest earned by it on such deposits of USD 3,76,247 has been paid as interest to the assessee after reducing bank charges of USD 105. Accordingly, the assessee company earned interest income of USD 376247 from its AE on this special purpose lending to its AE. Apart from this, the assessee had also advanced regular loans to its AE which were benchmarked by the assessee by applying LIBOR + 200 basis points as the ALP rate. This was accepted by the Id. TPO to be at arm's length. The mistake which the assessee committed was including this special purpose loan given to AE during the year in the sum of USD 110 million also in the list of total loans given to the AE and had erroneously stated in form 3CEB that all the loans to AE have been benchmarked by applying interest rate of LIBOR + 200 basis points. Though this is a disclosure error in Form No.3CEB, the fact on record clearly proves that assessee has not received interest @LIBOR + 200 basis points on the special purpose lending of USD 110 million from its AE. The fact is assessee has actually received interest at an average interest rate of 3% from its AE. We also find from page 193 of the paper book that assessee had maintained an account with State Bank of India in Bahamas where it had held foreign currency to the tune of USD 110127098.13. These funds were raised by the assessee through issue of Foreign Currency Convertible Bonds (FCCB). In other words, the monies raised by the assessee through issue of FCCB were lying in the bank account of State Bank of India in the name of the assessee at Bahamas. This FCCB funds lying in State Bank of India was fetching interest to the assessee @3% per annum. Those funds were lent to its AE as a special purpose loan to the tune of USD 110 million during the year on 16/05/2005. As stated supra, since the bid participation was unsuccessful, the funds were returned back by AE to the assessee on 26/06/2005 and the monies received in USD were again credited in the same bank account maintained by the assessee with State Bank of India Bahamas on 28/06/2005 in the sum of USD 110376142.02. The evidence in this regard is enclosed in pages 193-196 of the paper book. Out of the total sum credited in the bank account maintained with State Bank of India in the sum of USD 110376142.02, a sum of USD 110 million represent receipt of principal portion of the loan and interest of USD 3,76,247 after reducing bank charges of USD 105.

2.2 *The monies received from the assessee by the AE was parked by the AE with Barclays bank in the form of short term deposits at Mauritius. The monies were lying with bank account at Mauritius in the name of AE for a period of 41 days and it had fetched interest of USD 376247.02. Since the bid was unsuccessful on 28/06/2005, the AE withdrew the amount in the sum of 110376247.02 on 28/06/2005 and returned the money to the assessee on the very same day. This goes to prove that the AE had actually received interest @3% on the funds parked by it with Barclays bank. The very same interest amount of USD 376247.02 had been returned to the assessee company by the AE without retaining any margin thereon. This peculiar fact itself goes to prove that the fund that was given to AE was not at the disposal of the AE to be utilised for any other purpose, rather it was used for special purpose funding to participate in the bid, for which purpose the funds were placed in the form of short term deposits with Barclays bank. Hence, this peculiar fact distinguishes this special purpose loan transaction given to AE in the sum of USD 110 million with regular loans given by the assessee to its AE. Accordingly, the assessee had bifurcated this special purpose loan which had fetched interest @3% with the regular loan transactions which had fetched interest @LIBOR +200 basis points.*

2.3 *The Id. TPO observed that since the assessee had included this USD 110 million in Form 3CEB along with all other loans by stating that it had benchmarked at LIBOR + 200 basis points, the Id. TPO concluded that the interest rate at LIBOR + 200 basis points becomes a CUP available with the assessee and accordingly determined the ALP of the international transaction of lending of USD 110 million also by applying LIBOR + 200 basis points and made the transfer pricing adjustment.*

2.4 *As stated earlier, the lending of USD 110 million is to be considered separate and distinct from the regular loan given to the AE. In our considered opinion, considering the purpose for which this USD 110 million was given to its AE by the assessee and also considering the fact that the AE could not utilise the monies received from the assessee for any other purpose other than for the purpose of participation in the bid, we have no hesitation to hold that this lending of USD 110 million should be construed as a special purpose lending and accordingly to be treated as separate and distinct from loan simplicitor. We find that similar issue had come up for adjudication of this Tribunal in the case of Bennett Coleman And Co. Ltd vs. DCIT reported in 129 taxmann.com 398 (Mumbai Trib). The issue in dispute and the facts in the aforesaid case are as under:-*

2. *The core issue requiring our adjudication, in this case, is whether an interestfree debt funding of an overseas company in the nature of a special purpose vehicle (SPV), with a corresponding obligation to use it for the purpose of acquisition of a target company abroad, can be compared with a loan simpliciter, and be, subjected to an arm's length price adjustment, on the basis of Comparable Uncontrolled Price (CUP) method accordingly,. The issue in dispute is an ALP adjustment of Rs. 44.26 crores on account of notional interest on a loan stated to be of this nature by the assessee company to its fully owned foreign subsidiary, which is used as an SPV for overseas acquisitions.*

3. *To adjudicate on this issue, a few material facts, as discernible from material on record, need to be stated. The assessee before us is a company now merged in Bennett Coleman & Co. Ltd., the flagship company of a well-known Indian media group- commonly known as 'Times Group'. At the relevant point of time, the assessee company, then known as Times Infotainment Media Ltd (TIML-India, in short), was a fully owned subsidiary of Bennett Coleman & Co Ltd and was engaged, inter alia, in the radio broadcasting business. When the Times Group decided to expand its wings in the radio broadcasting business and acquire overseas companies engaged in this line of business, as is stated, it was considered commercially expedient to make these investments through the assessee company. A public listed company in the United Kingdom, by the name of Scottish Media Group plc (SMG-UK, in short), wanted to disinvest in its radio broadcasting business, and that is the reason it put to auction its entire shareholding in Virgin Radio Holdings Limited, UK, (Virgin Radio, in short) which was held through SMG's wholly-owned subsidiary Ginger Media Group Ltd, UK. (Ginger-UK, in short). TIML-India was one of the successful bidders in this auction. The assessee was then invited to participate in the 'final proposal' phase of this disinvestment deal. A final proposal dated 19th March 2008 was submitted by the TIML-India. This offer, at point no. 5, specifically stated, under title 'Identity of the shareholders (with immediate and ultimate ownership)' that the purchasing company will be "an SPV formed specifically for the purpose of acquiring Virgin Radio", which is "100% owned by TIML" and that "the immediate and ultimate shareholder of TIML is Bennett Coleman & Co Ltd". In point no. 6, it was further stated that "the transaction will be 100%*

equity financed from internal resources of TIML/BCCL" and that "no further financing is required given the size of this transaction relative to the TIML/BCCL group". What followed is an exclusivity agreement dated 3rd April 2008 with respect to possible sale by Ginger Media Group Ltd, one of SMG plc's wholly-owned subsidiaries to TIML-India "the entire share capital of Virgin Radio Holdings Ltd", which ultimately culminated in, on 30th May 2008, a sale agreement was entered into between Ginger UK, SMG-UK, TIML-India and a company by the name of TML Golden Square Ltd, UK (TIML Golden, in short). The TIML Golden was thus evidently the SPV (special purpose vehicle company) for the purpose of acquiring Virgin Radio. TIML was initially incorporated by a third party, Huntsmoor Nominees Limited, with a paid-up capital of £1, on 22nd May 2008, and it was subsequently acquired by TIML, on 30th May 2008, by purchasing the £ 1 share. Subsequently, one more UK based SPV came into the picture as the assessee acquired another TIML Global Limited (TIML Global, in short), a company incorporated with a £ 1 paid-up capital by Huntsmoor Nominees Limited, on 13th June 2008. This company was acquired by TIML-India, by purchased the £ 1 share on 16th June 2008. On acquisition of TIML Global, and with a view to make TIML Golden a step down subsidiary, the only £ 1 share of TIML Golden, which was held by TIML-India, was transferred to TIML Global. TIML Golden and TIML Global, at this point of time, were typical £ 1 companies without substance- which were to be used special purpose vehicles for the acquisition of Virgin Radios. This transaction also took place on 16th June 2008 itself. As a result of these transactions, TIML Golden became a wholly-owned subsidiary of TIML Global, TIML Global became a wholly-owned subsidiary of TIML, and, TIML anyway was already a wholly-owned subsidiary of BCCL. With this structure in place and the deal having been finalized, the flow of funds started to complete the transaction. TIML received Rs. 388.85 crores as interest-free deposits from its holding company, i.e. BCCL, and Rs. 100 crores as a subscription for 1% non-cumulative preference shares. TIML-India then remitted UK £ 56,824,316 (UK £ 1.2 million for equity, and balance UK £ 55.824 million as an interest-free loan to TIML-Global on 27th June 2008. Once this amount of UK £ 56.82 million was received by TIML-Global, it paid UK £ 53.51 million, on that day itself, on behalf of TIML-Golden, for the acquisition of Virgin Radio shares, and the balance amount of TIML-Golden for other acquisition-related

costs. The acquisition of shares in Virgin Radios by TIML-Golden was completed on 30th June 2008. A further payment of UK £ 3,75,000, as an interest-free loan, was made by TIML India to TIML Global for the working capital costs. It was in this backdrop that form 3CEB filed by the assessee company disclosed the following transaction with its AE: "Amount remitted Rs. 477,10,41,750".

2.4.1. The findings of the Tribunal are as under:-

6. We have heard the rival contentions at considerable length, perused the material on record and duly considered facts of the case in the light of the applicable legal position. The basic plea of the assessee, on which we are deciding this appeal, is the limited scope of application of the CUP method, and whether any commercial interest can be attributed, as an ALP adjustment, to such interest-free debt funding on the peculiar facts of this case. There have been considerable arguments on judicial precedents on the broad proposition that there can not be any arm's length price adjustments, under the transfer pricing legislation, on the interest-free debt funding to the SPVs, but, for the reasons we will set out in a short while, it is not really required to deal with that aspect of the matter. Learned counsel for the assessee has highlighted the peculiar nature of this transaction, emphasized that no interest can be attributed to such funding, particularly when the funds advanced are to be used only in the manner specified and in furtherance of the commercial interests of the assessee rather than the SPV, and submitted that, in any case, it could not be compared with loans simpliciter - as has been done by the authorities below. He has painstakingly taken us through the orders of the authorities below, including the Transfer Pricing Officer and the Dispute Resolution Panel, and made an effort to demonstrate glaring fallacies in the application of CUP method. He has also taken us through a large number of judicial precedents, but then, as we are deciding the matter on the first principles, and none of the judicial precedents come in the way of that exercise, we see no need to deal with all these judicial precedents at this stage. Learned Departmental Representative's basic argument has been that since such funding of SPV is required to be treated as an international transaction, it is required to be benchmarked anyway. On the question of application of CUP on the facts of this case, his plea

has been that since the funding is admittedly in the nature of, and described in the books of accounts, as a loan, the interest imputation is inevitable. When learned Departmental Representative was confronted with, what appeared to us, infirmities in the application of CUP method, it was his submission that even if there are some shortcomings in the determination of the arm's length price, though he maintains that there are no such infirmities in substance, the matter may be remitted at the assessment stage for fresh adjudication on the determination of arm's length price. He fairly submits that if Indian PLR is not good enough as a benchmark for this loan, in all fairness, at least LIBOR is a good enough benchmarking tool for GBP denominated loan. Learned counsel reiterates his submissions, submits that this transaction is shown as a loan in the books of accounts as that is the only way in which it can shown, under the legal requirements, but then nothing really turns on how the transaction is treated for accounting purposes. Learned counsel for the assessee has vehemently opposed this suggestion and submitted that what is before this Tribunal is an adjudication on the arm's length price adjustment made and confirmed by the authorities below; if this arm's length price adjustment is incorrect, the Tribunal has to delete the same. As for what other remedies are available to the authorities below to correct their mistakes, it is not for the Tribunal to do anything parallel or to override the same. He thus reminds us, in his inimitable subtle way, of our role as a neutral forum and our limitation of not being able to supplement or improve the case of the Assessing Officer and the Transfer Pricing Officer. In addition to these arguments, many other facets of the matter have been argued before us, but then, in our considered view, it is not really necessary to deal with those facets.

7. On a conceptual note, the determination of arm's length price is essentially an effort to neutralize the impact of intra- AE relationship in a transaction between two associated enterprises as also the impact of controlled conditions in such a transaction. In other words, the entire ALP ascertainment exercise is to determine if a hypothetical or real but same or materially similar transaction was to take place between two independent enterprises in uncontrolled conditions, whether such a hypothetical transaction would have been any different vis-à-vis the subject transaction entered

into two associated enterprises, and, if so, to quantify the impact of such variations.

While section 92(1) that any income arising from an international transaction, which essentially refers to the transactions with associated enterprises- under section 92B, shall be computed "having regard to the arm's length price", section 92 F (ii) provides that "arm's length price means a price which is applied or proposed to be applied in a transaction between persons other than associated enterprises, in uncontrolled conditions". It could thus be a historical price, which is applied in a transaction in the uncontrolled transaction, or a hypothetical price "proposed" to be applied in a transaction which is yet to take place or a transaction which is purely hypothetical, or even an entirely imaginary, formulabased, price- as is inherent in the scheme of the computation of ALP by methods permitted under section 92C- which includes indirect methods as well. We will come back to this aspect a little later.

9.

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12. It is important to understand the true nature of this transaction because everything hinges on what is the true nature of the transaction in question. The transaction is a remittance of Rs. 477.10 crores to a wholly-owned subsidiary for making further payment of the cost of acquisition of a target company in the name of a step-down subsidiary which is fully owned by this fully owned subsidiary of the assessee company. Let us not forget the fact that the assessee company was one of the successful bidders in the purchase of the entire equity capital of Virgin Radios, which was held by Ginger Group plc UK- a wholly-owned subsidiary of the Scottish Media Group plc. Upon carrying the due diligence, and completion of other prerequisite steps, the assessee makes a final proposal, on 10th March 2008, with respect to the acquisition of Virgin Radios from Ginger Group plc UK, when TIML Global UK was not even in existence. TIML Global, the AE to which the remittance in question is made, was incorporated on 13th June 2008 in the UK and acquired by the assessee on 18th June 2008. Yet this final offer states that an SPV is formed especially for

the purpose of acquiring Virgin Radios, and this SPV will be entirely funded from internal resources of the assessee company and its Indian parent company. Clearly, therefore, the agreement to acquire the Virgin Radios was reached much before the AE in question, i.e. TIML-Global, even came into existence, and the AE in question, i.e. TIML-Global, was used as a medium to acquire Virgin Radios. It is not thus a loan simpliciter to TIMLGlobal, but it is in the nature of an advance to TIML-Global with a corresponding obligation to use the funds advanced in the manner specified. The entire funds so remitted to the TIML-Global UK were spent by TIML-Global UK on the acquisition of Virgin Radios UK for TIML-Golden UK, a step-down subsidiary, and this end-use of funds remitted was essentially an integral part of the entire transaction. The role of the assessee company, though technically described as 'purchaser's guarantor in the agreement dated 30th May 2008, is so foundational and critical that the said agreement, in paragraph 22.1, states that "In consideration of the seller entering into this agreement, ...(the TIML-India), as primary obligor and not merely as surety, unconditionally and irrevocably guarantees to the seller the proper and punctual performance of the purchaser's obligations under this agreement and the transaction documents, including, without limitation, due and punctual payment of any sum which the purchaser is liable to pay". The assessee company is into the radio broadcasting business, and, much before even the AE came into existence, the assessee company had bid for, and successfully bid for, the target company, which was eventually acquired by its wholly-owned step-down subsidiary. The acquisition of the target company was thus at the instance of, in furtherance of business interests of the assessee company, and structured by the assessee company. The remittance of funds to TIML-Global was for this limited and controlled purpose, and sequence events and the material on record unambiguously confirm this factual situation- and that is not even called into question by the revenue authorities. The transaction of remittance to TIML-Global cannot, therefore, be considered on a standalone basis and can only be viewed in conjunction with the restricted use of these funds, for the strictly limited purposes, by the TIML-Global.

13.If at all, therefore, this transaction can be compared with any other transaction, such other transaction can only be for the purpose of making remittance to an

independent enterprise with the corresponding obligation to use the funds so remitted for acquiring a target company already selected by, and on the terms already finalized by, the entity remitting the funds. The essence of the transaction is a targeted acquisition and providing enabling funds for that purpose. Such a transaction, in our humble understanding, cannot be equated with providing funds to another enterprise as a loan simpliciter, on a commercial basis, which essentially implies that such a borrower can use the funds so received in such manner, even if subject to broad guidelines for purpose test, in furtherance of borrower's business interests. Ironically, however, that is precisely what the Transfer Pricing Officer has done and has been approved by the Dispute Resolution Panel as well.

14. It is also an admitted position that TIML-Global is a special purpose vehicle. A special purpose vehicle, or SPV as it is commonly called, is an entity that is set up for a special purpose or a special project. SPVs are often used by the promoters of a project or business to isolate the financial or legal risk associated with the project or activity for which the SPV was set up or because sometimes the activity or project in question requires an entity registered in a specific jurisdiction or specific jurisdictions. The business structuring through SPVs, particularly SPVs structured abroad, could be warranted on account of a variety of commercial and legal considerations, ranging from the comfort level of the outside parties dealing with entities incorporated in certain jurisdictions to the legal framework within which such entities operate, as also to cushion owners of these structures from financial, commercial or legal risk exposures emanating from the transactions that are undertaken through these SPVs. These SPVs are typical, to use transfer pricing terminology, "capital-rich low function entity".

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18. There are three fundamental questions that arise in this context- first, whether there can be such a funding transaction between the parties which are not associated enterprises, or, to put it differently, whether there can be

valid comparables, under the CUP method, for such a transaction of SPV funding; second, whether if such a transaction is hypothetically possible, what could be the rate of interest in such financing is done in an uncontrolled situation; and, third- if interest is not the arm's length consideration for such funding, what could constitute an arm's length price of such financing.

19. As for the first question, the answer is obvious. Once we have held that transactions between the owner of SPV and the SPV belong to a genus different from the transactions between lenders and borrowers, such transactions between an SPV and the entity creating such an SPV, as long as it is for a specific transaction structured by the owner entity- as in this case, is inherently incapable of taking place between independent enterprise. The moment this kind of funding is done, the relationship between the entity funding the SPV and the SPV will be rendered as of 'associated enterprise' within the meanings of Section 92A(1) as also 92A(2). It is also elementary that the transactions between associated enterprises, even if held to be arm's length in character, cease to be valid comparable under the CUP method. Such a controlled end use of the monies is possible when the lender has functional control over the borrower, and that very control vitiates the arm's length situation. Section 92F(ii), as we have noted earlier, defines arm's length price as a real or hypothetical price in the same or materially similar transaction "between persons other than associated enterprises, in uncontrolled conditions". In the first place, an enterprise and its SPV are inherently associated enterprises. The definition of 'associated enterprises' under section 92A(1) covers "an enterprise which participates, directly or through one or more intermediaries, in the management or control or capital of the other enterprise". An SPV is entirely managed, entirely controlled and entirely owned by the enterprise which sets up the SPV. So far as section 92A(2) is concerned, SPVs are covered by more than one clause as the entire voting power (clause a) and entire share capital (clause b) of the SPV is held by the owner of that SPV, but loan advanced, if the remittance is to be treated as a loan to the SPV, by the owner of the SPV is clearly more than 50% of the book value of the assets owned by the SPV (clause c) at each stage. That is one thing. The other aspect of the matter is that not only the transaction has to be between independent enterprises but also in uncontrolled conditions. When a strict condition about

end-use, and that too end-use being decided by the owner of the SPV so much in advance that the SPV was not even in existence when the end-use decision was taken, is an inherent part of the transaction of funds being remitted, this is anything but an uncontrolled condition. Viewed thus, there could indeed be a valid school of thought that the requirement of arm's length standards can, therefore, never be met, under the CUP method, so far as the nature of the present transaction is concerned.

20. As for the second question, even if one proceeds on the basis that one can assume or hypothesize a transaction similar to SPV funding in a non-AE relationship situation and fiduciary in nature- and such a hypothesis may also have some merits, it is important to bear in mind the fact that interest is compensation for the time value of money in the sense that when lender puts the money at the disposal of the borrower for a certain period, the interest that the borrower pays the lender is compensation for placing the money at the disposal of the borrower for borrower's use during this period. In a situation in which a borrower has sufficient opportunities to gainfully use the funds so placed at his disposal, and the gains from such use are high, interest rates are also high, and when there are no gains from such funds placed at the borrower's disposal, or when the gains from such funds are low or minimal, the interest rate also correspondingly travel south. In a situation, therefore, when the borrower has no discretion of using the funds gainfully, the commercial interest rates do not come into play at all.

21. That brings us to the third question, academic as it may sound at this stage, as to what, hypothetically speaking, could be a reasonable compensation under the CUP method, in an arm's length situation or, to borrow the terminology used in rule 10B(1)(a), 'comparable uncontrolled transaction', for making remittance to another corporate entity, even a special purpose vehicle, when the remitter decides the end-use of these funds in the strictest possible manner. Let us assume, for this analysis, that there is no intra-AE relationship between the two entities (i.e. Indian entity and the overseas entity set up for a particular purpose or project), and these entities are independent of each other. In our humble understanding, when the overseas entity is, from a commercial perspective, a de facto non-entity and it has

come into legal existence only for the furtherance of the interests of the company providing the wherewithal, all the gains that such an overseas entity belongs to the Indian company. The SPV in such a situation is no more than a conduit entity. In an arm's length situation, when an SPV is created for some specific project or purpose, therefore, the net gains of that project or purpose must go to the person(s) sponsoring the SPV. The next logical question then would be as to how does this principle translate into actionable reality. We find inputs from transfer pricing legislation in a developing economy in the African continent. Rule 8(1) of the Nigerian Income-tax (Transfer Pricing) Regulations 2018, which we have referred to and reproduced earlier in this order, throws important light on this aspect. What this rule holds, in plain words, is that an SPV, which does not control the financial risks associated with its funding activities, shall not be allocated the profits associated with those risks, and the profits or losses associated with such risks would be allocated to the owner(s) of the SPV. This approach addresses the dichotomy in the SPV structure business model in the sense that while risks of an SPV investment are assumed by the owner(s) of the SPV, all the rewards, in whatever form, go to the SPV itself, by removing the gap, or ectopia in tax law, between the assumption of risks and the taxation of rewards thereof. It proceeds on the hypothesis that in an arm's length situation, the risks and rewards for the risks go hand in hand, and when someone assumes particular risks, the rewards for that risk cannot be assigned to someone else. The hypothesis underlying such an approach appeals to us, and, in our humble understanding, perhaps it truly reflects the arm's length compensation for the role played by the owner of the SPV in providing all the requisite wherewithal to the SPV to achieve its objectives. Therefore, when the CUP method is to be adopted for ascertaining arm's length price of providing wherewithal to the SPV, for achieving its objectives and purpose, the arm's length consideration thereof could at best be the corresponding gain to the SPV concerned- whether directly or indirectly.

22. To sum up, there cannot be a transaction, between the independent enterprises, of interest-free debt funding of an overseas SPV by its sponsorer; if such a transaction between independent enterprises is at all hypothetically possible, the arm's length interest on such funding will be 'nil'; and, if there has to be an arm's length consideration under the CUP method, other than interest, for such

funding, it has to be net effective gains- direct and indirect, attributable to the risks assumed by the sponsorer of the SPV, to the SPV in question.

So far as the arm's length consideration for SPV funding, for consideration other than interest is concerned, it is academic in the present case because the entire case of the revenue proceeds on the basis that interest was leviable on this funding, and benchmarking the same on CUP basis. In any event, that aspect of the matter would be wholly academic because, in the present case, the consolidated financial statements of the TIML-Global, which takes into account the financial affairs of its step-down subsidiary TIML-Golden as well, reflect a loss figure. In other words, there is no economic gain to the SPV in the relevant financial period, and, therefore, even going by this theory, the arm's length price of providing funds to the SPV, under the CUP method, would be 'nil'. Except for this arm's length price imputation- if all it can be so imputed under the CUP method, no amount of commercial interest, as in a borrowing simpliciter- whether LIBOR based or PLR based, can be attributed to the funding to the SPVs. The action of the authorities below on this point, thus, is unsustainable in law. Ground Nos 2 to 9 are thus allowed in the terms indicated above.

2.5 The only distinguishing feature of the assessee's case with that of the facts prevailing in Bennett Coleman And Co. Ltd supra is that, in that case, special purpose lending was given for the purpose of participation in the bid and the bid was successful, whereas in the instant case, the bid was not successful. Barring this, all the facts are identical. Hence, ratio laid down by the Co-ordinate Bench of this Tribunal supra would be squarely applicable to the facts of the instant case before us.

2.6 In view of the aforesaid observations and respectfully following the judicial precedent relied upon hereinabove, we have no hesitation in directing the Id. TPO / AO to delete the transfer pricing adjustment made in respect of special purpose loan of USD 110 million. Accordingly, the ground No.1 raised by the assessee is allowed."

14. Respectfully following the above decision, we are also inclined to direct the AO/TPO to delete the addition made concerning the guarantee

given for Special Purpose Vehicle to achieve the specific purpose, for which the loan was obtained and subsequently repaid with interest fetched from the AE's bank. The corporate guarantee obtained by the assessee for the same purpose, cannot be treated differently and the transaction have directly linked to the business of the assessee. Respectfully following the above ratio of the decision we are inclined to allow the ground raised by the assessee and direct the AO/TPO to delete the addition proposed.

15. With regard to Ground No. 1(b) which is relating to TP adjustment of ₹.20,962,480/- on account of low rate of interest charged on advance to associated enterprise, Homefield International Pvt. Ltd Mauritius ("HIPL Mauritius"). Brief facts of the case relating to the ground are, the Transfer Pricing Officer has summarized the arguments of revenue and decided as under: -

3.2.4 The arguments of the revenue department are summarized as under :-

- *The assessee has extended loan to its associated enterprise.*
- *Lending or borrowing is not one of the main businesses of the taxpayer.*
- *The assessee has charged low rate of interest on the above loan facility.*

- *Two independent enterprises in the similar circumstances as that of the assessee and its subsidiary would have charged higher interest as compensation for the financial facility provided by one party to another keeping in view the financials of the subsidiary and no security being offered.*
- *But for the relationship between the assessee and its subsidiary the assessee would have earned higher interest on the loan given by it.*
- *The business prudence or necessity of advancing loans to subsidiary is not relevant for computing arm's length price in unrelated party transactions.*
- *taxpayer is tested party and it is the source of fund.*
- *It is a transaction of lending and not of borrowing which is being tested Various varieties of risk i.e. business, credit, etc lies with the taxpayer.*
- *Independent party would not lend outside India if it can get higher return in India Thus the benchmarking would be based on the interest rate receivable in India for giving loans.*
- *Rule of relevancy suggests that ALP rate of interest should be decided on the basis of taking TP's transactions of the lender into consideration and not that of borrower or the geography in which borrower is situated.*
- *Consequently it will be more relevant to see that how the assessee would have behaved in uncontrolled transaction.*
- *It is the taxpayer, who is bearing the loss of opportunity, to earn income on the amount lent. It is the taxpayer who is deprived of its capital or funds.*
- *But for the relationship between the assessee and its subsidiary, the assessee would have earned higher interest on the loan extended by it.*
- *When the arm's length principle is applied, the taxpayer and its subsidiary are to be treated as two separate and independent entities and in these circumstances, and how two independent parties would have structured the compensation for the loan advanced.*

- *In view of the above discussion, while testing the rate of interest on lending by an Indian entity the geography of the lender is of paramount importance to test the arm's length behaviour.*
- *The taxpayer has provided loan facility to its AEs charging low rate of interest thereon.*
- *The loan is unsecured thereby the AEs did not give any security.*
- *In an uncontrolled transaction like this between unrelated parties interest would have been charged taking into account credit worthiness of the AEs, margins, security or any other consideration relevant for deciding the financial solvency of the borrower.*
- *. Higher interest would have accrued to the assessee if the said amounts were given as loans to unrelated parties in the similar circumstances as that of its subsidiary.*

3.2.5 Charging of arm's length interest

The taxpayer has made loans advances to its AEs charging lower interest. Similar uncontrolled transaction would have provided for higher interest. In view of this fact the international transaction representing loan charging lower interest is not at arm's length price, with in the meaning of section 92C (3) (a) (b) and (c) of the Income Tax Act read with Rule 10B (1) (a) of the Income Tax Act, the arm's length interest is determined by following CUP method wherein the interest rate is determined under the circumstances in which the assessee and its subsidiary is operating i.e. what is the interest that would have been earned if such loans given to unrelated parties in similar situation as that of subsidiary. Since the tested party is the assessee, the prevalent interest that could have earned by the assessee by advancing a loan to an unrelated party in India, have to be determined.

3.2.6 Computation of Arm's Length Price:

Uncontrolled Price:

While computing the rate of interest various factors have to be considered. It is imperative to see the interest rate on cash credit facility from SBI in Indian Rupee, linking the interest rate with LIBOR the prevailing interest rates on foreign currency loans extended by banks in India, transaction cost, adjustment between a banker and non banker, adjustment for security and the credit

rating of the tax payer and the AE The assessee is borrowing short term loans @ 12.25 and earns an interest from Inter corporate deposits Interest from sundry advances @ 4.45% and 4% to 12% from various parties Sundry advances are in the form of housing loans to employees, other loans to employees and penalty charges from customers on undue late payment for materials supplied. However, assessee has provided loan to its AE HIPL Mauritius at the rate of 6 months US\$ LIBOR plus 200 bps markup Further, the assessee has also incurred various risks, and the loan is without security There are definite currency risk, entity risk and country specific risks which the assessee had not factored in while lending money The assessee has not given similar loans and advances to unrelated parties in foreign currencies By charging interest at a rate less than its own borrowing rate, the assessee has certainly exposed itself to the pressure on margins and working capital. It had passed on a tangible benefit to its AE for which it never got compensated Looking to all the facts and circumstances, a mark up of 2% is held chargeable on the assessee's rate of borrowing of 12.25% p.a. Thus, the arm's length rate is held to be at 14.25%. Based on the above, the arm's length price of the international transactions entered into by the assessee (providing financial facility in the advance loan to its associated enterprises) is computed as under:

The arm's length value of the interest is calculated as under:

Loan in INR corresponding to USD 28.36 Million = Rs 47,95,80,012/-

(Rs. 2,37,72,69,326 x 28.36/140.58)

Interest charged corresponding to USD 28.36 million = Rs 4,73,77,672/-

(Rs 23,48,50,250 x 28.36/140.58)

Interest chargeable @ 14.25% (Rs 47,95,80,012 x 0.1425) = Rs 6,83,40,152/-

Therefore, the ALP = Rs 6,83,40,152/-

Transaction Value = Rs 4,73,77,672/-

105% of the transaction value = Rs 4,97,46,556/-

95% of the transaction value = Rs 4,50,08,788/- is

As the ALP falls outside the limit of +/- 5% of the transaction value, an adjustment of Rs 2,09,62,480/- is made to the transaction value"

16. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the submissions of the assessee Ld. DRP rejected the submission of the assessee and sustained the proposed additions made by the Transfer Pricing Officer/Assessing Officer. The observation of the Ld. DRP is reproduced below: -

"2.1.3 Directions:

We have considered the TPO's order and the assessee's submissions. We find that this issue was deliberated upon by our predecessor panel which had held that interest was chargeable after taking the average prime lending rate and making suitable adjustment to various risk factors at the rate of 11% per annum. We find that if the assessee had charged interest from its AE at the rate equivalent to its own domestic cost of borrowing that would have put it in a no-profit-no-loss situation. In addition to this, the assessee also needs to protect itself against various risk factors such as currency risk, entity risk and country specific risks. Therefore, we find that charging the interest at a rate derived by adding a markup for the risk factors on the domestic cost of borrowing is the right approach. The TPO has exactly done the same. He found that the assessee's own cost of borrowing during the year was 12.25% on which he added a markup of 2% for various risk factors and arrived at the arm's length interest of 14.25%. We, therefore, uphold the TPO's action in the regard."

17. Aggrieved with the above order, assessee preferred appeal before us and at the time of hearing, Ld.AR of the assessee submitted that assessee had advanced the subject loan to its AE, HIPL Mauritius in F.Y.2005-06 and no new advances were given by the assessee in the current year. This loan is a continuing transaction in the current year on which interest is recovered at LIBOR + 200 bps. Assessee has advanced

loan to HIPL Mauritius amounting to USD 140.58 million which have been funded partly through FCCB issue proceeds to the extent of USD 112.22 million and partly remittance from India to the extent of USD 28.36 million. In respect of the loan granted from FCCB issue proceeds to the extent of USD 112.22 million, the TPO has accepted interest charged at LIBOR + 200 bps to be at arm's length. However, in respect of the balance amount of USD 28.36 million, he has held that the Assessee has borrowed funds in India at an average rate of interest of 12.25 % p.a. Adding a markup thereon of 2%, the arm's length ought to have been 14.25%. This has been upheld by the DRP.

18. Further, Ld.AR of the assessee submitted that loans were foreign currency loans as such the arm's length interest rate for such foreign currency loan shall be determined with reference to LIBOR rate of same foreign currency both for funds remitted from India as well as funds remitted from outside India and not with reference to rate of interest prevailing in India for loans in Indian Rupee.

19. In support of the above propositions Ld.AR of the assessee relied on the following case law: -

- i. Tata Chemicals Ltd. VDCIT (ITA No. 9057/Mum/2010 and ITA No. 8710/Mum/2011 pronounced on 31/03/2023)*
- ii. Commissioner of Income-tax, Jaipur-II v. Vaibhav Gems Ltd [2017] 88 taxmann.com 12 (Rajasthan) (Refer para 3,10,11,12)*
- iii. Commissioner of Income tax, Jaipur v. Vaibhav Gems Ltd[2018] 99 taxmann.com 2 (SC)*
- iv. CIT -1 v/s Cotton Naturals (I) Pvt. Ltd. [2015 55 Taxmann.com 523 (Del)] (Refer Para 39-40)*
- v. Manugraph India PvtLtd. v/s Pr. Commissioner of Income Tax-3, Mumbai (ITA 758/2017 - Bombay HC pronounced on 9 September 2019)*
- vi. Manugraph India Ltdv/s PCIT (ITA 454/2016 Bombay HC pronounced on 19 November 2018)*
- vii. Everest Kanto Cylinder Ltd. v/s Commissioner of Income Tax, LTU (ITA 294/2016- Bombay HC pronounced on 20 July 2018)*
- viii. Everest Kanto Cylinder Ltdv/s Commissioner of Income Tax, LTU (ITA 435/2015 - Bombay HC pronounced on 18 July 2017)*
- ix. Everest Kanto Cylinder Ltd. v/s Commissioner of Income Tax, LTU [2014] 52 taxmann.com 395 (Mumbai - Trib,) (Refer para 10 to 12)*
- x. Vivimed Labs Ltdv/s DCIT (ITA No. 404/Hyd/2015 - ITAT Hyd) (Refer para 13 &13.1)*
- xi. Transport Corporation of India Ltd. v/s ACIT (ITA No. 117/Hyd/2016 - ITAT Hyd) (Refer para 5 & 7)*
- xii. Nagarjuna Fertilizers and Chemicals Ltd. v/s ACIT (ITA Nos. 93 & 2031/Hyd/2017 - ITAT Hyd) (Refer Para 3.4, 6 & 8.1 to 8.3)*
- xiii. DCIT v. Gujarat NRE Coke Ltd(I.T.ANos. 1150 & 1151/Kol/2017 - ITAT Kolkata) (Refer Para 12 to 16)*
- b) The loan transaction under consideration are continuing loans from the FY 2005- 06 for which the Ld. TPO has accepted the ALP as LIBOR+200bps.*

20. On the other hand, Ld DR heavily relied on the order of lower authorities.

21. Considered the rival submissions and material placed on record, we observe that the assessee has remitted the above said loans to its AE in AY 2005-06 and the same loan was outstanding, hence we noticed that in assessee's own case for the A.Y. 2006-07 in ITA No. 9057/MUM/2010 dated 31.03.2023, the Coordinate Bench held as under:-

19.1. We have heard rival submissions and perused the materials available on record. At the outset, we find that the lending to AE has been made in earlier years and the same has been continuing during the year. No fresh lending was made during this year. The loans given to AE are continuing transactions during the year on which interest is recovered by the assessee company on LIBOR + 200 basis points. The same was considered to be at arm's length price while doing the benchmarking in the TP study report. The total loan outstanding to Home Field International Pvt. Ltd (HLP) Mauritius was USD 140.58 million which has been funded partly through FCCB issue proceeds to the extent of USD 112.22 million and remaining USD 28.36 million has been funded by way of remittance from India. The lending at the interest rate of LIBOR +200 basis points to the AE was accepted to be at arm's length price by the Id. TPO in A.Y.2006-07 i.e. the immediately preceding year which has been adjudicated hereinabove. The assessee had actually earned interest income of 36.37 lakhs, Rs.11.85 lakhs and Rs.14.09 lakhs. This interest was considered erroneously by the Id. TPO at 36.37%, 11.85% and 14.09%. Based on this, the Id. TPO by applying CUP method adopted 16% interest rate to be the arm's length price which is the domestic SBI Prime Lending Rate. (PLR). The assessee argued before the Id. DRP that when the loan is given in foreign currency, how the interest rate applicable at SBI PLR rates could be charged on the said loans. The assessee always argued that the currency in which the loan amount is getting consumed and the country in which the loan is getting utilized is to

be considered and since the loan is in USD and the repayment from AE is also going to be in USD, then interest rate @LIBOR + 200 basis points would be at arm's length. The assessee in support of its submission also submitted a quotation received from HSBC for similar type of transaction which quoted interest rate of LIBOR + 0.5%. As against this, the assessee has charged interest @ LIBOR + 2% from its AE and accordingly, it was submitted that assessee's interest rate is at arm's length. The Id. DRP however, took a different view. The Id. DRP observed that out of USD 140.58 million, the assessee already had funds lying by way of FCCB issue proceeds to the extent of USD 112.22 million in its dollar account. Hence, for that amount, interest to be adopted would be LIBOR + 2%. Accordingly, no TP adjustment would be required for the same. The Id. DRP however, held that with regard to remaining USD 28.36 million, since the same were sourced out of Indian funds, Indian banking lending rate should be considered which was determined by the Id. DRP at 11%. The Id. DRP directed the Id. TPO to determine the ALP @11% interest rate in respect of USD 28.36 million, which was duly implemented by the Id. AO in the final assessment order. Aggrieved, the assessee is in appeal before us.

19.2. We find that the issue as to whether LIBOR interest rate should be adopted in respect of loans given in foreign currency in which the said loan is to be recovered was subject matter of consideration by the Hon'ble Delhi High Court in the case of CIT vs. Cotton Naturals (I)(P) Ltd. reported in 276 CTR 445 (Del). The relevant operative portion in this regard is reproduced hereunder:-

"39. The question whether the interest rate prevailing in India should be applied, for the lender was an Indian company/assessee, or the lending rate prevalent in the United States should be applied, for the borrower was a resident and an assessee of the said country, in our considered opinion, must be answered by adopting and applying a commonsensical and pragmatic reasoning. We have no hesitation in holding that the interest rate should be the market determined interest rate applicable to the currency concerned in which the loan has to be repaid. Interest rates should not be computed on the basis of interest payable on the currency or legal tender of the place or the country of residence of either party. Interest rates applicable to loans and deposits in the national currency of the borrower or the lender would vary and are dependent upon the fiscal policy of the Central bank, mandate of the Government and several other parameters. Interest rates payable on currency specific loans/ deposits are significantly universal and globally

applicable. The currency in which the loan is to be repaid normally determines the rate of return on the money lent, i.e. the rate of interest. Klaus Vogel on Double Taxation Conventions (Third Edition) under Article 11 in paragraph 115 states as under:—

"The existing differences in the levels of interest rates do not depend on any place but rather on the currency concerned. The rate of interest on a US \$ loan is the same in New York as in Frankfurt—at least within the framework of free capital markets (subject to the arbitrage). In regard to the question as to whether the level of interest rates in the lender's State or that in the borrower's is decisive, therefore, primarily depends on the currency agreed upon (BFH BSt.B1. II 725 (1994), re. 1 § AStG). A differentiation between debt-claims or debts in national currency and those in foreign currency is normally no use, because, for instance, a US \$ loan advanced by a US lender is to him a debt-claim in national currency whereas to a German borrower it is a foreign currency debt (the situation being different, however, when an agreement in a third currency is involved). Moreover, a difference in interest levels frequently reflects no more than different expectations in regard to rates of exchange, rates of inflation and other aspects. Hence, the choice of one particular currency can be just as reasonable as that of another, despite different levels of interest rates. An economic criterion for one party may be that it wants, if possible, to avoid exchange risks (for example, by matching the currency of the loan with that of the funds anticipated to be available for debt service), such as taking out a US \$ loan if the proceeds in US \$ are expected to become available (say from exports). If an exchange risk were to prove incapable of being avoided (say, by forward rate fixing), the appropriate course would be to attribute it to the economically more powerful party. But, exactly where there is no 'special relationship', this will frequently not be possible in dealings with such party. Consequently, it will normally not be possible to review and adjust the interest rate to the extent that such rate depends on the currency involved. Moreover, it is questionable whether such an adjustment could be based on Art. 11 (6). For Art. 11(6), at least its wording, allows the authorities to 'eliminate hypothetically' the special relationships only in regard to the level of interest rates and not in

regard to other circumstances, such as the choice of currency. If such other circumstances were to be included in the review, there would be doubts as to where the line should be drawn, i.e., whether an examination should be allowed of the question of whether in the absence of a special relationship (i.e., financial power, strong position in the market, etc., of the foreign corporate group member) the borrowing company might not have completely refrained from making investment for which it borrowed the money."

40. The aforesaid methodology recommended by Klaus Vogel appeals to us and appears to be the reasonable and proper parameter to decide upon the question of applicability of interest rate. The loan in question was given in foreign currency i.e. US \$ and was also to be repaid in the same currency i.e. US \$. Interest rate applicable to loans granted and to be returned in Indian Rupees would not be the relevant comparable. Even in India, interest rates on FCNR accounts maintained in foreign currency are different and dependent upon the currency in question. They are not dependent upon the PLR rate, which is applicable to loans in Indian Rupee. The PLR rate, therefore, would not be applicable and should not be applied for determining the interest rate in the extant case. PLR rates are not applicable to loans to be re-paid in foreign currency. The interest rates vary and are thus dependent on the foreign currency in which the repayment is to be made. The same principle should apply.

41. Counsel for the Revenue had made reference to Chapter 10 of the U.N. Transfer Pricing Manual, relevant portion of which reads:—

"10.4.10. Financial Transactions

10.4.10.1. Intercompany loans and guarantees are becoming common international transactions between related parties due to the management of cross-border funding within group entities of an MNE group. Transfer pricing of inter-company loans and guarantees are increasingly being considered some of the most complex transfer pricing issues in India. The Indian transfer pricing administration has followed a quite sophisticated methodology for pricing inter-company loans which revolves around:

- *Examination of the loan agreement;*
- *A comparison of terms and conditions of loan agreements;*
- *The determination of credit ratings of lender and borrower;*
- *The identification of comparable third party loan agreements: and*
- *Suitable adjustments to enhance comparability.*

10.4.10.2. The Indian transfer pricing administration has come across cases of outbound loan transactions where the Indian parent has advanced to its associated entities (AE) in a foreign jurisdiction either interest free loans or loans at LIBOR (London Interbank Offered Rate) or EURIBOR (Euro Interbank Offered Rate). The main issue before the transfer pricing administration is benchmarking of these loan transactions to arrive at the ALP of the rates of interest applicable on these loans. The Indian transfer pricing administration has determined that since the loans are advanced from India and Indian currency has been subsequently converted into the currency of the geographic location of the AE, the Prime Lending Rate (PLR) of the Indian banks should be applied as the external CUP and not the LIBOR or EURIBOR rate.

10.4.10.3. A further issue in financial transactions is credit guarantee fees. With the increase in outbound investments, the Indian transfer pricing administration has come across cases of corporate guarantees extended by Indian parents to its associated entities abroad, where the Indian parent as guarantor agrees to pay the entire amount due on a loan instrument on default by the borrower. The guarantee helps an associated entity of the Indian parent to secure a loan from the bank. The Indian transfer pricing administration generally determines the ALP of such guarantee under the Comparable Uncontrolled Price Method. In most cases, interest rates quotes and guarantee rate quotes available from banking companies are taken as the benchmark rate to arrive at the ALP. The Indian tax administration also uses the interest rate prevalent in the rupee bond markets in India for bonds of different

credit ratings. The difference in the credit ratings between the parent in India and the foreign subsidiary is taken into account and the rate of interest specific to a credit rating of Indian bonds is also considered for determination of the arm's length price of such guarantees.

10.4.10.4. However, the Indian transfer pricing administration is facing a challenge due to non-availability of specialized databases and of comparable transfer prices for cases of complex inter-company loans as well as mergers and acquisitions that involve complex inter-company loan instruments as well as an implicit element of guarantee from the parent company in securing debt."

42. The first paragraph quoted above, rightly stipulates that inter-company loans would require examination of the loan agreement, comparison of the terms and conditions of loan agreements, the determination of credit rating of the lender and the borrower, identification of comparable third party loan agreements and suitable adjustments should be made. In addition to the aforesaid factors, the comparability analysis should also take into account the business relationship and the functions performed by the subsidiary AE for the parent company. In the present case, we are not concerned with paragraph 10.4.10.3 of the United Nations Transfer Pricing Manual. However, we are unable to agree with the position set out and asserted in paragraph 10.4.10.2 of the Manual. The reasoning given therein is contrary to the accepted international tax jurisprudence and the rules adopted and applied. There is no justification or a cogent reason for applying PLR for outbound loan transactions where the Indian parent has advanced loan to an AE abroad. Chapter 10 of the United Nations Practical Manual on Transfer Pricing relates to country practices. The said Chapter sets out an individual country's view point and its experiences for the information of the readers. The said Chapter does not reflect the view of the Manual. Paragraph 10.1 of the United Nations Practical Manual on Transfer Pricing for Developing Countries reads:—

"10.1. Preamble by the Subcommittee on Transfer Pricing: Practical Aspects

10.1.1. In the first nine chapters of this Manual, the Subcommittee has sought to provide practical guidance on the application of transfer pricing rules based on Article 9(1) of the UN Model Tax Convention and the arm's length principle embodied in that Article. With regard to chapters one through nine, the Subcommittee has discussed and debated the merits of the guidance that is provided and, while there may be some disagreement on certain points, for the most part the Subcommittee is in agreement that the guidance in those chapters reflects the application of the arm's length principle as embodied in the UN Model Tax Convention.

10.1.2. The Subcommittee recognizes that individual countries, particularly developing and emerging economies, struggle at times with the details of applying these treaty-based principles in a wide variety of practical situations. It therefore seemed appropriate to allow representatives of individual countries an opportunity to set out their individual country viewpoints and experiences for the information of readers. Those individual country views are contained in this chapter. It should be emphasized that it does not reflect a consistent or consensus view of the Subcommittee."

43. Normally there would be a difference between the lending rate and borrowing rate in each country. Some authors and writers suggest that the average or mid-point between the two should be taken. However, others like Klaus Vogel, have suggested that economic purpose and substance of the debtclaim or debt for which granting of credit calls for the lending rate would be determinative. Thus, in case of a capital investment, the borrowing rate will apply, whereas in case of credit allowed to a customer on sale of goods, the lending rate would apply. We do not deem it necessary to enter into this controversy and express our view as regards the same.

19.3. Further, we find that the Hon'ble Jurisdictional High Court in the case of PCIT vs. Manugraph India Pvt. Ltd in Income Tax Appeal No.758 of 2017 dated 09/09/2019 also had an occasion to consider the same issue. The relevant question raised before the Hon'ble Jurisdictional High Court was as under:-

"(a). Whether on the facts and in the circumstances of the case and in law, in terms of provision of Section 92C of the Income Tax Act read with Rule 10B of the Income Tax Rules, the Hon'ble Tribunal was right in restricting the rate of interest on loans given to Associated Enterprises @ LIBOR + 2% instead of 17.22% proposed by the Transfer Pricing Officer?"

19.3.1. This question was disposed of by the Hon'ble Jurisdictional High Court by observing as under:-

3. Regarding Question No.(a)

(a) It is an agreed position between the parties that the issue raised herein stand concluded against the Revenue and in favour of the Respondent - Assessee. This by the decision of this Court in the case of the same Respondent viz. Principal Commissioner of Income Tax v/s. Manugraph (Income Tax Appeal No. 454 of 2016) rendered on 19 November 2018.

(b) The aforesaid decision was rendered following an earlier decision of this Court in the case of CIT v/s. M/s. Everest Kanto Cylinders Ltd. (378 ITR 67). (c) Therefore, for the reasons indicated in the above orders, the question No.(a) does not raise any substantial question of law, Thus not entertained.

19.4. Similar views were expressed by the Hon'ble Jurisdictional High Court in the case of CIT vs. Everest Kanto Cylinder Ltd in Income Tax Appeal No.435 of 2015 dated 18/07/2017; Income Tax Appeal No.294 of 2016 dated 20/07/2018 and in the case of PCIT vs. Manugraph India Ltd in Income Tax Appeal No.454 of 2016 dated 19/11/2018. Respectfully following the same, we direct the Id. AO to delete the TP adjustment made in respect of interest on loan advanced to AE in A.Y.2007-08.

Accordingly, the ground No.1 raised by the assessee is allowed."

22. Respectfully following the above decision, we are inclined to allow the ground raised by the assessee in respect of proposed addition in Interest charges. Accordingly, the above ground is allowed.

23. With regard to Ground No. 1(c) which is in respect of TP adjustment of ₹.41,51,865/- on account of salary of employees deputed to the Joint Venture, IMACID, brief facts and the conclusion reached by the Transfer Pricing Officer relating to the above ground are reproduced below: -

"4. Deputation of employees to AE

The assessee has deputed three employees namely Mr Sanjay Agarwal, MrA.J Gupta as a Jt Managing Director and Mr. Sunil Chauhan. The amount recovered by the assessee for deputing all the three employees to AE IMACID is Rs. 57,70,357/- in the form of salary from its Associated Enterprises is compared to the Arms Length price or salary as under:

In the case of recovery of salary expenses from its AE the assessee has recovered more than 100% of the salary cost in the case of Mr Sanjay Agarwal. MrSanjay Agarwal was deputed from August 07 till March 08 i.e(8 months) the amount recovered by the assessee was Rs. 8,23,354/- where as the proportionate salary of Mr Sanjay Agarwal for that relevant period in India is Rs6,81,104/-. This shows that the assessee had actually recovered the salary with a markup of 20.88% $([823354-681104] \times 100 / 681104)$. In the case of Mr A.J Gupta the employee was deputed for 12 months to AE IMACID and assessee as recovered an amount of Rs36,45,397/- where the salary actually paid by assessee as per Form 16 is Rs. 89,03,646/-. In the case of MrSunil Chauhan, the employee was deputed for 12 months to AE IMACID and the assessee has recovered an amount of Rs. 13,01,606/- where the salary actually paid by the assessee as per Form 16 is Rs. 23,35,934/- The assessee has under recovered the salary expenses in case of two of the employees deputed to IMACID. Show cause was given to the assessee as to why assessee should not have made recovery with 10% mark up. The AR replied that

- the assessee has recovered service fee from its AE, IMACID at the rate of US\$ 7500 per month, which was agreed by the assessee and office CherifienDes Phosphates (OCP) and Chambal Fertilizers and Chemical Limited. The assessee is one of the joint venture partner and shareholder in its AE IMACID having a shareholding of 33.33%.*

- Further, it was stated that the arm's length price is based on market forces/ values of an activity. It is based on cost of the activity. There are circumstances where the market values of the activities or services could be lower than its corresponding cost. In the present case of the assessee, the market value of the services of the Joint Managing Director deputed by the assessee has been established to be US \$ 7500 per month (i.e. US\$ 90,000 per annum) by an agreement between unrelated Non AE third party i.e. joint venture partners of IMACID. Therefore this market value should be considered as arm's length price rather than the entire salary cost of the concerned employee.

As discussed above the assessee itself is recovering in case of other employee more than the salary cost. The assessee's conduct clearly demonstrates that it recovers the salary cost selectively. There have been instances of mark up on salaries. In this case the assessee by absorbing the total cost of the employees to the company has passed a tangible benefit to its AE for which it has not been compensated. However, the Hon'ble DRP in its order dated 30.9.2011 has directed for AY07-08 that in respect of salary paid to Mr AJ Gupta who worked as Jt. M.D of the J.V of the assessee 33.33% of his salary shall be treated as attributable to his services rendered to his employer the assessee, and the remaining to the J.V. As the facts of this year are similar to those for AY 07-08, the corresponding apportionment of salary attributable to the assessee and the J.V is Rs 27,67,882/- and Rs 59,35,764/- respectively. In line with the directions of the hon'ble DRP it may be seen that the concerned employee MrAJ. Gupta's salary attributable to the work done for the AE was Rs 59,35,764/- but the assessee recovered only Rs 36,45,397/-.

The amount recovered by the assessee in case of two of the employees namely Mr. A J Gupta and Mr Sunil Chauhan at Rs.49,47,003/- in the form of salary from its Associated Enterprises is understated. The arm's length price is computed as under:-

| | |
|---|---------------|
| Arms Length Salary (Salary Plus 10% Markup [5935764 + 2335934 x 1.1 | ₹.90,98,868 |
| Salary Recovered | ₹.49,47,003/- |
| Shortfall being adjustment under section 92CA | ₹.41,51,865/- |

105% of the transaction value = ₹.51,94,003/-

95% of the transaction value = ₹.46,99,653/-

As the ALP lies outside the limit of +/- 5% of the transaction value, an adjustment of Rs. 41,51,865/- (difference between Rs.90,98,868/-and Rs. 49,47,003/-) is made to the transaction."

24. Aggrieved, assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the submissions of the assessee Ld. DRP rejected the submission of the assessee and sustained the proposed additions made by the Transfer Pricing Officer / Assessing Officer. The observation of the Ld. DRP is reproduced below:

"2.2.3 Directions: -

We have considered the relevant facts and the submissions of the assessee. We observed that our predecessor panel deliberated on this issue for AY 2007-08 and held that the recovery made in respect of salary of Mr. A J Gupta was at arm's length as he was working in the capacity of JMD of the AE in which the assessee had 33.33% share As observed by the TPO, if considered in line with the directions of the DRP, it is noted that the concerned employee, Mr A.J Gupta's salary attributable to the work done for AE was Rs.59,35,764/-, but the assessee recovered only Rs.36,45,397/- and, hence, the amount recovered by the assessee in the form of salary from its AE is understated. Similarly, there was an under recovery in the case of Mr Sunil Chauhan, and we therefore, uphold the adjustment on this count."

25. At the time of hearing, Ld AR submitted that the Shareholder's agreement among the assessee, OCP and CFCL enables the assessee and CFCL to appoint JT. Managing Director (MD) on alternative basis for a period of two years at the remuneration to be agreed by all the JV partners. In furtherance of the same the assessee deputed Mr.A.J.Gupta

as Jt. MD. Further it has also deputed two other employees being technical personnel to IMACID, Mr. Sanjay Agarwal and Mr. Sunil Chauhan. The amounts recovered by the assessee from IMACID with respect to the deputation of its employees are at arm's length as the rates of \$7500 per month w.r.t to the deputation of Mr. A.J. Gupta and \$3000 per month w.r.t. Mr. Sanjay Agarwal and Mr. Sunil Chauhan, has been agreed by the assessee and the OCP and CFCL, who are unrelated and independent to each other. Thus, as per section 92F(ii) of the Act, it is a price agreed between persons who are not associated enterprises and is, thus, considered to be at arm's length price, therefore no transfer pricing adjustment is warranted.

26. Further, Ld.AR of the assessee submitted that with respect to the deputation of Mr A.J. Gupta as Jt. Managing director, it is stated that the Joint Venture partner CFCL, which is not a related party to the assessee, deputed its Jt. MD to AE IMACID and for such deputation it was paid @7500 p/m only as remuneration.

27. On the other hand, Ld DR heavily relied on the orders of lower authorities.

28. Considered the rival submissions and material placed on record. We observe from the submissions and material submitted before us that the assessee has deputed its employees on rotation basis to the Joint Venture IMACID, which formed to perform certain specific venture along with the other JV partner CFCL. These employees holding various positions in the organization was deputed to the JV on the basis of joint agreement, which is placed on record, on the basis of agreed salary, for which both the JV partners have deputed their employees on the agreed salaries. It is brought to our notice that the other JV partner has charged the same salaries as per the joint agreement. Since the other JV partner is not related party and agreed to perform the duties for the purpose of common interest, there may be higher or lower salaries given to the respective employees, when there is common agreements and for common interest, the difference of such cost should be considered as extra ordinary item and should be ignored. The assessee has brought on record the various documents to demonstrate that there is common interest involved in this transaction of deputing employees on rotation basis. Therefore, the proposed adjustment on this transaction is uncalled for and directed to be deleted. Accordingly, the ground raised by the assessee is allowed.

29. With regard to Ground No. 2 which is in respect of Disallowance of administrative expense under section 14A of the Act., brief facts of the grounds as summarized by the Assessing Officer and the conclusion reached by the Assessing Officer are reproduced below: -

"5.1 It is seen from Schedule 2 forming part of your P&L a/c., for the year ended 31.03.2008 (herein after referred to as the accounts) that the assessee has disclosed dividend income of 37.62 crores on long term trade investments, profit of 487.47 crores on sale of such investments, dividend of 47.39 cores on current investments and interest of 3.55 crores on tax free UTI Bonds Out of the same, the assessee has claimed dividend of 85 crores and interest of 1.52 crores as exempt from income tax u/s.10(34). Further, long term capital gain of 488 crores have been claimed exempt u/s 10(38) of the Act. It is further seen from schedule 4, on page 60 of the Annual Report the assessee has incurred expenditure of 21.18 crores under the head interest The assessee was, therefore, requested to show cause as to why the expenditure should not be disallowed u/s14A of the I.T Act r.w Rule 8D of the I.T Rules It is further more seen that in note B-1 to the return of income the assessee has stated that the company has not incurred any expenses for earning dividend income / interest on tax free bonds. The assessee submitted reply as under:

"We enclosed a copy of the judgment of the Bombay High Court in our own case in 256 ITR 395, wherein it was held that "The assessee-respondent had claimed that the interest attributable to the borrowings for investment in tax- free bonds was to be allowed under section 36(1)(iii)The Tribunal recorded a finding of fact that investment in question was a business investment and it allowed the sameThe High Court held that this ground raised no substantial question of law for its considerationThe question, therefore, needed no consideration."

The Hon'ble Supreme Court has rejected the SLP filed by the department. Thus no direct expenses can be correlated with the earning of the exempt income.

No indirect expenses have been incurred by the company. However, without prejudice to our contention, a certain percentage of the salaries of our treasury operation may be considered attributable towards the earning of the exempt income. We enclose a working of the same and accordingly an amount of Rs. 66,000 may be considered towards the indirect expenses and the amount u/s 14A may be considered for disallowance.

TATA CHEMICALS LIMITED

F.Y.06-07

A.Y.07-08

Working of disallowance u/s 14A

1. Allocation of expenses

| | |
|--|-------------------------|
| <i>Salary of CFO</i> | <i>70,00,000</i> |
| <i>Salary of other staff in Treasury Dept</i> | <i>50,00,000</i> |
| <i>Total</i> | <i><u>12,00,000</u></i> |
| <i>5% of salary of CFO, Deputy CFO & Head Treasury</i> | <i>350,000</i> |
| <i>5% of salary of staff</i> | <i><u>250,000</u></i> |
| <i>Total</i> | <i><u>600,000</u></i> |
| <i>Other Overheads (10% of total above)</i> | <i><u>60,000</u></i> |
| <i>Total disallowance u/s 14A</i> | <i><u>6,60,000</u></i> |

5.2 The assessee initially disallowed Rs.7,97,500/- u/s 14A. However, in the course of assessment proceedings, it submitted the revised working as mentioned above wherein certain percentage of the salaries of the treasury operations may be considered as attributable towards the earning of exempt income.

5.3 Provisions of Section 14A of the Income Tax Act clearly state that the Assessing Officer can determine the amount of expenditure incurred in relation to exempted income once he satisfied that the claim of the assessee that no expenditure has been incurred in relation to income, which does not form part of the total income, is incorrect. Moreover, the expenditure in relation to exempt income that is mandated to be disallowed u/s 14A is not just the direct expenditure but includes expenditure of all kinds including the indirect expenditure. Sub-section (2) of section 14A provides that the Assessing Officer shall determine the amount of

expenditure incurred in relation to such income which does not form part of the total income under the IT Act in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under the IT Act. Rule 8D of income tax rules lays down the prescribed method for determining the expenditure incurred in relation to exempt income. Sub-section (3) categorically provides the method prescribed under sub-section (2) shall also apply to a case where an assessee claims that no expenditure has been incurred by it in relation to income which does not form part of total income.

The assessee has claimed that no expenditure was incurred by it in relation to earning the exempted income of dividend of Rs 85 crores and interest of 1.52 crores as exempt from income tax u/s. 10(34). However, the assessee has not been able to prove that all the expenditure claimed by it has been incurred exclusively for earning the taxable income only. Instead of proving the above, the assessee's only explanation was that no expenditure whatsoever was incurred directly by the assessee in relation to earning the above exempt income.

5.4 In the above context, it would be absurd to presume that the said substantial incomes can be earned without taking conscious investment decisions by the management and without devoting substantial financial, for which expenses were incurred by the assessee during the year and debited human, establishment, communication and other resources of the assessee, to P&L Account.

5.5 Therefore, it is evident that all expenses connected with the exempt income have to be disallowed under section 14A regardless of whether they are direct or indirect, fixed or variable and managerial or financial in accordance with law. It is further evident that deduction in respect of expenditure incurred by the assessee in relation to exempt income and taxable income has to be determined as per mechanism laid down in section 14A and in accordance with the method as prescribed under Rule 8D. 5.6

5.6 The total disallowance 14A of Income Tax Act r.w.Rule 8D is computed as under:

| | | Amount (Crores) |
|-----|---|---|
| I) | Amount of Expenses directly incurred relating to tax free Income | NIL |
| II) | Proportionate expenses by way of interest incurred (expended): | |
| | Interest expended during the year (A) | 38.02 |
| | Average value of tax free investments (B) (Opening Tax Free Investments + Closing Tax free investments (Stock-in-trade + Investments)/2) | 598.17 |
| | Average of total assets (C) (Opening Total Assets + Closing Total Assets/2) | 6,139.16 |
| | Disallowance = A * B / C 38.02*598.17/61,39.16 | 3.70 |
| III | 0.5% of average value of tax free investment 0.5% of (B) above | 0.5% of Rs.598. 17 crores = Rs.2.99 crores |
| | Total disallowance as per 14A r.w.Rule 8D = (1 + II + III) | Rs.6.69 crores |

30. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the submissions of the assessee Ld. DRP rejected the submission of the assessee and sustained the proposed additions made by the Transfer Pricing Officer / Assessing Officer. The observation of the Ld. DRP is reproduced below: -

3.3 Directions:

We have considered the relevant facts and the contentions of the assessee and find that the AO has made an addition on account of expenditure u/s.14A. This is evidence enough that the AO is not satisfied with the calculation of the estimation of the assessee in the return of income. The act does not oblige the AO to record his satisfaction in writing and send it to the assessee. The assessee cannot read into the law what is not provided therein. Further, as held by Hon'ble Bombay High Court in the case of Godrej Boyce & Co, the provisions of Rule 8D are applicable for A.Y. 2008-09 and subsequent years. Hence, in principle, the application of Rule 8D is

confirmed. However, as regards the calculation mistakes pointed out by the assessee, we direct the assessing officer to verify the facts and work out the quantum of disallowance u/s. 14A read with Rule 8D."

31. Aggrieved with the above order assessee is in appeal before us and raised issue. At the time of hearing, Ld.AR of the assessee brought to our notice relevant facts of the case and submitted that Submission for the year under consideration, details of exempt income are as under:

| | |
|---|------------------------------|
| <i>Dividend income on shares and mutual funds</i> | <i>Rs. 85.01 Crs</i> |
| <i>Interest on UTI tax free bond</i> | <i>Rs. 1.53 CRs</i> |
| <i>Long term capital gain</i> | <i>Rs. 488.09 Crs</i> |
| <i>Total</i> | <i>Rs. 574.63 Crs</i> |

The dividend and interest income referred hereinabove, has been directly credited to the Assessee's bank Accounted.

32. In the return of income, the suo-motu disallowance under section 14A of the Act stood at ₹.7,97,500 being the administrative expenditure.

33. Ld.AR of the assessee submitted that no interest disallowance was made as against total investment as on 31.03.2008 of ₹.3,741.40 crore, investment yielding tax free income was ₹.421 crore and average of opening and closing balance of such investments yielding tax free income was ₹.598.17 crore (see paragraph 5.6 at pages 4 and 5 of the assessment order), interest free owned funds stood at ₹.5519.92

crore (being Share capital of ₹.234.06 crore + Reserves and surplus of ₹.3337.62 crore and Depreciation reserve of ₹.1948.24 crore.

34. Ld.AR of the assessee submitted that for administrative expenditure disallowance proportionate salary of CFO Deputy CFO, Head Treasury and Staff including overhead expenses was considered (refer Flap -2 of Factual Paper Book). This was in accordance with final assessment order passed for assessment year 2006-07 pursuant to directions given by the DRP. For assessment year 2007-08, the Assessing Officer had accepted this position in the draft assessment order itself (refer Flap - 23 of the Factual Paper Book).

35. Ld.AR of the assessee brought to our notice that before invoking rule 8D of the Rules, as per section 14A(2) of the Act, the Assessing Officer has to record his dis-satisfaction with the suo motto disallowance made by the assessee. In the present case, though the Assessing Officer has made a reference to the suo motto disallowance but the satisfaction as recorded by him proceeds on the basis that no such disallowance has been made. Hence, in the absence of an objective satisfaction, computing the disallowance under section 14A by invoking rule 8D was not permissible. In this regard reliance is placed on Tribunal's order in

Trent Ltd. vs ACIT being order dated 15.07.2020 in ITA No. 5775/Mum/2011- paragraphs 10 to 23 at pages 8 to 16 of the Order and Judgment of the Hon'ble Apex Court in Godrej & Boyce Mfg. CoLtd. (2017) 394 ITR 449.

36. Further, he submitted that on merits no interest disallowance could have been made in view of sufficient own funds. He relied on the case of South Indian Bank Ltd. v. CIT (2021) ITR 1 (SC). For administrative expenditure it is submitted that disallowance as made by the Assessee was justified.

37. Considered the rival submissions and material placed on record, we observe from the record that the AO has recorded his satisfaction in the assessment order, before us Ld AR made a submission that even though AO has recorded satisfaction still he has not recorded objective satisfaction. In our view, the satisfaction recorded by the AO is relevant to the disallowance under consideration and there is no need to record further. There is no such requirement in the law. It is enough that there is enough material to convey the information that there is non-satisfactory in the method of expenses recorded relating to exempt income. Therefore, we reject the objections raised by the Ld AR.

However, we are in agreement with the findings of Ld DRP that the disallowance u/s 14A is applicable to the assessee's case for this year and the proposed disallowance by AO needs certain adjustments. Accordingly, we direct the AO to consider the merit in submission of the assessee relating to the disallowance as per rule 8D(2)(ii) on interest expenditure. We observe that the assessee has sufficient interest free funds in the business. As held in the case of South Indian Bank Ltd., v. CIT (supra) the Hon'ble Supreme Court held as under: -

"17. In a situation where the assessee has mixed fund (made up partly of interest free funds and partly of interest-bearing funds) and payment is made out of that mixed fund, the investment must be considered to have been made out of the interest free fund. To put it another way, in respect of payment made out of mixed fund, it is the assessee who has such right of appropriation and also the right to assert from what part of the fund a particular investment is made and it may not be permissible for the Revenue to make an estimation of a proportionate figure. For accepting such a proposition, it would be helpful to refer to the decision of the Bombay High Court in Pr. CIT v. Bombay Dyeing and Mfg. Co. Ltd, I.T.A. No.1225 of 2015 where the answer was in favour of the assessee on the question, whether the Tribunal was justified in deleting the disallowance under Section 80M of the Act on the presumption that when the funds available to the assessee were both interest free and loans, the investments made would be out of the interest free funds available with the assessee, provided the interest free funds were sufficient to meet the investments. The resultant SLP of the Revenue challenging the Bombay High Court judgment was dismissed both on merit and on delay by this Court. The merit of the above proposition of law of the Bombay High Court would now be appreciated in the following discussion.

18. In the above context, it would be apposite to refer to a similar decision in Commissioner of Income Tax (Large Tax Payer Unit) Vs. Reliance Industries Ltd. (2019) 410 ITR 466 SC/ (2019) 20 SCC 478, where a Division Bench of this Court expressly held that where there is finding of fact that interest free funds available to assessee

were sufficient to meet its investment it will be presumed that investments were made from such interest free funds.

19. In *HDFC Bank Ltd. Vs. Deputy Commissioner of Income Tax*, (2016) 383 ITR 529 (Bom) / 2016 SCC Online Bom 1109, the assessee was a Scheduled Bank and the issue therein also pertained to disallowance under Section 14A. In this case, the Bombay High Court even while remanding the case back to Tribunal for adjudicating afresh observed (relying on its own previous judgment in same assessee's case for a different Assessment Year) that, if assessee possesses sufficient interest free funds as against investment in tax free securities then, there is a presumption that investment which has been made in tax free securities, has come out of interest free funds available with assessee. In such situation Section 14A of the Act would not be applicable. Similar views have been expressed by other High Courts in *CIT Vs. Suzlon Energy Ltd.* (2013) 354 ITR 630 (Guj)/ 2013 SCC Online Guj 8613, *CIT Vs. Microlabs Ltd.* (2016) 383 ITR 490 (Karn)/ 2016 SCC Online Kar 8490 and *CIT Vs. Max India Ltd.* (2016) 388 ITR 81 (P & H) / 2016 SCC Online P&H 6788 Mr. S Ganesh the learned Senior Counsel while citing these cases from the High Courts have further pointed out that those judgments have attained finality. On reading of these judgments, we are of the considered opinion that the High Courts have correctly interpreted the scope of Section 14A of the Act in their decisions favouring the assessees.

20. Applying the same logic, the disallowance would be legally impermissible for the investment made by the assessees in bonds/shares using interest free funds, under Section 14A of the Act. In other words, if investments in securities is made out of common funds and the assessee has available, non-interest-bearing funds larger than the investments made in tax-free securities then in such cases, disallowance under Section 14A cannot be made.

.....

28. The above conclusion is reached because nexus has not been established between expenditure disallowed and earning of exempt income. The respondents as earlier noted, have failed to substantiate their argument that assessee was required to maintain separate accounts. Their reliance on *Honda Siel (Supra)* to project such an obligation on the assessee, is already negated. The learned counsel for the revenue has failed to refer to any statutory provision which obligate the assessee to maintain separate accounts which might justify proportionate disallowance.

29. *In the above context, the following saying of Adam Smith in his seminal work - The Wealth of Nations may aptly be quoted:*

"The tax which each individual is bound to pay ought to be certain and not arbitrary. The time of payment, the manner of payment, the quantity to be paid ought all to be clear and plain to the contributor and to every other person Echoing what was said by the 18th century economist, it needs to be observed here that in taxation regime, there is no room for presumption and nothing can be taken to be implied. The tax an individual or a corporate is required to pay, is a matter of planning for a tax payer and the Government should endeavour to keep it convenient and simple to achieve maximization of compliance. Just as the Government does not wish for avoidance of tax equally it is the responsibility of the regime to design a tax system for which a subject can budget and plan. If proper balance is achieved between these, unnecessary litigation can be avoided without compromising on generation of revenue.

30. *In view of the forgoing discussion, the issue framed in these appeals is answered against the Revenue and in favour of the assessee. The appeals by the Assesseees are accordingly allowed with no order on costs."*

38. Respectfully following the above decision, we direct the AO to delete the additions proposed under rule 8D(2)(ii) since the assessee has enough interest free funds available in the business. With regard to other disallowance, the same are sustained. In the result, the ground raised by the assessee is partly allowed.

39. With regard to Ground No. 3 which is in respect of disallowance of payments made to various institutions u/s.40A(9) of the Act. At the time of hearing, Ld.AR of the assessee brought to our notice that the issue in appeal has been considered by the Co-ordinate Bench of this

Tribunal in assessee's own case for the A.Y. 2007-08 and Coordinate Bench has adjudicated and decided the issue in favour of the assessee and against the department. Ld.AR of the assessee prayed that the same decision may be adopted for the year under consideration.

40. On the other hand, Ld. DR has fairly accepted the submissions of the Ld.AR.

41. Considered the rival submissions and material placed on record, we observe from the record that identical issue is decided in favour of the assessee in assessee own case for the A.Y. 2007-08. We observe that in ITA No.2553/MUM/2012 for the A.Y. 2005-06 dated 06.07.2022 the coordinate Bench held as under: --

55. We have considered the rival submissions and perused the material available on record. From the perusal of the impugned order passed by the learned CIT(A), we find that this issue is recurring nature. We further find that the coordinate bench of Tribunal in DCIT vs Tata Chemicals Limited, in ITA Nos. 3383/Mum/2015, for assessment year 2002-03, vide order dated 22/04/2019, while deciding similar issue, observed as under:

"11.3 We have heard the rival submissions and perused the relevant materials on record.

As per the decisions filed by the Ld. counsel, we find that the above issues have been decided by the ITAT in favour of the assessee in assessee's own case for earlier assessment year. In the case of Tata Sports Club, similar issue has been decided by the Tribunal in favour of the assessee in AY 1995-96 (ITA No. 3082/M/02, dated 26.07.2006) and AY 1996-97 (ITA No. 6496/M/04, dated 17.08.2007).

In case of Nutan Bal SikshanSangh and Kindergarten Primary School and Mithapur/Kamgar Club, Mithapur, in AY 1992-93 (ITA No. 4442/M/96, dated 04.02.2000), in case of Tata Chem Sports & Cultural Club, Babrala in AY 1995-96 (ITA No. 3082/M/02, dated 26.07.2006), AY 1996-97 (ITA No. 6496/M/04, dated 17.08.2007), AY 1992-93 (ITA No. 4442/M/96, dated 04.02.2000), in case of Flag Day Collection in AY 1992-93 (ITA No. 4442/M/96, dated 04.02.2000), in case of Fort Medical Society in AY 1995-96 (ITA No. 3082/M/2002, dated 26.07.2006), in AY 1996-97 (ITA No.6496/M/04, dated 17.08.2007) and in case of Tata Chem Co-op. Credit Society in AY 1995-96 (ITA No. 3082/M/02, dated 26.07.2006), in AY 1996-97 (ITA No. 6496/M/04, dated 17.08.2007), A.Y. 1992-93 (ITA No. 4442/M/96, dated 04.02.2000), similar issues have been decided by the Tribunal in favour of the assessee.

Facts being similar, we uphold the order of the Ld. CIT(A) and dismiss the 1st ground of appeal."

56. The learned DR could not show any reason to deviate from the aforesaid order and no change in facts and law was alleged in the relevant assessment year. The issue arising in the present appeal is recurring nature and has been decided in favour of the assessee by the decisions of the coordinate bench of the Tribunal in preceding assessment years. Thus, respectfully following the order passed by the coordinate bench of Tribunal in assessee's own case cited supra, we find no infirmity in the impugned order passed by the learned CIT(A) on this issue. As a result, ground no. 1 raised in Revenue's appeal is dismissed."

42. Further in assessee's own case for the immediately preceding assessment years i.e., for A.Y. 2006-07 and 2007-08, vide common order in ITA.No.9057/MUM/2010, ITA No. 6900/MUM/2012 and 8710/MUM/2011 dated 31.03.2023 the Coordinate Bench observed as under: -

21.1. We have heard rival submissions and perused the materials available on record. We find that assessee had made payments to the following clubs / institutions.

Corporate Office

Tata Sports Club - Rs 3,30,000

Mithapur

MithapurNutanBalshikshanSangh - Rs 19,00,000

Kindergarten Primary School - Rs 10,75,000

Babrara

Tatachem D A V Public School - Rs 47,89,989

Tatachem Sports and Cultural Club - Rs 83,260

Payments made to clubs towards entrance

fees and subscription

Wellington Sports club - Rs.8,85,000

Bombay Gymkhana club - Rs. 42,702

Cricket club of India - Rs.30,00,000

Poona club Ltd. - Rs. 3,50,000

Country Club India Ltd - Rs. 70,000

Total Rs 125,25,951

21.2. The said payments were sought to be disallowed by the Id. AO by applying the provisions of section 40A(9) of the Act pursuant to the directions of the Id. DRP. Both the parties mutually agreed that this issue has already been settled in favour of the assessee by the coordinate bench decisions of this tribunal in assessee's own case as under:-

Contribution to Tata Sports Club

Covered by Tribunal order for A.Y.2006-07 supra vide ground No.3

MithapurNutanBalshikshanSangh

Covered by Tribunal order for A.Y.2006-07 supra vide ground No.3

Kindergarten Primary School

Covered by Tribunal order for A.Y.2006-07 supra vide ground No.3

Tatachem D A V Public School

Covered by Tribunal order for A.Y.2006-07 supra vide ground No.3

Tatachem Sports and Cultural Club

Covered by Tribunal order for A.Y.2006-07 supra vide ground No.3

21.3. With regard to payment made to various clubs as detailed above, we find that the Hon'ble Supreme Court in the case of CIT vs. United Glass Manufacturing Co. Ltd reported in 28 taxmann.com 429 had stated that club membership fees paid for employees for seeking membership in the clubs and accordingly payment of entrance fees and subscription made thereon are allowable business expenditure u/s.37 of the Act. Similar propositions were also laid down by the Hon'ble Jurisdictional High Court in the case of Otis Elevator Co. India Ltd. vs. CIT reported 195 ITR 682 (Bom).

21.4. Respectfully following the aforesaid decisions, we direct the Id. AO to delete the disallowance made in this regard. Accordingly, the Ground No. 3 raised by the assessee is allowed.

43. Since the issue is exactly similar and grounds as well as the facts are also identical, respectfully following the above decision in assessee's own case for the immediately preceding i.e., A.Y.2007-08, we allow the ground raised by the assessee.

44. With regard to Ground No. 4 which is in respect of subscription paid to Tata sons Ltd., under the Brand Equity. At the time of hearing, Ld.AR of the assessee brought to our notice that the issue in appeal has been considered by the Co-ordinate Bench of this Tribunal in assessee's own case for the A.Ys. 2001-02 to 2007-08 and Coordinate Bench has

adjudicated and decided the issue in favour of the assessee and against the department. Ld.AR of the assessee prayed that the same decision may be adopted for the year under consideration.

45. On the other hand, Ld. DR has fairly accepted the submissions of the Ld.AR.

46. Considered the rival submissions and material placed on record, we observe from the record that identical issue is decided in favour of the assessee in assessee own case for the A.Y. 2001-02 to 2007-08. We observe in assessee's own case for the immediately preceding assessment years i.e., for A.Y. 2006-07 and 2007-08, vide common order in ITA.No.9057/MUM/2010, ITA No. 6900/MUM/2012 and 8710/MUM/2011 dated 31.03.2023 the Coordinate Bench observed as under: -

"6. The Ground No. 4 raised by the assessee is with regard to the treatment of subscription paid to Tata Sons Ltd under the Brand Equity and Business Promotion Agreement.

6.1. We have heard the rival submissions and perused the materials available on record. We find that the assessee had entered into Brand Equity and Business Promotion (BEBP) Agreement dated 18.12.1998 with Tata Sons Ltd for use of Tata Logo by the assessee, pursuant to which payment has been made by the assessee. This payment was sought to be disallowed by the Id. AO on the ground that the assessee was a Tata Group Company since 1939 and has its own reputation and logo. Hence there is no need to use separate Tata Logo. Accordingly, the Id. AO disallowed

the said payment as not meant for business purposes of the assessee.

6.2. We find that this issue is no longer res integra in view of the decisions of this tribunal in assessee's own case in the following cases :-

ITA No. 6366/Mum/2014 dated 15.09.2017 for A.Y. 2001-02

ITA No. 3383/Mum/2015 dated 22.04.2019 for A.Y. 2002-03

ITA No. 2439/Mum/2011 dated 19.02.2021 for A.Y. 2003-04

ITA No. 2440/Mum/2011 dated 06.07.2022 for A.Y. 2004-05

6.3. The Id. AR also stated that the similar issue has been decided by this tribunal in the case of assessee's own subsidiary Rallis India Ltd case in ITA No. 5701/Mum/2008 for A.Y. 2004-05 ; in the case of BPL Refrigeration Ltd vs ACIT reported in 91 ITD 203 and in the case of Tata Autocomp Ltd in IT(TP)A No. 7596/Mum/2012 dated 12.06.2013.

6.4. Respectfully following the aforesaid judicial precedents, the Ground No. 4 raised by the assessee is allowed."

.....

22. The ground No. 4 & 5 raised by the assessee for A.Y.2007-08 are identical with ground No.4 & 5 raised by the assessee for A.Y.2006-07 supra. Hence, the decision rendered in A.Y.2006-07 shall apply mutatis mutandis for A.Y.2007-08 also. Accordingly, the ground No.4 is allowed and ground No.5 is dismissed as not pressed."

47. Since the issue is exactly similar and grounds as well as the facts are also identical, respectfully following the above decision in assessee's own case for the immediately preceding A.Y.2007-08, we allow the ground raised by the assessee.

48. With regard to Ground no. 5 which is in respect of disallowance of computer upgradation, Ld. AR of the assessee submitted that this ground is not pressed, accordingly the same is dismissed as not pressed.

49. With regard to Ground No. 6 which is in respect of notional loss on Foreign Exchange Fluctuation of FCCB, Ld. AR of the assessee submitted that this ground is not pressed, accordingly the same is dismissed as not pressed.

50. With regard to Ground No. 7 which is in respect of premium payable on redemption of FCCB, Ld. AR of the assessee submitted that this ground is not pressed, accordingly the same is dismissed as not pressed.

51. With regard to Ground No. 8 which is in respect of disallowance of deduction of machinery hire charges, Ld. AR of the assessee brought to our notice that the issue in appeal has been considered by the Coordinate Bench of this Tribunal in assessee's own case for the A.Y.2002-03 and Coordinate Bench has adjudicated and decided the issue in favour of the revenue and against the assessee.

52. On the other hand, Ld. DR has fairly accepted the submissions of the Ld.AR.

53. Considered the rival submissions and material placed on record, we observe from the record that identical issue is decided in favour of the revenue in assessee own case for the A.Y. 2002-03. We observe that in ITA No.2965/MUM/2015 for the A.Y. 2002-03 dated 22.04.2019, the coordinate Bench held as under: --

8.5 We have heard the rival submissions and perused the relevant materials on record. The reasons for our decision are given below.

We refer here to the case laws cited by the assessee before the Ld. CIT(A). In the case of CIT v. IsharDass Tilak Chand (1979) 120 ITR 440 (P&H), the assessee-firm derived income from selling country liquor as licensed contractor. Annual license fee was payable in specified equal instalments. Prescribed percentage was payable in lump sum as security deposit adjustable against license fee arrear or penalty levied for breach of conditions for license. The Government forfeited security deposit against arrears of license fee. The AO added the forfeited amount in assessable income. The Tribunal allowed security deposit adjusted as revenue expenditure in same manner as payment of license fee. The Tribunal also held that forfeiture was not by way of penalty for breach of any term of license. The Hon'ble High Court held that (i) There is no material on record to show that the forfeiture order was not merely a direction for adjustment of the security amount against the arrears of license fee. The Revenue did not suggest before the Tribunal that the failure to pay any installment of license fee entailed a criminal penalty, nor pointed out that there was any other breach of condition of license or any excise law to support its plea that the said forfeiture resulted from a violation of law disentitling the assessee's claim for deduction of the amount as a business expenditure, (ii) The finding given by the Tribunal that the security deposits was adjusted towards the arrears of license fee and the same was not a forfeiture by way of penalty for the breach of any

term of the license etc., was a finding of fact and no question of law arose.

In Thackers H.P. & Co. v. CIT (1982) 134 ITR 21 (MP), the assessee firm, carrying on the business of purchase and sale of tendu leaves, entered into a contract with Orissa Forest Corporation Ltd. for the purchase of tendu leaves and in connection there with, deposited a certain sum as security with the Corporation. As the contract was not fulfilled, the Corporation forfeited the security. For the AY 1974-75, the assessee claimed the security money so forfeited, as a business loss, which was disallowed by the AO. On appeal, the first appellate authority allowed the assessee's claim. On further appeal, the Tribunal restored the order of the AO, holding that the impugned security deposit was in the nature of capital expenditure for commencing the venture and, therefore, could not be deducted as a business loss. On appeal by the assessee, the Hon'ble High Court held that :

"It is well settled that the forfeiture of a security deposit under a contract is a business loss and not a capital loss. The security amount deposited under a contract is not for obtaining the contract but for the due performance of its terms. Moreover, in the instant case, it was obvious that the contract with the corporation was not a new business started by the assessee but was only a venture in the course of business which the assessee was already carrying on and, therefore, it could in no sense be held that the deposit of security was made for acquiring a business. Accordingly, the loss resulting from the forfeiture of security money was a revenue loss."

In CIT v. Textool Co. Ltd. (1982) 135 ITR 200 (Mad), the assessee imported certain items necessary for its manufacturing business under licensing scheme, requiring the assessee to deposit advance premium representing full amount of value of licensed imports with Indian Cotton Mills Federation, with stipulation that if assessee did not utilize full import entitlement, Federation would forfeit premium to the extent of resultant short fall. Owing to business exigencies, the assessee could not fully utilize import entitlements and Federation forfeited part of premium which it wrote off as revenue loss. On appeal by the revenue, the Hon'ble High Court held that:

"when the assessee claims a business loss, the main question to be considered is whether the loss is incidental to the business. Having regard to the facts and findings recorded by it, the Tribunal was correct in coming to the conclusion that the deduction claimed by the assessee in writing off the forfeited amounts was in the course and

incidental to the assessee's business. Accordingly, the impugned amounts were deductible from the total income of the assessee".

In the instant case, in the financial year 1994-95, the assessee entered into sale and lease back agreements with L&T, Bajaj Auto and HDFC Ltd. The lease agreements provided for certain lease deposit and annual rent. During the year under reference, an amount of Rs.2,58,92,853/- was amortized and provided towards lease deposit. We find that on the basis of above facts, the present case is distinguishable from the above case laws relied on by the Ld. counsel.

We are of the considered view that the amount paid as consideration for obtaining the lease is for the acquisition of a capital asset which enables the lessee to carry on its business. It is a capital expenditure. It cannot be split up into the number of years of the duration of the lease in order to claim a proportionate fraction as revenue expenditure each year. The acquisition is of exclusive right or privilege over the lease, it a strong point that the consideration paid is on capital account. Receipts and payments in connection with acquiring or disposing of lease are usually on capital account.

In view of the above, we uphold the order of the Ld. CIT(A) and dismiss the 7th ground of appeal."

54. Since the issue is exactly similar and grounds as well as the facts are also identical, respectfully following the above decision in assessee's own case for the A.Y.2002-03, we dismiss the ground raised by the assessee.

55. With regard to Ground No. 9 which is in respect of deduction under section 80-IA, at the time of hearing, Ld.AR of the assessee brought to our notice that the issue in appeal has been considered by the Co-ordinate Bench of this Tribunal in assessee's own case for the

A.Ys. 2006-07 and 2007-08 and Coordinate Bench has adjudicated the issue in favour of the assessee and against the department. Ld.AR of the assessee prayed that the same decision may be adopted for the year under consideration.

56. On the other hand, Ld. DR has fairly accepted the submissions of the Ld.AR.

57. Considered the rival submissions and material placed on record, we observe from the record that identical issue is decided in favour of the assessee in assessee own case for the A.Y. 2006-07 and 2007-08. We observe that in assessee's own case for the immediately preceding assessment years i.e., for A.Y. 2006-07 and 2007-08, vide common order in ITA.No.9057/MUM/2010, ITA No. 6900/MUM/2012 and 8710/MUM/2011 dated 31.03.2023 the Coordinate Bench observed as under: -

8.2. The audit report in Form 10CCB for the year under consideration is enclosed in page 125 of the paper book. The profit and loss account of the eligible power unit is enclosed in page 133 of the paper book. The workings for deduction u/s. 80IA of the Act are enclosed in page 131 of the paper book.

8.3. For the year under consideration, the sales figure for electricity is derived by multiplying units of electricity produced by the power plant with the fair market transfer price of Rs.4.74 per unit. The rate of Rs.4.74 per unit is derived as a equivalent cost of power per unit if the power would have been purchased from local state

electricity board- i.e. Gujarat State Electricity Board. This is done as per the provisions of section 80(IA)(8) of the Act which provides for adoption of Fair Market Value (FMV) for goods transferred to another business of the assessee.

8.3.1. The sale of steam generated by the power project has been recorded at cost of producing the same. The sale of steam could not be recorded at fair market value as there is no ready market for steam i.e. steam is not a Marketable product.

8.3.2. As far as electricity is concerned, the cost of production of power is arrived at scientifically as per the cost records and the same has been matched against the figure of Sales which is the amount which would be required to be expended if the electricity had to be purchased from Gujarat Electricity Board, as per the provisions of Section 80(IA)(8) of the Act. The saving of cost has been determined as the profit from the industrial unit by the company.

8.3.3. The assessee further drew the attention of the Id. AO to the letter of the CBDT addressed to the IMC dt. 3.10.2001 (submitted vide letter dated 26-10-2010) wherein the issue of allowance of deduction u/s 80(IA) of the Act with respect to captive consumption of power units has been discussed at length.

8.3.4. The cost of the steam generated by the power project is the actual cost of production as per Cost Accounts. The sale of steam generated by the power project has been recorded at cost of producing the same. The sale of steam could not be recorded at fair market value as there is no ready market for steam i.e. steam is not a Marketable product. Hence, there is no profit no loss on steam. In support of the claim, the working sheet of rate of power of Gujarat State Electricity Board was also enclosed.

8.4. We find that the case of the Id. AO is that—

(i) since the said power plant is a captive power plant, deduction u/s.80IA of the Act is not eligible to the assessee;

(ii) the assessee had adopted the rate of Rs.4.74 per unit to book income from sale of power. This is nothing but the rate charged by the Gujarat Electricity Board had it supplied power to the assessee. Hence, the assessee has inflated the profit on sale of power by showing the cost of production at a rate much lower than the one as per the tariff of Gujarat Electricity Board; and

(iii) the assessee has claimed deduction u/s.80IA of the Act on the sale of steam also. This is merely a notional book entry passed by the assessee and accordingly, not eligible for deduction u/s.80IA of the Act.

8.5. We would like to adjudicate each of the aforesaid propositions separately. First, whether deduction u/s. 80IA of the Act would be eligible in respect of captive power plant i.e. power generated in the power plant when captively conceived by other non- eligible units, deduction u/s.80IA of the Act would be eligible for the said power plant. This issue is no longer res integra in view of the decision of the Hon'ble Madras High Court in the case of Tamilnadu Petro Products Ltd. vs. ACIT reported in (2011) 51 DTR (Mad) 67. Similarly, the Hon'ble Delhi High Court in the case of CIT vs. Orient Abrasive Ltd in ITA Nos. 991/2010, 1078/2010, 1077/2010, 1079/2010 and 535/2011 dated 31/07/2014 had also held that assessee would be eligible for deduction u/s.80IA of the Act in respect of captive consumption of power generated from the eligible unit. Respectfully following the aforesaid decisions, we hold that assessee was duly justified in claiming deduction u/s.80IA of the Act for captive consumption of power. In any case, the very same deduction was granted under the same facts and circumstances by the Id. AO himself in A.Y.2001-02. Once, the deduction u/s.80IA of the Act has been granted in the first year of its claim, then in subsequent year, the same cannot be withdrawn unless there are adverse factual developments. In the instant case, there is absolutely no adverse factual development that had been placed on record by the Revenue to justify its withdrawal of deduction u/s.80IA of the Act in the 6th year of its claim of the assessee. Reliance in this regard has been rightly placed by the assessee on the decision of the Hon'ble Jurisdictional High Court in the case of CIT vs. Paul Brothers reported in 216 ITR 548 (Bom).

8.6. It is a fact that the steam generated from the power plant is transferred for usage in manufacturing soda ash and salt. For this transfer of usage of steam from power plant to the chemical plant, the assessee had reflected sale of steam in the profit and loss account of power plant and claimed deduction u/s.80IA of the Act. The steam generated effectively is a by-product of the power plant. Even though this income is booked by the assessee by way of book entry i.e. by booking income in the eligible unit and claiming expenditure in the non-eligible unit, in our considered opinion, the said profit represents profit derived from the power plant which is an eligible undertaking. We find that the assessee for the purpose of determining the value of steam transferred to the noneligible unit, had adopted the cost of production of steam as the sale price. The cost of production of steam has been considered by the assessee by using the cost accounting records which is prescribed

and which is as per the mandate of cost accounting rules which has been consistently followed by the assessee. In this regard, the eligibility of an assessee to claim deduction u/s.80IA of the Act for the sale of steam from power unit to non-eligible unit has been subject matter of consideration by the Co-ordinate Bench decision of this Tribunal in the case of DCW Ltd vs. The Additional Commissioner of Income Tax reported in 37 SOT 322(Mum). The relevant observation of this Tribunal on the impugned aspect of the issue is reproduced hereunder:-

"18.8 The next item of miscellaneous income is the income from sale of steam produced by the assessee. Briefly the facts and nature of steam are that the captive power undertaking also has waste heat recovery boiler, which is part of the power undertaking. The power generated by the running of diesel generating set is used in the manufacture of caustic soda. Running of Diesel Generating Sets produce heat, which is recovered from the waste heat recover boiler in the form of steam. During the year ended March, 2003, the total quantity of steam generated is 1,02,295 MT. The said steam is used as power for the manufacture of PVC and Ilmenite and 6,240 MT was used towards internal consumption. During the year 66,990 MT of steam was consumed in the manufacture of PVC and 29,065 MT was consumed in the manufacture of Ilmenite.

18.9 The submission of the learned AR of the assessee is that since power in the form of steam was generated by the captive power plant and consumed in the manufacture of PVC and Ilmenite, therefore, the assessee is entitled for deduction under section 80-IA. Further, the learned AR submitted that on identical set of facts, the department filed Special Leave Petition before Hon'ble Supreme Court against the judgment of Hon'ble Madras High Court in T.C. No. 1773 of 2008 and vide judgment dated 6th November, 2008, the Apex Court dismissed the department's appeal. In the said judgment Madras High Court dismissed the Department's appeal against the decision of Tribunal holding that the assessee was entitled to claim deduction under section 80-IA of the Act on the value of steam used for captive consumption by the assessee. CIT v. Tanfac Industries Ltd. [S.L.P.(C) No. 18537 of 2009] (319 ITR 8 & 9). In the light of above discussion, we find that the steam produced by the assessee is eligible unit is a bye-product and income from sale of steam is the income derived from industrial undertaking, therefore, deduction under section 80-IA is allow-able. We, accordingly, set aside the order of CIT(A) on this issue and the claim, of the assessee is allowed."

8.7. *In view of the above, we hold that assessee is entitled for deduction u/s.80IA of the Act in respect of sale of steam from its power plant to non-eligible units.*

8.8. *Now coming to the rate per unit of power adopted by the assessee for recognizing income on account of sale of power, we find that assessee had adopted the rate of Rs.4.74 per unit which is the same rate charged by Gujarat Electricity Board on the assessee had the power been drawn by the assessee from the Gujarat Electricity Board Grid. We find that the main grievance of the Revenue is that the cost of production of power for the assessee is less than Rs.4.74 per unit and hence, the assessee is not eligible to claim deduction u/s.80IA of the Act by considering the sale price of Rs.4.74 per unit which is nothing but the price charged on the power supply by Gujarat Electricity Board on the assessee. We find that this issue is no longer res integra by the decision of the Hon'ble Jurisdictional High Court in the case of CIT vs. Reliance Industries Ltd reported in 421 ITR 686 (Bom). The relevant question raised before the Hon'ble Jurisdictional High Court is reproduced as under:-*

(c) Whether, on the facts and in the circumstances of the case and in law, the Id. Tribunal was right in upholding the decision of the Id.CIT(A) who had deleted the addition made by the then AO by restricting the deduction u/s. 80IA at Rs. 48,76,82,681/-as against Rs. 131,43,30,575/- claimed by the assessee?"

8.8.1. *The Hon'ble Jurisdictional High Court disposed of the above question by observing as under:*

4. *Question (c) pertains to the dispute between the department and the assessee regarding the rate at which the electricity generated by one unit of the assessee company and provided to the another be valued. The assessee contended that such valuation should be at the rate at which the electricity distribution companies are allowed to supply electricity to the consumers. The revenue on the other hand argues that the appropriate rate should be the rate at which the electricity is purchased by the distribution companies from the electricity generating companies.*

5. *This controversy arose in the background of the fact that the assessee had set up a captive power generating unit and claimed deduction under Section 80IA of the Income Tax Act, 1961 ("the Act" for short) in respect of the profits arising out of such activity. Obviously, therefore the attempt*

on the part of the assessee was to claim larger profit under the unit which was eligible for such deduction as against this, attempt of the revenue would be see that the ineligible unit shows greater profit.

6. The Tribunal in the impugned judgment extracted extensively from the order of CIT (Appeals) and independent reasons for confirming the same. In such order CIT (Appeals) had placed reliance on an earlier judgment of the Tribunal in case of Reliance Infrastructure Ltd. v. Addl. CIT [2011] 9 taxmann.com 186 (Mum. - Trib.). Learned counsel for the assessee had placed on record a copy of the judgment of the Tribunal in case of Reliance Infrastructure limited. In such judgment an identical issue came up for consideration. The Tribunal by detailed judgment had held and observed as under:—

"44. In the given facts and circumstances of the case, we are of the view that the profits of the business of generation of power worked out by the Assessee on the basis of the price that it paid to TPC for purchase of power continues to be the best basis even after the order of MERC and therefore the same has to be accepted as was done in the past and as approved by the ITAT in Assessee's case. We therefore dismiss ground No.4 of the revenue."

7. Counsel for the assessee pointed out that the judgment of the Tribunal in case of Reliance Infrastructure Ltd. (supra) was carried in appeal by the revenue before the High Court in Income Tax Appeal No.2180 of 2011, such appeal was dismissed making following observations:—

"6. As far as question (d), namely, the claim relating to purchase price from Tata Power Company is concerned and that was for the deduction under Section 80IA, the ITAT in paragraph 21 onwards has noted the factual findings and also referred to the order of the Maharashtra Electricity Regulatory Authority (for short "MERC"). Paragraph 36 set outs as to how the claim arose. The claim has been considered in the light of Section 80IA and particularly proviso and explanation thereto. The Tribunal eventually held that till the Assessment Year 2005-2006, the Revenue considered the rate at which the power was purchased by the Assessee from Tata Power Company as market value. There is nothing brought on record as to how the rate determined by

the MERC is the true market value. The Assessee gave explanation that the rates determined by the MERC do not reflect the correct market rate. The finding is that the mode of computation and deduction under Section 80IA requires no deviation from the past. The findings of fact and to be found in paragraphs 42 to 50 also reflect that the very issue came up for consideration for the Assessment Year 2003-2004. For the reasons assigned by the ITAT and finding that the attempt is to seek reappreciation and reappraisal of the factual data that we come to a conclusion that even question (d) as framed is not a substantial question of law."

8.9. In view of the above, we hold that assessee was justified in recognizing the sale income of power at the rate of 4.74 power unit.

8.10. In view of the independent observations, we find that basis on which the deduction u/s.80IA of the Act has been denied by the Id. AO for the year under consideration has no legs to stand in the eyes of law. Hence, we direct the Id. AO to grant deduction u/s.80IA of the Act in respect of its captive power plant, in accordance with law. Accordingly, the ground No.6 raised by the assessee is allowed."

.....

24. The ground Nos. 7,8 & 9 raised by the assessee for A.Y.2007-08 are identical to ground Nos. 6,7 & 10 raised by the assessee for A.Y.2006-07 supra. Hence, decision rendered thereon in A.Y.2006-07 shall apply mutatis mutandis for A.Y.2007-08 also. Accordingly, the ground No.7 raised by the assessee is dismissed as not pressed; ground No.8 is allowed and ground No.9a is allowed and ground No.9b is dismissed as not pressed.

58. Since the issue is exactly similar and grounds as well as the facts are also identical, respectfully following the above decision in assessee's own case for the immediately preceding A.Y.2006-07, we allow the ground raised by the assessee

59. With regard to Ground No. 10 which is in respect of Post-Retirement Medical Benefits debited to General Reserves, brief facts as summarized by the Assessing Officer are reproduced below: -

"The assessee had claimed deduction of Rs.5.88 crores towards post retirement benefits debited to General Reserves. The assessee in its Submission stated that the same as per the transitional provisions of AS-15 is allowable since the liability is certain accrued.

The assessee's submission was not acceptable as the deduction on account of payment towards employees benefit is allowable deduction only on payment basis as per the provisions of Section 43B. Since the assessee did not make the actual payment, the claim for deduction cannot be allowed.

As the assessee has furnished inaccurate particulars of total income, with a view to willfully evading tax, penalty proceedings u/s. 271(1)(c) are hereby initiated."

60. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the detailed submissions of the assessee, Ld. DRP rejected the submissions of the assessee and sustained the action of the Assessing Officer observing as under: -

11.3 Directions:

We have considered the assessee's submissions and the proposed disallowance by the assessing officer in the draft assessment order. This issue was deliberated upon by our predecessor panel for AY 2007-08 wherein the proposed disallowance by the assessing officer was upheld. As there is no change in facts and circumstances except for the assessee's contention that there is a mistake apparent from record in the quantum of disallowance we uphold the proposed disallowance in principle and direct the assessing officer to verify the exact quantum of disallowance after considering the assessee's submissions in this regard."

61. Aggrieved assessee is in appeal before us raising the issue. At the time of hearing, Ld.AR of the assessee submitted that Assessee Company has a scheme whereby the existing employees & employees who retired from the services of the Company at the age of superannuation of normal retirement date are entitled for free medical check-up and medicines at the Company hospital for the rest of their life. The amount represents the accrual based on an actuarial valuation and expenses incurred during the year. The accrual is determined on the basis of the contractual obligation of the company and since it has been valued on a scientific method by following actuarial basis, it constitutes an accrual of expenses and allowable deduction. Hence it is not a contingent and unascertained liability but the ascertained liability based on the scientific study.

62. Further, Ld.AR of the assessee submitted that during Assessment Year 2007-08, Rs. 36,27,588/- reduction in the opening liability and being credited to the profit and loss account during FY 2006-07, the Assessee has paid necessary taxes on the same which AO has accepted. In effect the AO accepted the movement as revenue in nature and accordingly taxed the same.

63. Further, Ld.AR of the assessee submitted that during Assessment Year 2008-09, the Assessee has debited Profit and Loss account with Rs.1.76 Cr. the additional liability accrued during the year based on the AS-15 Valuation Report. The Assessing Officer disallowed Rs. 1.76 Cr citing that "the payment towards employees' benefit is allowable deduction only on payment basis as per the provisions of Section 43B". As a result the Assessing Officer disturbed the consistency and has changed his position from preceding year and disallowed the additional charged accrued during the year (based on valuation report) and charged to P&L. The liability accrued during the year should be allowed on CONSISTENT basis and section 43B should have no application to such Expenditure.

64. In support of the contentions of the Ld.AR of the assessee, he relied on the following case law: -

- 1. Eveready Industries (India) Ltd. 98 taxmann.com 90 (2018) (Calcutta-H.C.) (para 10- 11) (Refer C.1.-26, pgs 292-295)*
- 2. Mahindra & Mahindra Ltd. 117 taxmann.com 518 (Mum. ITAT) [2020] (para 14 Pg22- 23) (Refer C.L-27, pgs 296-330)*
- 3. Delhi High Court in Ranbaxy Laboratories (334 ITR 341) (para 4-9) (Refer C.L.-28. Pgs331-334)*
- 4. Nalco ITA No.27 of 2006 (2022) (Orissa-H.C.) (para 18-24; Pg 6-7) (Refer C.L. 29. pgs 335-341)*

5. *GlaxoSmithKline Consumer Healthcare Ltd. 64 taxmann.com 84 [2015] (Chandigarh- ITAT) (pg12-18 para 29-35) (Refer C.L. 30, pgs 342-368)*

6. *Rural Electrification Corporation Ltd. ITA Nos.5153& 6327/Del/2014 (pg 4-6: para 4-4.5) [Refer C.L. 31. pgs 369-391]*

7. *Bokaro Power Supply Co. (P.) Ltd (para 3-5.2 page 5) (Refer C.L.- 32, pgs 392-398)* 8. *Mcleod Russel India Ltd. 114-115/Kol/2016 (Para 1- 11) (Refer C.L.- 33, pgs 399-420)*

65. On the other hand, Ld. DR relied on the order of the lower authorities.

66. Considered the rival submissions and material placed on record, we observe from the record that the assessee has claimed expenditure relating to creation of provision based on actuarial basis relating to medical treatment/benefit in the assessee's own hospital to all the employees both retired and existing employees. The AO has invoked provisions of sec.43B to deny the claim of the assessee and the same was sustained by Ld DRP in principal and remitted the verification of claim to AO. However, on careful consideration, the assessee has claimed the expenditure based on Actuarial valuation and accepted accounting method. These expenditures are allowed as regular business expenditure u/s 37 of the Act. We observe that similar claims of the assessee were considered by the Hon'ble Calcutta High court in the case of Everready Industries (India) Ltd., (supra) and held as under: -

"10. As far as question no. (v) is concerned, Mr. Agarwal very strenuously argued that the provisions for Rs. 82, 64, 000/- was a benefit conferred on the employees on superannuation or was a retirement benefit.

11. Analysing the question, we find that this issue does not appear from the question raised. The issue which is raised is whether the provision regarding Rs. 82,64,000/- was in the nature of a contingent liability and thus not allowable. Neither was the issue raised in the way Mr. Agarwal has sought to raise it now, before the Tribunal. Learned counsel tried to submit that on application of Section 40A (7) and Section 36 (1) (iv) of the said Act, these provisions being one for benefit of employees on superannuation ought to be approved by the appropriate authority and in the absence of that the deduction was not admissible. We find on examination of the order of the Tribunal that its decision was based on *Bharat Earth Movers v. CIT* [2000] 112 Taxman 61/245 ITR 428 where the Supreme Court held that the liability was not a contingent liability. In that case, the Supreme Court was concerned with beneficiary schemes for encashment of leave of the assessee company *Bharat Earth Movers*. In this case a scheme for medical benefit post retirement was involved. The tribunal treated the liability as accrued and to be discharged in the future, based on the above Supreme Court decision. In our opinion, this finding of the tribunal is based on standard accounting principles and consequential application of the law laid down by the Supreme Court in *Bharat Earth Movers (supra)*. We find no infirmity in the reasoning or conclusion reached by the Tribunal."

67. Similarly, in the case of *Mahindra & Mahindra Ltd.*, (117 tamann.com 518), the Coordinate Bench of the Tribunal held as under: -

"14. The next issue to be decided in this appeal is with regard to deduction of provision for post retirement scheme for housing in the sum of Rs. 751,45,000 and for post retirement medical schemes in the sum of Rs. 206,30,000.

14.1 We have heard rival submissions and perused the material available on record. We find that during the year under review, the

company has claimed deduction for Rs. 751.45 lakhs towards provision for liability under its Post Retirement Scheme. The liability was quantified based on actuarial valuation. The scheme titled as 'Post Retirement Scheme' is in respect of select cadre of employees who meet certain criteria at the time of retirement from the company and thereafter. The benefit is payable to those employees who have completed at least 10 years of service with the company and 5 years of service in Group Management Board. This is the incentive given to key employees and the purpose is that they should not leave employment and after retirement they should not join the competitors.

14.2 The company made provision for the amounts that would be payable under the post-retirement scheme to the present employees in relation to services rendered in the year under assessment. The provision was made to retain pool of talent and to prevent them from moving to competitors. We find that the assessee had submitted that the liability in respect thereof had been scientifically determined based on actuarial valuation of the same as at the end of the each year. The Copy of the said actuarial valuation report is enclosed in pages 413-427 of the paper book filed before us. It was vehemently stated before the lower authorities that, the liability had indeed arisen during the current year and the said scheme has been formulated wholly and exclusively for the purpose of the business of the company, the said sum of Rs. 751.45 lakhs should be allowed as business expenditure. The Id. AO, however, disallowed the claim holding it to be a mere provision and contingent in nature. Further, he observed that this benefit will be given to retiring employees and not working employees and hence, not allowed as business expenditure.

14.3 Similarly, with regard to provision made for post-retirement medical scheme in the sum of Rs. 206.30 lakhs, the Id. AO disallowed the same on the same ground that it is a mere provision and contingent in nature and that the benefit will be given to retiring employees and not to working employees. The copy of the said actuarial valuation report for post retirement medical benefits is enclosed in pages 429-445 of the paper book filed before us.

14.4 We find that the issue under dispute is squarely covered in favour of the assessee by the coordinate bench decision of this Tribunal in the case of Hindustan Petroleum Corporation Ltd. v. Jt. CIT [IT Appeal No. 1294 (Mum.) of 2011, dated 26-9-2012]. We have gone through the said Tribunal order and find that this issue is squarely decided in favour of the assessee on similar facts and circumstances. We also find that assessee had filed a modified ground of appeal before us on 'without prejudice basis' that in any

case, at least the actual payment made during the year towards post retirement scheme for housing and post retirement medical benefit should be allowed as deduction. We find that assessee is indeed entitled for deduction on provision basis itself and hence, it is not required to adjudicate the modified ground of appeal filed before us and the Id. AO is hereby directed to grant deduction for provision for post retirement scheme for housing in the sum of Rs. 7,51,45,000 and post retirement medical scheme in the sum of Rs. 2,06,30,000 while giving effect to this order. Accordingly, the concise ground No. 12 raised by the assessee is allowed."

68. Respectfully following the above decisions, we are inclined to allow the claim of the assessee after due verification by the AO. In this case the then AO in AY 2007-08 accepted the credit entry and assessed to tax as such. The revenue cannot treat the similar transactions differently in different assessment years. Since the issue under consideration has to be allowed in favour of the assessee, still for the sake of determination of allowability of quantum of expenditures, we direct AO to verify the same considering the fact that AO has recorded that the assessee has debited the expenditure to General Reserves, it may have adjusted the excess provisions as per Accounting Standard, therefore, it needs verification. After verification as per law the same may be allowed. Accordingly, the ground raised by the assessee is allowed for statistical purpose.

69. With regard to Ground No. 11, at the time of hearing, Ld.AR of the assessee submitted that this ground is not pressed, accordingly the same is dismissed as not pressed.

70. With regard to Ground No. 12 which is in respect of weighted deduction in respect of scientific research and development under section 35(2AB) of the Act. At the time of hearing, Ld. AR of the assessee submitted that the assessee has incurred expenditure on research and development and disclosed the same in annual report. Further, he brought to our notice that the issue in appeal has been considered by the Co-ordinate Bench of this Tribunal in assessee's own case for the A.Y. 2007-08 in ITA No 8710/MUM/2011 dated 31.03.2023 and Coordinate Bench has adjudicated the issue and remanded back the matter to the file of the Assessing Officer. Ld. AR of the assessee prayed that similar direction may be issued for the year under consideration.

71. On the other hand, Ld. DR has fairly accepted the submissions of the Ld.AR.

72. Considered the rival submissions and material placed on record, we observe from the record that identical issue is decided in favour of

the assessee in the A.Y.2007-08. While deciding the issue, the Coordinate Bench of the Tribunal in ITA No. 8710/MUM/2011 dated 31.03.2023 and held as under: - -

"27. The ground No.12 is with regard to weighted deduction in respect of scientific research and development u/s.35(2AB) of the Act.

27.1. We have heard rival submissions and perused the material available on record. We find that the assessee vide letter dated 27/12/2010 filed before the Id. AO during the course of assessment proceedings made a claim that it had incurred capital and revenue expenses on research and development which would be eligible for deduction u/s.35(1)(iv) / 35 (2AB) while completing the assessment. The assessee also drew the attention of the Id. AO to page 23 of the annual printed accounts. The break-up of the said expenditure was as under:-

Capital expenses - Rs.3.32 Crores

Revenue expenses - Rs.6.02 Crores

27.2. The Id. AO did not agree to the contentions of the assessee on the ground that this claim is made for the first time before him during the course of assessment proceedings and since the claim was not made either in the return of income or in the revised return of income, applying the decision of the Hon'ble Supreme Court in the case of Goetze India Ltd reported in 284 ITR 323 (SC), denied to grant deduction for the same. We find that the decision of Goetze India Ltd does not prohibit an assessee who has a valid claim to be made before the appellate authorities. Moreover the restriction provided by the said decision, shall not apply to appellate authorities. This is provided in the last paragraph of the decision of the Hon'ble Supreme Court. However, the veracity of the claim had not been examined at all by the Id. AO. Hence, we deem it fit and appropriate, in the interest of justice and fairplay, to restore this issue to the file of the Id. AO for denovo adjudication in accordance with law. The assessee is at liberty to produce fresh evidences, if any, in support of its contentions. Accordingly, the ground No.12 raised by the assessee is allowed for statistical purposes."

73. Since the issue is exactly similar and grounds as well as the facts are also identical, respectfully following the above decision in assessee's own case for the A.Y. 2007-08, we remit this issue back to the file of the Assessing Officer for fresh adjudication in accordance with law, Accordingly, this ground is allowed for statistical purpose.

74. With regard to Ground No. 13 which is in respect of sales-tax exemption benefit, brief facts relating to the ground as summarized by the Assessing Officer and the conclusion reached by the Assessing Officer are reproduced below: -

"16. Sales tax exemption benefit claimed as exempt on the ground of, During the year, the assessee had utilized sales tax exemption of Rs. 17,75,73,424 in view of the Hon'ble ITAT, Mumbai Bench's decision in the case of DCIT v. Reliance Industries Ltd. (273 ITR (AT) 16 Mum)

It is seen that the Hon'ble Supreme Court has set aside the Hon'ble Bombay High Court's judgement in the case of Reliance Industries Limited on the similar issue to be decided afresh. Therefore, the issue of taxability of sales tax exemption benefit has not reached finality.

The assessee during the course of proceeding, argued that the DRP had allowed the similar relief in A.Y.2006-07. But, it is seen that the relief allowed by the DRP was based on Hon'ble Bombay High Court's judgement in the case of Reliance Industries Limited, which had been set aside by the Apex Court.

In view of the above, the Sales Tax exemption benefit claimed as exempt is added to the total income of the assessee

75. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the detailed submissions of the assessee, Ld. DRP rejected the submissions of the assessee and sustained the action of the Assessing Officer observing as under: -

"Objection No 13:

The learned Additional Commissioner of Income Tax erred in adding back the Sales Tax exemption of Rs 17,75,73,424/- to the total income as revenue receipt.

14.1 Facts:

The assessing officer in the draft assessment order has observed that the assessee had utilised sales tax exemption of Rs.17,75,73,424 in view of the hon'ble ITAT Mumbai bench's decision in the case of DCIT vs Reliance Industries Ltd 273 ITR (AT) 16 Mum but the Hon'ble Supreme Court had set aside the hon'ble Bombay High Court's decision in the case of Reliance Industries Ltd on similar issue. Sin the issue had not reached finality, the assessing officer proposed to treat the amount, as revenue receipt and tax accordingly.

*14.2 **Assessee's submissions:***

The assessee has reiterated its submissions as made before the AO.

*14.3 **Directions:***

We have considered the draft assessment order and the assessee submissions. As the matter is subjudice, we decline to interfere in the matter."

76. Aggrieved assessee is in appeal before us raising the issue. At the time of hearing, Ld.AR of the assessee submitted that on 07.05.2000, the Assessee had commenced commercial production in the new unit set up at Mithapur in Okhala Taluka, Jamnagar District of the State of

Gujarat. As per the "New Incentive Policy - Capital Investment Incentive (General) Scheme 1995- 2000" of the Government of Gujarat, the Assessee was entitled to certain incentives including Sales Tax exemption benefit. A bare perusal of the said scheme shows that the object and purpose behind the said scheme was-

- a. to accelerate development of the backward areas of the state*
- b. to create large scale employment opportunities*
- c. to increase total flow of investment to the industrial sector and*
- d. to sustain long term growth and achieve sustainable development. (see the Resolution dated 11.09.1995 of the Industries and Mines Department in the Government of Gujarat in Flap - 10 of the Factual Paper Book).*

77. In this regard, Assessee was given Eligibility Certificate for availing the Sales Tax incentives by the Joint Commissioner of Industries, Industries Commissionerate, where the eligible investment in the fixed assets of the unit was taken at ₹.144.18 crore and it is found to be eligible for claiming the sales tax exemption benefit to the extent of Rs.64.95crore. It is further clarified therein that the said eligibility certificate would be effective from 11.03.2004 upto 06.04.2007 (Eligibility Certificate dated 04.05.2005 at Flap - 10 of the Factual Paper Book).

78. The aforesaid Eligibility Certificate came to be amended by the Industries Commissioner on 31.03.2006, enhancing the period which as per the earlier certificate was from 11.03.2004 to 06.04.2007 to 26.02.2004 to 25.05.2011. Further, the upper limit for such Sales Tax exemption was raised to ₹.144.18 crore (see the Amendment Certificate dated 31.03.2006 at Flap -10 of the Factual Paper Book).

79. During the year under consideration, such Sales Tax exemption benefit was received to the extent of Rs. 17,75,73,424 which was claimed by the Assessee, in its return of income, as a capital receipt not chargeable to tax under the Act. The Assessing Officer has rejected the Assessee's submission in his final assessment order dated 30.11.2012 (paragraph 16 at page 25 of the assessment order). The said treatment has been upheld by the DRP, where the relevant discussion is in paragraph 14 at pages 19 and 20 of their order.

80. Further, Ld.AR of the assessee submitted that it was justified in treating the Sales Tax exemption benefit as a capital receipt for the following amongst other reasons each of which is in the alternative and without prejudice to any others: -

a. It is well settled by now that the nature of an incentive or benefit being capital or revenue is to be decided based on the object and purpose with which the incentive scheme is introduced by the concerned government. In this regard, reliance is placed on judgments of the Hon'ble Apex Court in Ponni Sugars and Chemicals Limited 306 ITR 392, MEPCO Industries Limited 319 ITR 208, Shree Balaji Alloys (2016) 80 taxman.com 239 and Chaphalkar Brothers 400 ITR 279 and the Bombay High Court in Kirloskar Oil Engine Ltd. 364 ITR 88. As stated above, the object and purpose of the New Incentive Policy Capital Investment Incentive (General) Scheme 1995-2000 of the Government of Gujarat was acceleration of development in the backward areas within the state of Gujarat, creation of large scale employment opportunities, increase of the total flow of investment to the industrial sector and sustain long term growth and achieve sustainable development. of a similar scheme of the Government of West Bengal (see the discussion in paragraphs 13 to 18 at pages 17 to 19 of the Tribunal's Order Being Flap 19 of the Factual Paper Book).

81. Further, Ld. AR of the assessee submitted that, the Tribunal in the following cases was concerned with the said Gujarat Scheme and has upheld the assessee's claim that the Sales Tax exemption benefit received under the said scheme would be capital in nature.

i. Sanghi Industries Limited being Order dated 20.04.2018 in ITA No.979/HYD/2017, where the necessary facts are referred to in paragraph 11 at page 6 and the conclusion reached by the Tribunal is in paragraph 9.5 from pages 12 to 15 of the Order (see pages 10 to 38 of the note filed on 25th September 2023),

ii. Ambuja Cement Ltd. being order dated 07.11.2022 in ITA No. 2968/MUM/2015, where the necessary discussion is in paragraphs 17 to 19 at pages 4 to 18 and the discussion on the Gujarat Scheme is at pages 6 and 7 of the Order (see pages 39 to 89 of the note filed on 25th September 2023).

iii. Grasim Industries Ltd. being Order dated 23.06.2023 in ITA No.3439/MUM/2005, wherein the relevant discussion is in paragraphs 50 This principle has also been accepted by the Tribunal in the Assessee's own case for assessment year 2003-04, though in the context to 59 at pages 25 to 30 of the Order. The discussion on the Gujarat Scheme is in paragraph 58 at page 30 (see pages 90 to 139 of the note filed on 25th September 2023),

iv. Indian Petrochemicals Corporation Ltd., being order dated 29.06.2012 in ITA No.664/AHD/2008, where the relevant discussion is in paragraphs 4 to 8 at pages 2 and 3 of the Order (see pages 140 to 171 of the note filed on 25th September 2023),

82. Apart from the above, Ld. AR draw our attention to the DRP's Order dated 27.09.2010 for the assessment year 2006-07, wherein, this aspect with respect to the Scheme of the State of Gujarat stood accepted (see internal pages 11 and 12 thereof at Flap 21 of the Factual Paper Book) and by the AO himself, while passing the draft assessment

order for the assessment year 2007-08 (see internal pages 21 and 22 of the draft assessment order at Flap - 23 of the Factual Paper Book).

83. On the other hand, Ld. DR relied on the order of the lower authorities.

84. Considered the rival submissions and material placed on record, we observe that the assessee has claimed the sales tax exemption benefit under the New Incentive Policy – Capital Investment Incentive (General) Scheme 1995-2000 of Government of Gujarat. The AO has rejected the claim of the assessee relying on the decision of Hon'ble Supreme Court, wherein they have set aside to Hon'ble Bombay High Court for fresh adjudication. Since the issue was not reached finality. However, we observe that this issue has already reached finality in the following cases.

85. The Hon'ble Supreme Court in the case of Ponni Sugars Chemicals Limited (306 ITR 392) considered the similar issue and held as under: -

"2. In the above batch of civil appeals, based on the arguments addressed before us, we are mainly concerned with the following two questions, namely :

"(i) Whether the incentive subsidy received by the assessee is a capital receipt not includible in the total income ?

(ii) Whether the assessee was entitled to exemption under s. 80P(2)(a)(i) of the IT Act, 1961 in respect of interest received from the members of the society ?"

3. At the outset, it may be noted that this batch of civil appeals covers four incentive subsidy Schemes of 1980, 1987, 1988 and 1993. All the four schemes are almost identical. They are different in matter of details. However, in 1980 and 1987. Schemes there is an additional benefit by way of rebate in respect of payment of excise duty which is not there in the remaining two Schemes of 1988 and 1993.

4. With the above preface, we refer to the facts in the case of Salem Co-operative Sugar Mills Ltd. [civil appeal arising out of SLP(C) No. 12355/06].

5. That matter concerns the 1980 Scheme. The dispute pertains to asst. yr. 1986-87. In this matter both the above questions arises for determination. The incentives conferred under that Scheme were twofold. First, in the nature of a higher free sale sugar quota and second, in allowing the manufacturer to collect excise duty on the sale price of the free sale sugar in excess of the normal quota, but pay to the Government only the excise duty payable on the price of levy sugar. In that connection, we quote cl. 7 of the Scheme, which reads as under :

"The beneficiaries of the incentive scheme shall ensure that the surplus funds generated through sale of the incentive sugar are utilized for the repayment of term loans, if any, outstanding from the Central Financial Institutions. The sugar factories should submit utilization certificates annually from chartered/cost accountant, holding certificate of practice. Utilisation certificate in respect of each sugar season during the incentive period should be furnished on or before the 31st December of the succeeding year. Failure to submit utilization certificate within the stipulated time may result not only in the termination of release of incentive free sale quota, but also in the recovery of the incentive free sale releases already made, by resorting to adjustment from the free sale releases of future years."

6. At this stage, we may again note that the 1980 and 1987 Schemes are similar to each other. In the case of Salem Co-operative Sugar Mills Ltd. we are concerned with the Scheme of 1980.

7. On the first question, namely, whether the incentive subsidy received by the assessee is a capital receipt, Shri P.V. Shetty, learned senior counsel appearing on behalf of the Department

(appellant) submitted that the additional Revenue generated by higher free sale sugar quota cannot be considered to be a capital receipt in the hands of the assessee (respondent herein) as held by the High Court. He further contended that similarly retention of the collective excise duty on the sale price of free sale sugar in excess of the normal quota and paying to the Government only the excise duty payable on the price of levy sugar resulted in revenue generation in the hands of the assessee which contention of the Department has been erroneously rejected by the High Court. According to the learned counsel, under the Scheme, there were two distinct concepts, namely, the concept of accrual of income in the hands of the assessee and the concept of application of additional funds generated thereunder. According to the learned counsel, application of additional funds is neither material nor relevant for deciding the character of the incentive subsidy. In this connection, learned counsel placed reliance on the judgment of this Court in the case of Sahney Steel & Press Works Ltd. & Ors. vs. CIT (1997) 142 CTR (SC) 261 : (1997) 228 ITR 253 (SC).

8. Shri Ganesh, learned senior counsel appearing on behalf of the assessee submitted that the benefits were conferred on the assessee under the 1980 and 1987 Schemes, namely, additional price by reason of enhancement of free sale sugar quota, which resulted in the benefit of additional price, which price had to be utilized only for repayment of loans taken by the assessee to establish a new unit or for expanding the existing unit. The said Schemes were not meant for a running unit. The second benefit, according to the learned counsel, lay in the rebate of excise duty under which the assessee was required to pay excise duty on the manufacture of additional quota of free sale sugar. According to the learned counsel, in judging the character of the incentive, the "purpose test" is applicable. In other words, according to the learned counsel, the character of the receipt in the hands of the assessee had to be determined with respect to the purpose for which the subsidy was given and that the point of time at which it is paid or its source or its form was irrelevant. In this connection, learned counsel also places reliance on the same judgment of this Court in the case of Sahney Steel & Press Works Ltd. (supra).

9. The key question which arises for determination is: what is the character of the incentive subsidy under the said Schemes?

10. At the outset, it may be stated that during the relevant year in question, on account of economic factors, namely, high cost, the new sugar factories could not come up as it was not economically viable. Due to high cost, the financial institutions did not come forward to advance loans to the entrepreneurs of new sugar factories. Secondly, the tempo of establishing new sugar factories

received a serious set back, therefore, the Government appointed a Committee known as Sampat Committee to examine the question relating to economic viability of new sugar factories. One of the terms of reference suggested was to work out various incentives for making new sugar factories economically viable units. The increase of the cost of the project during the relevant years was on account of the increase in the cost of plant and machinery. The said Committee gave its report in which the Committee recommended that the economic viability of a factory would mean that the unit should not break even after meeting the working expenses, interest on borrowings, depreciation on plant and machinery, but it should also be able to declare a reasonable dividend on the equity capital. According to the Committee, the factory should be able to generate sufficient funds to repay the instalments of the term loans. Under Para 21.0 the said Committee stated that five possible incentives for making a sugar plant economically viable unit could be provided for, namely, capital subsidy, allowing a larger percentage of free sale sugar, high levy sugar price, allowing rebate on excise duty and remission of purchase tax. In this case, we are concerned with allowability of a larger percentage of free sale sugar and rebate on excise duty. Following the said report of the Sampat Committee, the above Schemes came to be formulated.

11. We have examined in this case the 1980 and 1987 Schemes. Essentially all the four schemes are similar except in the matter of details. Four factors exist in the said Schemes, which are as follows:

(i) Benefit of the incentive subsidy was available only to new units and to substantially expanded units, not to supplement the trade receipts.

(ii) The minimum investment specified was Rs. 4 crores for new units and Rs. 2 crores for expansion units.

(iii) Increase in the free sale sugar quota depended upon increase in the production capacity. In other words, the extent of the increase of free sale sugar quota depended upon the increase in the production capacity.

(iv) The benefit of the scheme had to be utilized only for repayment of term loans.

12. One important aspect may also be noted that in the case of Salem Co-operative Sugar Mills Ltd. we are concerned with notification dt. 15th Nov., 1980. It indicates the above factors of the Scheme. The important point to be noted is that Government of

India, financial institutions as well as the sugar industries are parties to the scheme in the sense that but for the scheme the financial institutions would not have given term loans to set up new units/expansion of the existing units.

13. The main controversy arises in these cases because of the reason that the incentives were given through the mechanism of price differential and the duty differential. According to the Department, price and costs are essential items that are basic to the profit making process and that any price related mechanism would normally be presumed to be revenue in nature. In other words, according to the Department, since incentives were given through price and duty differentials, the character of the impugned incentive in this case was revenue and not capital in nature. On the other hand, according to the assessee, what was relevant to decide the character of the incentive is the purpose test and not the mechanism of payment.

14. In our view, the controversy in hand can be resolved if we apply the test laid down in the judgment of this Court in the case of Sahney Steel & Press Works Ltd. (supra). In that case, on behalf of the assessee, it was contended that the subsidy given was up to 10per cent of the capital investment calculated on the basis of the quantum of investment in capital and, therefore, receipt of such subsidy was on capital account and not on revenue account. It was also urged in that case that subsidy granted on the basis of refund of sales tax on raw materials, machinery and finished goods were also of capital nature as the object of granting refund of sales tax was that the assessee could set up new business or expand his existing business. The contention of the assessee in that case was dismissed by the Tribunal and, therefore, the assessee had come to this Court by way of a special leave petition. It was held by this Court on the facts of that case and on the basis of the analyses of the Scheme therein that the subsidy given was on revenue account because it was given by way of assistance in carrying on of trade or business. On the facts of that case, it was held that the subsidy given was to meet recurring expenses. It was not for acquiring the capital asset. It was not to meet part of the cost. It was not granted for production of or bringing into existence any new asset. The subsidies in that case were granted year after year only after setting up of the new industry and only after commencement of production and, therefore, such a subsidy could only be treated as assistance given for the purpose of carrying on the business of the assessee. Consequently, the contentions raised on behalf of the assessee on the facts of that case stood rejected and it was held that the subsidy received by Sahney Steel could not be regarded as anything but a revenue receipt. Accordingly the matter was decided against the assessee. The importance of the judgment of this Court

in Sahney Steel case (supra) lies in the fact that it has discussed and analysed the entire case law and it has laid down the basic test to be applied in judging the character of a subsidy. That test is that the character of the receipt in the hands of the assessee has to be determined with respect to the purpose for which the subsidy is given. In other words, in such cases, one has to apply the purpose test. The point of time at which the subsidy is paid is not relevant. The source is immaterial. The form of subsidy is immaterial. The main eligibility condition in the scheme with which we are concerned in this case is that the incentive must be utilized for repayment of loans taken by the assessee to set up new units or for substantial expansion of existing units. On this aspect there is no dispute. If the object of the subsidy scheme was to enable the assessee to run the business more profitably then the receipt is on revenue account. On the other hand, if the object of the assistance under the subsidy scheme was to enable the assessee to set up a new unit or to expand the existing unit then the receipt of the subsidy was on capital account. Therefore, it is the object for which the subsidy/assistance is given which determines the nature of the incentive subsidy. The form of the mechanism through which the subsidy is given is irrelevant.

15. In the decision of House of Lords in the case of Seaham Harbour Dock Co. vs. Crook (1931) 16 Tax Cases 333 (HL) the Harbour Dock Co. had applied for grants from the Unemployment Grants Committee from funds appropriated by Parliament. The said grants were paid as the work progressed the payments were made several times for some years. The Dock Co. had undertaken the work of extension of its docks. The extended dock was for relieving the unemployment. The main purpose was relief from unemployment. Therefore, the House of Lords held that the financial assistance given to the company for dock extension cannot be regarded as a trade receipt. It was found by the House of Lords that the assistance had nothing to do with the trading of the company because the work undertaken was dock extension. According to the House of Lords, the assistance in the form of a grant was made by the Government with the object that by its use men might be kept in employment and, therefore, its receipt was capital in nature. The importance of the judgment lies in the fact that the company had applied for financial assistance to the Unemployment Grants Committee. The Committee gave financial assistance from time to time as the work progressed and the payments were equivalent to half the interest for two years on approved expenditure met out of loans. Even though the payment was equivalent to half the interest amount payable on the loan (interest subsidy) still the House of Lords held that money received by the company was not in the course of trade but was of capital nature. The judgment of House of Lords shows that the source of

payment or the form in which the subsidy is paid or the mechanism through which it is paid is immaterial and that what is relevant is the purpose for payment of assistance. Ordinarily such payments would have been on revenue account but since the purpose of the payment was to curtail/obliterate unemployment and since the purpose was dock extension, the House of Lords held that the payment made was of capital nature.

16. One more aspect needs to be mentioned. In Sahney Steel & Press Works Ltd. (supra) this Court found that the assessee was free to use the money in its business entirely as it liked. It was not obliged to spend the money for a particular purpose. In the case of Seaham Harbour Dock Co. (supra) assessee was obliged to spend the money for extension of its docks. This aspect is very important. In the present case also, receipt of the subsidy was capital in nature as the assessee was obliged to utilize the subsidy only for repayment of term loans undertaken by the assessee for setting up new units/expansion of existing business.

17. Applying the above tests to the facts of the present case and keeping in mind the object behind the payment of the incentive subsidy we are satisfied that such payment received by the assessee under the Scheme was not in the course of a trade but was of capital nature. Accordingly the first question is answered in favour of the assessee and against the Department.

86. Further, we have noticed that scheme of Gujarat Government on Sales incentives are considered by the coordinate bench in the case of Grasim Industries Ltd (supra) and decided issue in favour of the assessee, the same is reproduced below:

"50. The issue arising in grounds No. 7.1 and 7.2, raised in assessee's appeal, is pertaining to the taxability of sales tax exemption received by the assessee.

51 The brief facts of the case pertaining to this issue, as emanating from the record, are: During the year under consideration, the assessee availed sales tax exemption benefit of Rs. 117.45 crore, which is already included in the gross sales and profit offered for tax. The assessee claimed the sales tax exemption to be the capital receipt and thus excluded the same from profit while computing the taxable business profits. In this regard, the

assessee made the following submissions during the assessment proceedings:-

—1. The assessee company is inter alia engaged in manufacture of Fibre, Pulp, Chemicals, Fabric, Yarn, Cement and Sponge Iron. The assessee has interest in diverse business. The Company started with a fabric plant in 1950 and today has emerged as one of the largest public company with turnover exceeding Rs.6100 crores. The Company has achieved all round growth by putting up new plants and expanding existing plants.

2. The manufacturing Units are located in various parts of the country details of which has been filed with the return of income and a copy is attached for your ready reference.

3. You will kindly observe that many of the manufacturing Units are located in backward/notified area and the State Government of the respective States have granted subsidy by way of exemption of sales tax payment on sale of finished goods and purchase of raw material and other inputs for promoting setting-up of industries in backward/notified area. Huge capital investment is needed for development of backward / notified areas and since the State Government cannot give subsidy in cash due to recourse constraints, subsidy has been granted by allowing the assessee to retain the sales tax payable to the State Government.

4 A note stating brief description of the various schemes is attached and a copy of the Schemes and eligibility certificates is also enclosed.

A perusal of the Scheme and the purpose for which it was framed by the State shows that the incentive was given for bringing about necessary infrastructure in processing / developing the backward / notified area and thus the incentive is in the capital field and therefore cannot be taxed as revenue receipt. The incentive is based on the amount of investment in fixed assets. It is to induce or motivate the businessman to move and take a risk.

5. The assessee company is liable to pay sales tax on sale of finished goods and purchase of raw material and other inputs as per the applicable sales tax law of the State. However, in accordance with the Scheme, the

assessee has been allowed to retain the same subsidy. The assessee is required to file returns with the concerned authorities, which work out the notional liability of sales tax and complete the assessment. In the books, the total amounts of sale proceeds are credited to profit and loss account, which includes notional liability of sales tax. The amount of notional sales tax liability should have been reduced from the revenue receipts as it is embedded in such receipts, though having character of subsidy. We submit that books of account are not sacrosanct and if true nature of the receipt or payment is different then the same has to be evaluated on the basis of substance of the transaction and in accordance with the law applicable to such transaction.

6. The Hon'ble Supreme Court, in the case of Sahney Steel (228 ITR 253) has held that the decision would depend upon the salient features of the Scheme. If it is given as a general assistance to the assessee to carry on his business or trade, it would be a trading receipt, but if the object of the subsidy, irrespective of its source, is to enable the assessee to acquire new plant and machinery for future expansion of its manufacturing capacity in a backward area, the entire subsidy must be held to be a capital receipt.

Further the Supreme Court in the case of P J Chemicals (210 ITR 830) has held that the incentive granted at the prescribed percentage of fixed capital investment in backward districts was an incentive to encourage entrepreneurs to move to the backward areas was an incentive to encourage entrepreneurs to move to the backwards areas to establish industries and was not a payment to meet any portion of the actual cost of fixed assets u/s 43(1) of the Act.

7. The assessee company submits that the amount of sales tax subsidy received during the previous year Rs. 117.84 crores is capital in nature and should be excluded profits while computing taxable income.

| | | |
|-----|---|-------|
| (a) | Aditya Cement and Bhatinda Grinding Unit (North Zone) | 27.71 |
| (b) | South Cement and Grasim Cement (East and South Zone) | 55.18 |

| | | |
|-----|------------------------|--------|
| (c) | Vikram Ispat, Salav | 33.62 |
| (d) | Elegant Spinners | 0.52 |
| (e) | Vikram Woollens | 0.14 |
| (f) | Birla While GRC, Savli | 0.28 |
| | | 117.45 |

8. Amount of sales tax subsidy for the previous year are as per return filed by the assessee company with the respective state/sales tax authorities and may change on completion of assessment.//

52. The AO, vide assessment order passed under section 143(3) of the Act, held that the State Governments have not given any amount of subsidy either in cash or in-kind to the assessee. It was further held that the object of the government is to grant sales tax exemption to increase sales and not the capital investment in the state. It was further held that under the scheme, the assessee is not required to pay the amount of sales tax and there cannot be any question of receiving the subsidy. Therefore, the AO rejected the claim of the assessee and held that the sales tax exemption received by the assessee is revenue in nature and therefore is part of the taxable profit of the business.

53. The learned CIT(A), vide impugned order, dismissed the ground raised by the assessee on this issue. Being aggrieved, the assessee is in appeal before us.

54. We have considered the submissions of both sides and perused the material available on record. As per the assessee, the object for the grant of the incentive by the State Governments is to promote setting up industries in the backward/notified areas and therefore, the subsidy is capital in nature. In the year under consideration, the assessee received sales tax subsidiary under the following schemes:-

- Packet Scheme of Incentive, 1988 dated 01/10/1988 by State of Maharashtra*
- Sales Tax New Incentive Scheme for Industries 1989, Rajasthan*
- Sales Tax Exemption Scheme (Madhya Pradesh Industrial Policy & Action Plan, 1994)*

- *Sales Tax Waiver Scheme (Package of Fiscal Incentives offered by Government of Tamil Nadu to Industries)*
- *Punjab Industrial Incentive Code under the Industrial Policy, 1996 Haryana Valued Added Tax Act, 2003*
- *Sales Tax Exemption Scheme (M.P. Vanijyikar Adhiniyam, 1994)*
- *Sales Tax Incentive Scheme (Incentives offered by Government of Gujarat under the New Incentive Policy-Capital Investment Incentive (General) Scheme-1995-2000)*

55. We find that the taxability of sales tax exemption received under the schemes of the State of Maharashtra, Haryana, Rajasthan, and Madhya Pradesh came up for consideration before the coordinate bench of the Tribunal in assessee's own case in JCIT v/s Grasim industries Ltd, in ITA No. 2155/Mum/2016 etc., for the assessment years 1996-97 to 2000-01. The coordinate bench vide order dated 29/04/2022 decided a similar issue in respect of these schemes in favour of the assessee and held that the subsidy/incentive received by the assessee is in the nature of capital receipt and not chargeable to tax. We find that after analysing each sales tax subsidy scheme, the coordinate bench held that the only purpose of these schemes is for setting up industries in the respective areas for industrial development in State and also to accelerate development and absolutely not for augmenting the profits of the assessee. The relevant findings of the coordinate bench, in the aforesaid decision, in this regard are as under:-

—5.3.5. From the perusal of the aforesaid schemes together with its objects and preamble, we find that the dominant purpose for which the incentive scheme per se introduced by the respective State Governments was only for the purpose of setting up of industries in the respective areas for industrial development in State and also to accelerate development and absolutely not for augmenting the profits of the assessee.

Effectively, the schemes of various State Governments envisaged the rapid industrialisation, growth and new employment generation in the respective areas which would in turn promote the growth of the State. Hence, it could be safely concluded that subsidy / incentive granted is only for setting up of the units based on the fixed percentage of the capital cost and not for running the business of the assessee. Moreover, even this

subsidy which is determined based on sales tax assessment orders for 9 years, 6 years etc., are subject to maximum outer limit already fixed under the respective schemes. Though the quantification of the subsidy has been made post commencement of business, the measurement of subsidy is immaterial. In our considered opinion, none of the schemes contemplated to finance the assessee in the form of subsidy / incentive for meeting the working capital requirements of the assessee company post commencement of business. Hence, by applying the purpose test, apparently, the subsidy / incentive received in the instant case would only have to be construed as capital receipts not chargeable to income tax. In this regard, we find that Id. AR placed reliance on the decision of Hon“ble Supreme Court in the case of Ponni Sugars and Chemicals Ltd., reported in 306 ITR 392, wherein the incentive conferred under that scheme were two fold. First, in the nature of higher free sale sugar quota and second, in allowing the manufacturer to collect Excise duty on sale price on the free sale sugar in excess of the normal quota, but to pay to the Government only the Excise duty payable on the price of levy sugar. The Hon“ble Supreme Court in para 14 of its decision had held that —character of receipt of subsidy has to be determined with respect to the purpose for which the subsidy is given. The point of time at which the subsidy is paid is not relevant. The source is immaterial. The form of subsidy is immaterial.|| In fact, the Hon“ble Supreme Court while rendering this decision had duly considered its earlier decision in the case of Sahney Steel and Press Works Ltd., reported in 228 ITR 253 and had absolutely no quarrel with that judgement. Rather, it concurred with the decision rendered in Sahney Steel and Press Works Ltd., case. In this regard, it would be relevant to reproduce the operative portion of the decision of Hon“ble Supreme Court in the case of Ponni Sugars and Chemicals Ltd., as under:-

14. The second case is Lincolnshire Sugar Co. Ltd. v. Smart 20 TC 643. In that case it was found that Lincolnshire Sugar Co. Ltd carried on the business of manufacturing sugar from home grown beet. The company was paid various sums under British Sugar Industry (Assistance) Act, 1931, out of monies provided by the Parliament. The question was whether these monies were to be taken into account as trade receipts or not. The object of the grant was that in the year 1981, in view of heavy fall in prices of

sugar, sugar industries were in difficulty. The Government decided to give financial assistance to certain industries in respect of sugar manufactured by them from home-grown beet during the relevant period. Lord Macmillan held that—

"What to my mind is decisive is that these payments were made to the company in order that the money might be used in their business."

He further observed that:

"I think that they were supplementary trade receipts bestowed upon the company by the Government and proper to be taken into computation in arriving at the balance of the company's profits and gains for the year in which they were received."

15. In the case before us, the payments were made to assist the new industries at the commencement of business to carry on their business. The payments were nothing but supplementary trade receipts. It is true that the assessee could not use this money for distribution as dividend to its shareholders. But the assessee was free to use the money in its business entirely as it liked and was not obliged to spend the money for a particular purpose like extension of docks as in the Seaham Harbour Dock Co. 5 case (supra).

16. There is a Canadian case St. John Dry Dock & Ship Building Co. Ltd. v. Minister of National Revenue 4 DLR 1, which has close similarity to the case of Seaham Harbour Dock Co. 's case (supra). In that case it was held that where subsidies were given under statutory authority, the statutory purpose for which they are authorised is relevant and may even be decisive in determining whether it is taxable income in the hands of the recipient. In that case, it was pointed out after discussing the Seaham Harbour Dock Co. 's case (supra) as well as that of Lincolnshire Sugar Co. Ltd. 5 case (supra) that subsidy given by the Canadian Government to encourage construction of dry docks was 'an aid to the construction of dry dock and not an operational subsidy'.

17. This precisely is the question raised in this case. By no stretch of imagination can the subsidies whether by way of refund of sales tax or relief of electricity charges or water charges can be treated as an aid to setting up

of the industry of the assessee. As we have seen earlier, the payments were to be made only if and when the assessee commenced its production. The said payments were trade for a period of five years calculated from the date of commencement of production in the assessee's factory. The subsidies are operational subsidies and not capital subsidies.||

56. *Thus, respectfully following the aforesaid decision, rendered in assessee's own case, we are of the considered view that the sales tax exemption received by the assessee, in the year under consideration, under the similar schemes of the State of Maharashtra, Haryana, Rajasthan, and Madhya Pradesh are in the nature of capital receipts and therefore not taxable in the hands of the assessee.*

57. *As regards the Sales Tax Waiver Scheme (Package of Fiscal Incentives offered by the Government of Tamil Nadu to Industries), forming part of the paper book from pages 289-334, we find that the objective of the scheme was for fostering the pace of industrialisation and to enhance the competitiveness of Tamil Nadu for attracting a large share of industrial projects. Accordingly, the Government of Tamil Nadu introduced the aforesaid scheme which includes capital subsidies and sales tax concessions. From page No. 294 of the paper book, we find that as per the said scheme the State Government has provided a set of waivers and deferrals which can be availed by the investor setting up a mega-investment. It is further provided that the concession is available to industries set up anywhere regardless of its location. In this regard, the assessee has also placed on record the eligibility certificate issued under the aforesaid scheme granted to the assessee's unit located at Reddipalayam Village for the manufacture of cement. Therefore, upon perusal of the aforesaid documents we are of the considered view that the sales tax exemption scheme floated by the Government of Tamil Nadu is of the nature similar to the schemes considered by the coordinate bench in the earlier years, and thus, sales tax exemption received under this scheme is in the nature of capital receipt.*

58. *Similarly, as regards the Sales Tax Incentive Scheme (Incentives offered by the Government of Gujarat under the New Incentive Policy-Capital Investment Incentive (General) Scheme-1995-2000), forming part of the paper book from pages 553-575, we find that the said scheme was to accelerate the development of the backward areas of the State and to create large-scale employment opportunities. Further, under the said scheme, it was also stressed that the need is to increase the total flow of investment to the industrial sector with the proper development of*

infrastructure and human resources to sustain long-term growth and achieve sustainable development. From the perusal of the eligibility certificate issued under the aforesaid scheme, forming part of the paper book on page 577, we find that the same also mentions the total investment in fixed assets by the assessee. Therefore, in view of the above, we find that the sales tax exemption scheme of the Government of Gujarat is of the nature similar to the schemes considered by the coordinate bench in the earlier years, and thus, sales tax exemption received under this scheme is in the nature of capital receipt.

59. As regards the Punjab Industrial Incentive Code under the Industrial Policy, 1996, forming part of the paper book from pages 481-490, we find that the said scheme was formulated with a view to promote growth of the industry in the State and for that purpose it provides various incentives for new industrial units that come into production or undertake expansion on or after 01/04/1996. We find that in the scheme, inter-alia, the capital subsidy is provided to the new large and medium units set up in the notified area as mentioned in Annexure-I of the scheme. We find that under the said scheme certificate of eligibility was also issued to the assessee in respect of Vikram Bathinda Cement Grinding Unit. Thus, the dominant purpose for which this incentive scheme was introduced is also for setting up the industry in the notified area to promote industrial growth in the State. Therefore, we are of the considered view that the sales tax exemption received by the assessee under the scheme is also in the nature of capital receipt. Therefore, in view of the above, the sales tax exemptions received by the assessee under all the schemes of various State Governments, as noted above, are in the nature of capital receipt, and thus, are not taxable in the hands of the assessee. Accordingly, grounds no.7.1 and 7.2 raised in assessee's appeal are allowed."

87. Respectfully following the above decisions, we are inclined to allow the claim of the assessee and direct AO to allow the incentives as capital receipts. Accordingly, the ground raised by the assessee is allowed.

88. With regard to Ground No. 14, which is in respect of contribution to Patterson Memorial School, Kenya, brief facts of the ground are, the assessing officer in the draft assessment order has observed that the

assessee had donated a sum of Rs.1.59 Cr for up-gradation of "Patterson Memorial School" in Kenya where its 100% subsidiary "Magadi Soda Company is based. The assessee claimed it as revenue expenditure whereas the assessing officer held that the payment, which is in the nature of social welfare, is not a regular business expense incurred for carrying out its trade or business, but the payment is an application of income. Since the expenditure was not incurred for the purpose of business, the same was held as not allowable, relying on the judgement of Hon'ble Bombay High Court in the case of Voltas Ltd. (207 ITR 47).

89. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the detailed submissions of the assessee, Ld. DRP rejected the submissions of the assessee and sustained the action of the Assessing Officer observing as under: -

15.2 Directions :

We have considered the draft assessment order and the assessee submissions. We find that the assessee has failed to bring any material on record to substantiate that the expenditure incurred was wholly and exclusively for the purpose of business. We therefore uphold the proposed disallowance by the assessing officer. The objection is rejected."

90. Aggrieved assessee is in appeal before us raising the issue. At the time of hearing, Ld.AR of the assessee submitted that Assessee has a 100% subsidiary company being the Magadi Soda Company in Kenya which is a prestigious project of national importance for Kenya. It is situated close to lake Magadi which has a natural source of soda ash which is one of the products produced by the Assessee. The natural soda ash contained in the water of the said lake is more than 30%. Patterson's Memorial Secondary School was started in the year 2007 after the demise of the then Executive Director of Magadi Soda Company being Mr. Brian Patterson who died from a road accident along the Magadi Road. This school has established in his memory to assist the local community in the area where incidentally the children of the employees of the said company would also be studying. In the course of hearing, the Hon'ble Bench has inquired about the statistics of the children of the employees studying in this school. Since, in this appeal, we are concerned with the assessment year 2008-09, the said information is presently not available. However, pre-dominant purpose behind the setting of the school was welfare and development of the local community. The benefit of this would incidentally also go the employees and their children. It is submitted that measures taken for setting up of educational and medical facilities for the welfare and

development of the community where the manufacturing facility exists is for the smooth carrying on of its business. In this regard, attention is invited to judgment of the Madras High Court in Madras Refinery Limited 266 ITR 170. Prior to the insertion of the limitation by way of Explanation 2 below section 37(1) of the Act by the Finance (No. 2) Act, 2014 w.e.f. 01.04.2015, it has been accepted that expenditure under the Corporate Social Responsibility was an allowable expenditure. This expenditure would be primarily for the community at large and not restricted to the benefit of the employees.

91. In this regard, Ld.AR of the assessee relied on the following case law : -

a) Gujarat Narmada Valley Fertiliser and Chemicals Ltd. 422 ITR 164 (Guj HC)

b) Indian Farm Forestry Development (2019) 101 taxmann.com 169 (Del HC) (see pages 172 to 180 of the note filed on 25th September 2023)

c) Eastern Coalfields Ltd. 450 ITR 184 (Cal HC)

d) Honda Motorcycle and Scooter India (P.) Ltd. (2021) 124 taxmann.com 81 (Del.Tribunal) (see pages 181 to 198 of of the note filed on 25th September 2023)

e) JSW Cement Ltd. (2022) 143 taxmann.com 312 (Mum Tribunal) (see pages 199 to 207of the note filed on 25th September 2023)

Other cases relied upon:

1. SBI 420 ITR 376 (Bom.H.C.) 2019, Pg 3-5 para 4-11 (Refer C.L.-11, pgs 176-182)

2. IPCL ITA No. 1428/2016 dt. 22.01.2019 (Bom.H.C.), Pg 2-3 para 2-4-(Refer C.L.-12pgs 183-185)

92. On the other hand, Ld. DR relied on the order of the lower authorities.

93. Considered the rival submissions and material placed on record, we observe from the records that the assessee has contributed to Patterson Memorial School in Kenya, since the assessee has a 100% subsidiary namely, Magadi Soda Company. It was submitted before us, in order to have good relationship with the Government of Kenya and local community, it has made the above contribution. Further it was submitted that the employees of the subsidiary company can also take benefit. We observe that this welfare activity was carried out by the assessee in the name TATA Group and it is in interest of the assessee since it is 100% subsidiary in Kenya. In our view, the concept of corporate social responsibility is recent development, where the companies has to spend certain percentage of earned profit towards development of local community. However, prior to that, the various corporates were adopting this activities without there being any legislation or commitments towards local communities. The assessee has

carried out this activities towards welfare measure not just for their own employees but also development and welfare of local communities. When new project or industry is set up in remote or new country, these measures plays an important role in developing social harmony and loyalty in the local community. It makes the business develop and prosper. These are the activities which connects the local communities and local government. These measures are required and necessary for the overall welfare of the business which goes in long way in achieving the corporate goal. Therefore, these expenses are necessary and for the purpose of business even though incurred on behalf of fully owned subsidiary, which ultimately benefits the group interest. The similar expenditures were allowed in the following cases i.e., in the case of Gujarat Narmada Valley Fertilizer and Chemicals Ltd., the Hon'ble Gujarat High Court held as under: -

"3.10 The challenge to the order passed by the Appellate Tribunal is on the following grounds:

.....

(b) it is submitted that the learned ITAT has erred in law and on facts in deleting disallowance u/s. 37(1) of the Act, without appreciating that the A.O. had correctly made disallowance of expenses u/s. 37(1) of the Act since the assessee failed to establish that the direct concern and the direct purpose of the expenditure was furtherance of assessee's business and failed to prove that the payments under consideration were made for commercial expediency and for the purpose of assessee's business."

.....

34. Similarly, the view taken by the Bombay High Court in Phaltan Sugar Works Ltd. v. CIT [1995] 215 ITR 377 that once it is established that there was nexus between the expenditure and the purpose of the business (which need not necessarily be the business of the assessee itself), the Revenue cannot justifiably claim to put itself in the arm-chair of the business or in the position of the board of directors and assume the role to decide how much is reasonable expenditure having regard to the circumstances of the case. No businessman can be compelled to maximize his profit. The Income-tax authorities must put themselves in the shoes of the assessee and see how a prudent businessman would act. The authorities must not look at the matter from their own view point but that of a prudent businessman. As already stated above, we have to see the transfer of the borrowed funds to a sister concern from the point of view of commercial expediency and not from the point of view whether the amount was advanced for earning profits."

....

9.7 In Madras Refineries Ltd. (supra), the Madras High Court observed as under:

"As a good corporate citizen and as a measure of gaining goodwill of the people living in and around its industry which is to some extent a polluting industry, it provided funds for establishing drinking water facilities to the residents in the vicinity of the refinery and also provided aid to the school run for the benefit of the children of those local residents. It incurred an expenditure of Rs. 15,32,000 for that purpose.

The Assessing Officer declined to allow that expenditure on the ground that it was not an item of expenditure incurred by the assessee for earning the income earned by it in that year.

On appeal, the Commissioner held that the assessee may have been obliged to incur that expenditure for the good of and in the interest of the community in and around its place of business, and that activity was one which was capable of being regarded as an activity for the promotion of its business. He, however, without assigning any reason held that only a sum of Rs. 5 lakhs out of the sum claimed, was to be allowed as a deduction.

On further appeal to the Tribunal, the Tribunal, after examining the records placed before it and having been satisfied that the money had in fact been spent in the

manner claimed by the assessee, held that winning the goodwill of the people of the locality, helps in boosting the business in many ways. It allowed the entire amount claimed as a deduction.

The concept of business is not static. It has evolved over a period of time to include within its fold the concrete expression of care and concern for the society at large and the people of the locality in which the business is located in particular. Being known as a good corporate citizen brings goodwill of the local community, as also with the regulatory agencies and the society at large, thereby creating an atmosphere in which the business can succeed in a greater measure with the aid of such goodwill. Monies spent for bringing drinking water as also for establishing or improving the school meant for the residents of the locality in which the business is situated cannot be regarded as being wholly outside the ambit of the business concerns of the assessee, especially where the undertaking owned by the assessee is one which is to some extent a polluting industry."

9.8 In Cheran Transport Corporation Ltd. (supra), the Madras High Court observed as under:

"However, we may incidentally add that the Supreme Court, while dealing with a business loss as distinguished from a business expenditure has laid down, approving the earlier decisions, including that of the Orissa High Court in CIT vs. Industry & Commerce Enterprises (P) Ltd. [1979] 118 ITR 606 that where Government bonds, as securities, were purchased by the assessee with a view to increase his business with the Government or with the object of retaining the goodwill of the authorities for the purpose of his business, the loss incurred on the sale of such bonds or securities was allowable as business loss. In that case, according to the statement of case drawn up, the assessee was told that if it subscribed for the Government bonds, preferential treatment would be granted to it in the placing of orders for motor vehicles required by the various Government departments. However, it must be stated that the aspect of contravention of public policy or contravention of any law, was not considered in the abovesaid Supreme Court case also. Anyway, in view of the factual difference between CIT vs. Kodandarama & Co. [1983] 144 ITR 395 (AP) and the present case, we reiterate that CIT vs. Kodandarama & Co. [1983] 144 ITR 395 (AP) is not applicable to the present facts."

9.9 In *Chemicals and Plastics India Ltd. (supra)*, the Madras High Court, after referring to various other decisions, held as under:

"6. The question whether a particular expenditure is a revenue expenditure or a capital expenditure is a vexed question. The line of demarcation is often found to be a very thin one and each case has to be decided on the facts and circumstances. In fact the trend of judicial decisions show a progressive liberal view on the concepts to treat many an item as revenue expenditure with regard to which a contrary conclusion could have been reached. Hidayathullah J. in the decision reported in [1962] 44 ITR 689 (SC)(K.T.M.T.M. Abdul Kayoom v. CIT) held that each case depends on its own facts and close similarity between one case and another is not enough, even a significant detail may alter the entire aspect. Hidayatullah J. in the said decision, also observed as follows:

" What is decisive is the nature of business, the nature of the expenditure, the nature of the right acquired, and their relation inter se, and this is the only key to resolve the issue in the light of the general principles, which are followed in such cases."

7. In the case reported in [1969] 72 ITR 137 (Mad)(CIT v. Ashok Leyland Ltd.) which was affirmed by the Supreme Court in [1972] 86 ITR 549 (CIT v. Ashok Leyland Ltd.), explaining the position of law, this court stated as follows (page 143):

"The facts of each case, the attendant circumstances revolving around the expenditure, the aim, object and purpose of the same, their impact on the assessee, particularly in matters relating to the future of the assessee's trade and business, whether it could be sustained on ordinary canons of commercial expediency simpliciter, whether it is a step-in-aid of future expansion or prolongation of life of an existing business, whether it is to secure an enduring benefit, whether the expenditure constitutes conceivable nucleus to form the foundation for the posterior profit earning, whether the expenditure could be viewed as an integral part of the conduct of the business and to avoid in-roads and incursions into its concrete present and potential future, are all some of the main incidents which have a bearing on the decision whether, in a given case, the expenditure is capital or chargeable to revenue. On the whole, an objective application of the judicial mind to the facts of each case is necessary."

8. *The approach, hence, needs to be that of a practical and prudent businessman rather than from the Revenue's strict classification of a right. As the Supreme Court held in the decision reported in [1997] 223 ITR 101 (Sri VenkataSatyanarayana Rice Mill Contractors Co. v. CIT), what is to be seen is not whether the payment was compulsory for the assessee to make or not. The correct test is that of commercial expediency. The apex court considering the various decisions held that any contribution made by the assessee to a fund which is directly connected or related to the carrying on of the assessee's business or which results in benefit to the assessee's business, has to be regarded as a deduction allowable under section 37 of the Income-tax Act, 1961. Although the case related to a contribution to a public welfare fund, the ratio decidendi will guide the decision in this case too.*

9. *It may be noted that in the decision reported in [2004] 266 ITR 170 (Mad)(CIT v. Madras Refineries Ltd.), while considering a claim of the expenditure incurred by an assessee providing drinking water facility as well as establishing or improving the school meant for the residents in the locality, a Division Bench of this court, held that the amount spent could not be regarded as being wholly outside the ambit of the business concerns of the assessee. The Division Bench held as follows (headnote):*

"The concept of business was not static. It has evolved over a period of time to include within its fold the concrete expression of care and concern for the society at large and the people of the locality in which the business is located, in particular. Being known as a good corporate citizen brings goodwill of the local community, as also with the regulatory agencies and the society at large, thereby creating an atmosphere in which the business can succeed in a greater measure with the aid of such goodwill."

10. *The facts in this case before us stand on a stronger footing, since the contribution made by the company is for the Chamber of commerce whose activities are closely linked with the welfare of the corporate entities who are members therein and whose interest are taken care of by the Chamber of Commerce, irrespective of whether the expense incurred is compulsory or otherwise. Hence, considering the fact that the payment is made for the purpose of the business, it satisfies the commercial expediency test to accept the case of the assessee. In the circumstances, we do not find any justification to accept the case of the Revenue that the provisions of section 137 have to be viewed in a very strict manner.*

It may be noted that section 137 itself is concerned with "an expenditure laid out or expended wholly or exclusively for the purpose of the business or profession" to qualify for deduction. With the necessity no longer a valid test, we reject the Revenue's appeal."

....

10. Thus, the sum and substance of the principle discernible from the above noted decisions is that the concept of business is not static. It has evolved over a period of time to include within its fold the concrete expression of care and concern for the society at large and the people of the locality in which the business is located in particular. The assessee- company in the case on hand is engaged in the business of manufacturing chemicals and chemical products. It has been fairly admitted by the learned counsel appearing for the assess-company that its client is a polluting company. The assessee-company is conscious of its social obligations towards the society at large. The assessee-company is a Government undertaking and, therefore, is obliged to ensure all the protective principles of State policy as enshrined in the Constitution of India. The moneys has been for various purposes as enumerated above cannot be regarded as outside the ambit of the business concerns of the assessee. The approval needs to be that of a practical and prudent businessman rather than from the Revenue's strict classification of a right. The correct test should be of commercial expediency and not whether the payment was compulsory for the assessee to make or not.

10.1 The Supreme Court in Panipat Woollen & General Mills Co. Ltd. AIR 1986 SC 2082 has held that it is not open to the court to go behind the commercial expediency which had to be determined from the point of view of a businessman. The test of commercial expediency cannot be reduced in the shape of a ritualistic formula, nor can it be put in a water-tight compartment so as to be confined in a straight jacket. The test merely means that the court will place itself in the position of a businessman and find out whether the expenses incurred could be said to have been laid out for the purpose of the business or the transaction was merely a subterfuge for the purpose of sharing or dividing the profits ascertained in a particular manner. If the expenses incurred amount to a profit of an enduring nature they may be treated as capital expenditure, whereas if the expenses merely serve to promote or increase the commercial activity they may amount to an expenditure which is incurred for the purpose of the business.

10.2 The question whether a particular expenditure is a revenue expenditure or a capital expense is a vexed question. The line of

demarcation is often found to be as the thin one and each case has to be decided on the facts and circumstances.

10.3 In view of the aforesaid discussion, we have reached to the conclusion that the order passed by the Appellate Tribunal is just and proper and needs no interference in the present appeal at our end.

94. Respectfully following the above decision, we are inclined to direct AO to allow the above contribution to the school as allowable expenditure. Accordingly, the ground raised by the assessee is allowed.

95. With regard to Ground No. 15, which is in respect of write off of new projects on same line of business, brief facts relating to the ground as summarized by the Assessing Officer that assessee has claimed Projects written off of Rs.2.53 crores and before Assessing Officer on this issue, the assessee vide letter dated 23.12.2011 has submitted as under:

During the year 2006-07, TCL worked on "Project Victoria" basically a project in Tanzania close to Lake Natron for establishment of Soda Ash Plant A joint Venture Agreement was signed between TCL and Government of Tanzania. For the project initial studies like environment impact assessment were taken up.

Lake Natron is a huge natural lake and the water contains more than 30% of soda Ash. It has natural soda ash and perhaps the world's biggest soda ash reservoir. Tanzania Government said that this will be their national importance project to manufacture Soda Ash

We would like to inform you that TCL is in the Soda Ash business from 1939 and manufacturing Soda Ash almost 7 lakh to 8 lakh tons per year at its Mithapur Plant in Gujarat by synthetic process

It acquired Brunnermond Group, U.K. which also has a Soda Ash Plant Brunnermond Group. U.K. also has another Soda Ash Plant in Magadi, Kenya, which is also based on natural soda ash

TCL further acquired interest in GCIP, US which has huge Soda Ash reserves and the Soda Ash is manufactured there by mining.

To expand further the soda ash business this project was signed with Tanzania Government However environmentalist objected to this project saying that if the soda ash plant comes up there, it will spoil the natural habitat and flamingos

Environment Impact Assessment and other agencies certified that it will not have any impact on natural habitat but considering the objection of environmental group. TCL finally decided to give up this project.

During the year 2006-07 and 2007-08, TCL incurred total expenses of Rs.2,53,08,210 which was basically for preliminary studies, travel expenses for the Soda Ash Project There is no acquisition of fixed assets.

We enclose the copy of press release in this regard appearing in Hindustan Times Newspaper on 22.05.2008 in this regard. We also enclosed a note of Managing Director dated 31.10.2007 about Lake Natron Project.

We consider this amount as allowable business expenditures as it was incurred for the purpose of expansion in existing line of business We rely on the following judgements:

- a. Indu Rama Synthetics (D) Ltd-333 ITR 18 (Delhi)*
- b. CIT vs Priya Village Roadshows Ltd 332 ITR 594(Delhi)*
- c. CIT vs Graphite India Limited 221 ITR 420(Cal)"*

96. After considering the above submissions, AO rejected the same and disallowed the same with the following observations:

In the assessee's case the issue involved is not whether the expenditure incurred is on a new line of business or is it the extension of the same business. The main issue is whether the capital expenditure incurred on a new project can be treated as revenue expenditure once the project is discontinued or abandoned

for whatever reason The expenditure incurred by the assessee is essentially in the nature of capital expenditure to begin with The expenditure incurred for these projects by the assessee company was in order to decide whether to acquire some profit making assets for the purposes of its business, which would be of an enduring nature. The nature of the expenditure incurred is intrinsically capital in nature. These projects if they were to be completed would have undoubtedly be an item expenditure that would have gone to create capital assets, which would be eligible for depreciation under the Income Tax Act. The preliminary expenditure incurred cannot be anything other than a capital expenditure as it would go to only add to the capital of the projects. It was clearly an expenditure incurred for ascertaining whether to acquire new assets of some durability for the purposes of earning profit. The following judgments clearly support the above view:

(i) CIT v. J.K.Chemicals Ltd. [207 ITR 985 (Bom)]

(ii) CIT v. Zenith Steel Pipes & Industries (315 ITR 95 (Bom.))

(iii) Malabar & Pioneer Hosiery Pvt. Ltd. VsCIT (2008) 302 ITR 72 (Ker)

(iv) Century Spinning & Manufacturing CoLtdVsCIT 128 CTR 317 (Bom)

Therefore, the assessee's claim of write off of expenditure of Rs.2.53 crores incurred in relation to projects written off is disallowed as these expenses constitute capital expenditure and are not deductible from the income of the assessee as per the provisions of the Income Tax Act.

97. Aggrieved assessee preferred objection before Ld. DRP and filed detailed submissions. After considering the detailed submissions of the assessee, Ld. DRP rejected the submissions of the assessee and sustained the action of the Assessing Officer observing as under: -

16.2 Directions:

We have considered the draft assessment order and the assessee's submissions We find that the assessee has failed to bring any material on record to substantiate that the expenditure incurred was not in the nature of capital expense but of revenue expense.

Also, these projects if they were to be completed, would have undoubtedly be an expenditure that would have gone to create capital asset and would be eligible for depreciation under the I.T. Act. The preliminary expenditure cured cannot be anything other than a capital expenditure, as it would go only to add to the capital of the projects. Further, we also find that the assessee's main business interests are in Kenya whereas this project was undertaken in Tanzania. We therefore uphold the proposed disallowance by the assessing officer. The ground is rejected.

98. Aggrieved assessee is in appeal before us raising the issue. At the time of hearing, Ld.AR of the assessee submitted that, one of the product manufactured and produced by the Assessee is soda ash. The Assessee is in the soda ash business from the year 1939 and is presently manufacturing soda ash of almost 7 to 8 lakh tons per year at its Mithapur Plant in Gujarat, but by the synthetic process. In May 2005, the Assessee had acquired 1/3rd equity stake in Indo Maroc Phosphore S.A., Moroco. In the financial year 2005-06, it had acquired stake in Brunner Mond Group in the U.K. which had a soda ash plant in the U.K. as well as held 100% stake in the Magadi Soda Company in Kenya. Further, during the financial year 2007- 08, it acquired interest in General Chemicals Industrial Products Inc. in the USA which was again engaged in similar business. Emphasis has been laid on this fact to substantiate that the Assessee is already carrying on the businesses of manufacture, production and sale of soda ash directly or through its

subsidiaries. Hence, any further expansion would be in the same line of business.

99. With a view to expand its business, the Assessee had signed an agreement with the Government of Tanzania for Project Victoria' close to lake Natron. Lake Natron is a huge natural lake where the water contains more than 30% of soda ash. It is perhaps the world biggest soda ash reservoir. For this purpose, it carried out the environment impact assessment where the concerned agencies also certified that it will not have any impact on the natural habitat associated with the lake. However, considering the objections raised by the environmental groups concerning the said lake, it finally decided to give up this project. In respect of this project it had incurred total expenses of Rs.2,53,08,210 basically concerning professional fees for preliminary studies, travel expenses and other incidental expenses (refer the details in Flap 13 of the Factual Paper Book).

100. Further, Ld.AR of the assessee submitted that it is well settled by now that when the assessee incurs an expenditure in respect of a project in the same line of business which later on is abandoned. The

expenditure would be allowable under section 37(1) of the Act. In this regard, he relied on the following case law: -

i. CIT v. Idea Cellular Ltd. (2016) 76 taxman.com 77 (see pages 208 to 211 of the note filed on 25th September)

ii. PCIT v. Trigent Software Ltd.(2023) 147 taxman.com 52 (see pages 212 to 216 of the note filed on 25th September 2023) and

iii. CIT v. Manganese Ore India Ltd. 384 ITR 413.

101. In view of the above, it is submitted that the said project related expenditure may be allowed as a deduction.

102. Further, Ld.AR of the assessee brought to our notice the decision rendered by the Tribunal in assessee's own case for the A.Y. 1990-91 in ITA/4568/M/03 dated 10.11.2015 Pg 77-81, Para 39 (Gr. No. 16-iii) and for the A.Y. 1990-91, OGE to ITAT order passed by Assessing Officer dt.04.03.2016, (Refer Flap no. -15 of Factual Paper Book) and submitted that department didn't raise this issue before High Court, however on other grounds, the appeal of the revenue was quashed because of low tax threshold limit.

103. On the other hand, Ld. DR relied on the order of the lower authorities.

104. Considered the rival submissions and material placed on record, we observe that the assessee has incurred certain expenditure to commence a project in Tanzania but due to environment concerns the same was dropped. However, the assessee has incurred certain expenditure towards project feasibility and travelling expenses were incurred and due to abandonment of the project, these expenses has to be written off. The issue is whether these expenses are revenue or capital in nature. The similar issue was considered by the Hon'ble Jurisdictional High Court in the case of CIT v. Idea Cellular Ltd., (2016 76 taxman.com 77) and held as under: -

"9. We have carefully perused the memo of the appeal. We have also perused the order of the assessing officer and that of the first appellate authority. Mr. Malhotra has elaborately taken us through these orders to submit that the assessing officer found from the record itself and particularly from a document, namely, a letter or response from the assessee that the purpose of the expenditure cannot be said to be other than bringing up a capital asset into existence. The fact that later on the site was not chosen for hoisting the tower is immaterial. However, we find that the tribunal applied the correct test. The tribunal found that there is no dispute that the expenditure in question was incurred for the purpose of construction of a cellular tower, but the project was then abandoned due to the reason that the site was not suitable. The reasons assigned by the assessing officer and the first appellate authority are unsustainable, according to the tribunal for the simple reason that cellular towers were being erected for the purpose of assessee's own business of providing cellular services to the customers. The towers are meant for the business of providing cellular services. It is by utilising these towers that such services are provided. It is not an independent source of income. It is only to make the cellular services provided more efficient, convenient and profitable. When the towers are not exclusively meant for leasing out to third parties for earning the revenue, but used for

transmission of telephone signals of assessee's own cellular services, then, it cannot be said that the towers, which are used for the assessee's own business, are new source of income. A cellular tower can be a new independent source of income, if it is erected exclusively for leasing out to the other operators. However, on facts, this was not the position and the tribunal, therefore, rightly concluded that in series of decisions, the High Courts and the Hon'ble Supreme Court of India has laid down the principle that if an expenditure is incurred for doing the business in a more convenient and profitable manner and has not resulted in bringing any new asset into existence, then, such expenditure is allowable business expenditure. In the present case, no new business was set up, but towers in addition to which were already set up were proposed at site, which project was later on abandoned.

10. We do not find that the tribunal has committed any perversity or applied incorrect principles to the given facts and circumstances. When the facts and circumstances are properly analysed and correct test is applied to decide the issue at hand, then, we do not think that questions (a) and (b), as pressed, are substantial questions of law. The appeal is devoid of merits and it is dismissed. There would be no order as to costs."

105. Further, the Hon'ble Jurisdictional High Court in the case of PCIT v. Trigent Software Ltd., (supra) held as under: -

"13. Applying the ratio of the aforementioned judgments in the present case, it can be seen that the appellant is admittedly in the business of development of software solution and management, and therefore, it's endeavour to develop a new software was nothing but an endeavour in its existing line of business of developing software solutions. Admittedly, the product which was sought to be developed, never came into existence and the same was abandoned. No new asset came into existence which would be of an enduring benefit to the assessee, and therefore, in these circumstances, the expenditure could only be said to be revenue in nature.

14. We are of the view that the view already expressed by the ITAT in the order impugned requires no interference. We find no merit in the present appeals, and the same are accordingly dismissed.

106. Therefore, respectfully following the above decisions, we are inclined to allow the claim of the assessee that these project expenditures are revenue in nature once the project is abandoned. Accordingly, the ground raised by the assessee is allowed.

107. With regard to Ground No. 16 which is in respect of adjustment to book profits of wealth tax and doubtful debt, Ld. AR of the assessee submitted that this ground is not pressed, accordingly the same is dismissed as not pressed.

108. Further assessee has raised following Supplementary grounds in its appeal: -

"1. Transfer Pricing adjustment.

1.1 The Transfer Pricing adjustments are bad in law, illegal, without/in excess of jurisdiction, contrary to statutory provisions (including sections 4, 5, 9, 92C, 92CA, etc.), contrary to principles of natural justice and therefore the said adjustments should be deleted and quashed.

1.2 The Learned Assessing Officer committed a gross error of law and fact in not applying his mind and examine the issue of Transfer Pricing under the relevant statutory provisions.

1.3 The Transfer Pricing adjustments made by the Assessing Officer are completely violative of the statutory provisions, inter alia, on the grounds that the Learned Assessing Officer failed to arrive at a prima facie belief requiring a reference to the Transfer Pricing Officer and without being satisfied that it is necessary and expedient to make a reference to the Transfer Pricing Officer.

1.4 The Learned Assessing Officer committed gross error of law and fact in making an automatic reference to the Transfer Pricing Officer without his own independent application of mind and therefore the proceedings before the Transfer Pricing Officer are bad in law, illegal, without/in excess of jurisdiction requiring the quashing of the Order passed by the Transfer Pricing Officer and the consequential adjustments made in the Assessment Order.

1.5 The proceedings before the Transfer Pricing Officer and his Order and consequential adjustments are bad in law, illegal and contrary to the statutory provisions since the Commissioner of Income-tax granted an approval in a mechanical manner without an independent application of mind.

1.6 The Transfer Pricing adjustments made in the Assessment Order are bad in law and illegal and contrary to the statutory provisions because the Learned Assessing Officer and the Learned Commissioner of Income-tax did not examine the Transfer Pricing Reports and other documents and material and did not apply their minds to such statutory evidence. The Learned Assessing Officer and the Learned Commissioner of Income-tax did not discharge their necessary respective judicial functions conferred on them by the statute and this has totally vitiated the Transfer Pricing adjustment.

1.7 The Transfer Pricing adjustments are bad in law and illegal in as much as the conditions laid down in section 92C(3) are not satisfied before the passing of the final Assessment Order.

1.8 On the facts and in the circumstances of the case, Transfer Pricing adjustments cannot be made without arriving at the finding that the intention of the assessee was to evade tax or manipulate prices or shift profits outside of India. Further, such finding of tax evasion and of shifting of profits is a condition precedent to making the Transfer Pricing adjustments.

2. The Transfer Pricing Order passed by the Additional Commissioner of Income Tax (Transfer Pricing) is illegal, bad in law, without authority of law, contrary to the statutory provisions and therefore, the whole order is vitiated and unsustainable, and accordingly, the resultant Transfer Pricing Adjustment made by the Assessing Officer, and included in the Assessment Order, should be deleted and quashed.

3. The Assessment Order passed by the Additional Commissioner of Income Tax is without jurisdiction, illegal, bad in law and contrary to legal provisions and therefore the entire order should be quashed."

109. With regard to supplementary additional Grounds raised by the assessee, Ld. AR of the assessee submitted that these grounds are not pressed, accordingly the same are dismissed as not pressed.

110. In the result, appeal filed by the assessee is partly allowed.

Order pronounced in the open court on 10th November, 2023

Sd/-
(VIKAS AWASTHY)
JUDICIAL MEMBER

Mumbai / Dated 10.11.2023
Giridhar, Sr.PS

Sd/-
(S. RIFAUR RAHMAN)
ACCOUNTANT MEMBER

Copy of the Order forwarded to:

1. The Appellant
2. The Respondent.
3. CIT
4. DR, ITAT, Mumbai
5. Guard file.

//True Copy//

BY ORDER

(Asstt. Registrar)
ITAT, Mum