

IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCH "I", MUMBAI
BEFORE SHRI VIKAS AWASTHY, JUDICIAL MEMBER AND
SHRI GAGAN GOYAL, ACCOUNTANT MEMBER

ITA No. 3377/Mum/2006 (A.Y.1998-99)

Standard Chartered Bank

Taxation Department, 23-25,
M. G. Road, 3rd Floor, Fort,
Mumbai-400 001
PAN: AABCS4681D

..... Appellant

Vs.

DDIT (Intl. Tax)-2(1)

Scindia House, Ballard
Estate, N. M. Marg,
Mumbai-400 038

..... Respondent

&

ITA No. 3364/Mum/2006 (A.Y.1998-99)

DDIT (Intl. Tax)-2(1)

Scindia House, Ballard
Estate, N. M. Marg,
Mumbai-400 038

..... Appellant

Vs.

Standard Chartered Bank

Taxation Department, 23-25,
M. G. Road, 3rd Floor, Fort,
Mumbai-400 001

PAN: AABCS4681D Respondent
Appellant by : Shri Madhur Agarwal, Ld. AR
Respondent by : Shri Anil Sant, Ld. DR
Date of hearing : 27/09/2023
Date of pronouncement : 13/11/2023

ORDER

PER GAGAN GOYAL, A.M:

These cross appeals by Assessee and Revenue are directed against the order of Ld. CIT (A)-V, Mumbai, dated 22/03/2006 passed u/s. 250 of the Income Tax Act, 1961 (in short 'the Act') for A.Y. 1998-99. The assessee has raised the following grounds of appeal:-

1. DISALLOWANCE OF PAYMENTS MADE TO MASTER CARD / VISA INTERNATIONAL - Rs. 2,07,41,569/- (Pages 15 to 18 of CIT (A)' order)

a) The learned CIT (A) erred in confirming the disallowance of Rs. 2,07,41,569/- made u/s. 40(a) by the Assessing Officer on account of payments made to MasterCard International Incorporated, USA and Visa International Service Association, USA.

b) It is respectfully submitted that the learned CIT (A) failed to appreciate that-

MasterCard and Visa International have no permanent establishment in India.

Master Card and Visa International are membership associations and not profit making bodies. Both these entities are acting on the principle of mutuality.

Under section 195(1) of the Act, the person responsible for paying is required to deduct tax only if the sum is chargeable under the provisions of the Act. When the amount is not taxable in India, there is no requirement of deduction of tax at source u/s. 195.

c) It is respectfully submitted that since the payments made to Master Card/ Visa are not chargeable to tax, there was no obligation on Appellant to deduct tax from such payments.

2. LOSS ON UNMATURED FORWARD CONTRACTS - Rs. 10, 82, 92,653/- (Pages 27 to 29 of CIT (A)' order)

a) The learned CIT (A) erred in confirming the disallowance of Rs. 10, 82, 92,653/- being notional loss on revaluation of foreign exchange contracts.

b) It is respectfully submitted that the learned CIT (A) failed to appreciate that the Appellant had claimed the loss on revaluation of foreign exchange contracts at the yearend in accordance with the method of accounting followed by the Appellant as per section 145 of the Income Tax Act, 1961, as amended with effect from 01.04.1997.

c) The disallowance upheld by CIT (A) is unjustifiable and must be quashed.

3. EXPENDITURE ON REFURBISHMENT OF PREMISES AND SOFTWARE - 6, 05, 52,891/- (Pages 29 to 37 of CIT (A)' order)

a) The learned CIT (A) erred in estimating 25% of the expenditure incurred on refurbishment of leasehold premises as capital in nature aggregating to Rs. 1,38,60,752/-.

b) The learned CIT(A) further erred in confirming the disallowance of expenditure incurred on Software Development expenses made by the Assessing Officer aggregating to Rs. 1, 24,52,240/-,

c) The learned CIT (A) has not dealt with the disallowance made by the Assessing Officer on account of expenditure incurred on Computer Software Rs. 2, 78,39,000/- and Renovation and Repairs Rs. 64,00,899/-

4. TAXABILITY U/S. 115JA (Pages 37 to 39 of Ld. CIT (A)' order)

Without prejudice to Ground 1 above:

a) The learned CIT (A) erred in law in confirming the action of the Assessing Officer in applying the provisions of section 115JA when they were not attracted to the facts of the case.

b) The learned CIT (A) failed to appreciate that:

Section 90(2) provides that the provisions of the Act shall apply to the assessee, who is otherwise eligible for double tax treaty relief only to the extent that they are more beneficial to him.

Circular No. 333 dated April 12, 1982 issued by the Central Board of Direct Taxes (CBDT) provides that where a Double Taxation Avoidance Agreement (DTAA) provides for a particular mode of computation of income, the same would be followed irrespective of the provisions of the Income tax Act.

The DTAA specifically lays down the method of determination of profits of the PE subject to allowability of expenses under the domestic law and therefore, it overrides the provisions of Section 115JA (which stipulates the presumptive rate of profits and to which therefore, no recourse need to be had in view of the CBDT CircularNo.333 referred to above.

Since the section provides for presumptive rate of profits, which is not beneficial to the Appellant, due to its carried forward losses and which, therefore has to be disregarded in view of the provisions contained in section 90(2) of the Act.

Courts of many countries have held that the international binding effect of the treaty cannot be affected by such subsequent domestic legislation and such domestic legislation violates international law and causes a breach of the international obligations brought about by the treaty.

Since the tax agreements are special rules, the issue of conflict falls upon the maxim "a subsequent general law does not override a prior special law ".In view of this, the tax agreements being specific rules will 'precede' tax laws and prevail upon them.

Section 115JA (4) provides that, save as otherwise provided in Section 115JA, all other provisions of the Act shall apply to every company mentioned in the said section. It therefore, appears that there is no intention of the Legislature to specifically override the provisions of Section 90 of the Act and therefore, by implication, the provisions of applicable tax treaties by the introduction of Section 115JA.

The Memorandum explaining the provisions of the Finance Bill, 1996, explaining the introduction of section 115JA states that studies have shown that in spite of the fact that companies have earned book profits and have paid handsome dividends, no tax has been paid by them to the exchequer. In case of the Branch-PE of a foreign company, the question of payment of dividends out of book profits does not arise. For this reason also, the provisions of Section 115JA are not intended to apply to Branch-PE of foreign companies, which are governed by the tax treaty provisions.

c) It is respectfully submitted that the decisions of the Authority for Advance Ruling relied on by the CIT (A) are not binding on the Appellant.

5. the Appellant craves leave to add, alter and/or amend one or more of the above grounds of appeal.

6. The Appellant prays for appropriate relief.

Additional Grounds

1. The learned Joint Commissioner of Income-tax, Special Bench 27, Mumbai (JCIT) erred in restricting the claim of Head Office Expenditure of Rs.30, 70, 87,596/- to Rs. 10, 38, 35,677/- being 5% of the 'Adjusted Total Income' under the provisions of section 44C of the Income Tax Act, 1961 (the Act) having failed to appreciate that section 44C has no application to the Appellant's case. The learned JCIT ought to have held that in view of Article 26 of the Double Tax Avoidance Agreement between India and the United Kingdom ("the DTAA"), section 44C could not have been applied in computing the Appellant's income for the purposes of the Act.

It is respectfully submitted that in view of express provisions of Article 26 of the DTAA, section 44C will have no application since the provisions of section 44C are discriminatory in favour of an Indian enterprise vis-à-vis Permanent Establishment of a UK enterprise. In this connection, reliance is placed on the Mumbai tribunal's decision in Metchem Canada Inc. v/s. DCIT [284 ITR (A.T.) 196].

2. the Appellant craves leave to add, alter and/or amend one or more of the above grounds of appeal.

3. The Appellant prays for appropriate relief.

2. The revenue has raised the following grounds:-

1. On the facts and in the circumstances of the case and in law, the Id. CIT (A) erred in directing to allow the expenses of Rs. 49, 31, 09,436/- as deduction on the grounds:

- (i) that though expenses have been incurred outside India, these have been incurred for the purpose of business of the assessee in India;*
- (ii) that the expenses are not capital or personal in nature and therefore allowable u/s. 37(1) of the Act;*

(iii) that the expenses incurred on account of the Indian Branch and expatriate salaries are for the services rendered in India and these cannot be considered as Head Office expenses within the ambit of section 44C of the I.T. Act, 1961, ignoring the fact -

(a) that the term Head Office expenditure as defined in Section 44C has a very wide scope and includes all expenses in the nature of salaries, rent, travelling by any employee or other person of any office outside India and such other matters connected with executive and general administration.

(b) that no distinction is made in Section 44C between such expenses, which are for the direct benefit of the Permanent Establishment and expenses on salaries to expatriate employees which are all expenses of an administrative and executive nature and fall within the definition of 'Head Office expenses', as given in Section 44C of the I.T. Act.

2. On the facts and in circumstances of the case and in law, the Id. CIT(A) erred in deleting the addition made on account of allowing exemption to the assessee u/s. 10(15)(iv) on net income basis and not on gross.

3. On the facts and in the circumstances of the case and in law, the Id. CIT(A) erred in directing to allow the deduction of Rs.3,89,51,202/- in respect of the interest payment made to the RBI on the grounds :-

(1) that the amount paid to the RBI is only compensatory in nature and not penal interest or penalty;

(ii) that since there is a shortfall in the CRR balance, the interest is recovered by RBI to compensate for the loss of interest on the balance for the period of shortfall.

(iii) that the RBI has not yet levied penalty or fine u/s.46 or 47A of the BRA, 1949 or 58B of the RBI Act, 1934 and the amount specified in the show-cause notice is not a penalty or fine, ignoring the fact :-

(a) that the RBI has levied interest @ 3% on the amount of shortfall in CRR balance for the period of shortfall, which actually amounts to levy of penal interest by RBI.

(b) That such payment of interest is a fine or penalty for contravention of guidelines of the RBI.

The appellant prays that the order of the Id. CIT (A) on the above ground be set aside and that of the A.O. Restored.

The appellant craves, leave to amend or/ and alter any ground or add a new ground which may be necessary.

The brief facts of the case are The Appellant is a foreign bank incorporated in United Kingdom (UK) and has been carrying banking business in India through branches. The Appellant is a tax resident of UK and is eligible to claim the benefits of the Double Taxation Avoidance Agreement entered into between India and UK ('the tax treaty'). Indian branches of the Appellant are treated as permanent establishment in India under the tax treaty.

During the year under consideration, the Appellant has raised various grounds of appeals before the Hon'ble ITAT against the order of Hon'ble CIT(A) dated 22 March 2006 passed under section 250 of The Income-tax Act, 1961 ('the Act'). The Appeal was also filed by the Department before the Hon'ble ITAT against the above CIT (A) order.

The Appellant has filed the legal paper-book with respect to both the appeals (i.e., the Appellant's as well as the Department's appeal) on 23 June 2022.

The Appellant submits that the brief synopsis of facts and submission on the grounds of appeal raised by the Appellant / Department before the Ld. ITAT for the AY 1998-99 as under:

Bank's appeal no. 3377/Mum/ 2006

Ground No. 1: Payment to Master card/Visa International

1.1 Ground

(a) The learned CIT (A) erred in confirming the disallowance of Rs. 2, 07, 41,569/- made u/s. 40(a) by the Assessing Officer on account of payments made to

MasterCard International Incorporated, USA and Visa International Service Association, USA.

(b) It is respectfully submitted that the learned CIT(A) failed to appreciate that:

- *MasterCard and Visa international have no permanent establishment in India.*
- *Master Card and Visa International are membership associations and not profit making bodies; both these entities are acting on the principle of mutuality.*
- *Under section 195(1) of the Act, the person responsible for paying is required to deduct tax only if the sum is chargeable under the provisions of the Act. When the amount is not taxable in India, there is no requirement of deduction of tax at source u/s. 195 of the Act.*

(c) It is respectfully submitted that since the payments made to Master Card/ Visa are not chargeable to tax, there was no obligation on Appellant to deduct tax from such payments.

1.2 Submission

The Appellant submits that this deduction was disallowed for non-deduction of TDS in the relevant year, however, the deduction has been allowed in the A.Y. 1999-00 by the Assessing Officer ('the AO') on account of the deposit of tax by the Appellant. Hence, the Appellant does not wish to press this ground in AY 1998-99.

In the result this ground of appeal raised by the assessee is dismissed.

Ground No. 2: Loss on unmatured forward contracts

2.1 Ground

(a) The learned CIT (A) erred in confirming the disallowance of Rs. 10, 82, 92,653/- being notional loss on revaluation of foreign exchange contracts.

(b) It is respectfully submitted that the learned CIT (A) failed to appreciate that the Appellant had claimed the loss on revaluation of foreign exchange contracts at the yearend in accordance with the method of accounting followed by the Appellant as per section 145 of the Income Tax Act, 1961, as amended with effect from 01.04.1997.

(c) The disallowance upheld by CIT (A) is unjustifiable and must be quashed.

2.2 Submission

The Appellant submits that this loss on unmatured forward contract of A.Y. 1998-99 has already been allowed by the AO in the assessment order of A.Y. 1999-00 and hence, the Appellant does not wish to press this ground in A.Y. 1998-99. **In the result this ground of appeal raised by the assessee is dismissed.**

Ground No. 3: Expenditure on refurbishment of premises and software

3.1 Ground:

a) The learned CIT(A) erred in estimating 25% of the expenditure incurred on the refurbishment of leasehold premises as capital in nature aggregating INR 1,38,60,752/-.

- b) *The CIT(A) further erred in confirming the disallowance of expenditure incurred on software Development expenses made by the AO aggregating to INR 1,24,52,240/-.*
- c) *The Ld. CIT (A) has not dealt with the disallowance made by the Assessing Officer on account of expenditure incurred on Computer Software of INR 2,78,39,000/- and renovation and repairs of INR 64,00,899/-.*

3.2 Brief Facts:

- a) During the F.Y. under consideration, the Appellant has incurred expenditure on renovation of its various leasehold premises. The expenses incurred are mainly on account of interior works, electrical works, cabling and wiring, carpets, development of software cost etc.
- b) This amount has been accounted as deferred revenue expenditure, amortized over a period generally of three years, in the books of account. However, in the computation of income, the entire amount was claimed as deduction as the same are revenue expenditure.

3.3 AO's contention (Page 30, para 13):

The AO disallowed the entire expenses holding that the expenditure is incurred for creating assets of enduring benefits and the same cannot be allowed as revenue expense. Also, by amortising these expenses in the books, the Appellant itself is admitting the fact that these expenses are creating assets of enduring

benefit and not revenue in nature. Further, the AO allowed the applicable depreciation.

3.4 CIT(A)'s decision (Page 29, para 11):

- The Ld. CIT (A) estimated that 25% of the expenditure was incurred on the assets which became the capital assets of the Appellant which could be carried by the Appellant after the expiry of lease period and the balance 75% of expenses are held to be incurred in respect of partitions, painting, electrical lighting etc. which became integral part of the leased premises and which cannot be removed by the Appellant after the expiry of the lease period.
- With regard to software development costs, the Ld. CIT(A) relied on the decision of Hon'ble Rajasthan HC, in the case of CIT vs. Aravali Constructions (259 ITR 30) and held that expenses are capital in nature.

3.4 Appellant's submissions

- The Appellant submits that this issue is covered in favor of the Appellant by the decision of the Co-ordinate bench of the Tribunal in the Appellant's own case for the assessment year 1999-2000, wherein the Tribunal following the decision of Hon'ble Supreme Court in the case of Madras Auto Service Pvt. Ltd. [233 ITR 468] **(Copy of decision is enclosed in the Bank's paper book at page 14)** allowed the deduction for the entire refurbishment expenses **(Copy of A.Y. 1999-00 ITAT order was handed over during the hearing on 27 September 2023) vide page 9, para 13 and 14)** which reads as under:

“13. Considered the rival submissions and material placed on record, we observed that Hon’ble. Supreme Court in the case of Madras Auto Services Pvt. Ltd., (supra) on similar issue adjudicated in favour of the assessee. While holding so Hon’ble Supreme Court held as under: -

“The assessee is a limited company carrying on the business of sale of motor parts. Its head-office is at Madras. It has a branch at Bangalore. Under an agreement of lease dated 1st of February, 1966, the assessee obtained from M/S. Hajira Comer and Mrs. Rabia Bai Razack a lease of premises Nos. 64 and 64/1 situated at Sri Narasimharaja Road, Bangalore for a period of 39 years commencing from 1st of January, 1966. Under the terms and conditions of the lease, the lessee (that is to say the assessee), had the right to demolish at its own expense the existing premises and appropriate to itself all the material thereof without paying to the lessors any compensation and construct a new building thereon to suit the purpose of their business as per the plan approved by the lessors. Under Clause 2 of the lease deed, the lessee was required to pay a rent of Rs. 1000/- per month for the first fifteen years, Rs. 1500/- per month for the next ten years, Rs. 1650/- per month for the next ten years and Rs. 2000/- per month for the remaining years. The lease deed further provided that the new construction shall, right from the commencement of the work, be the property of the lessors; and upon completion of the work of construction the lessee will have only the right to be a tenant for a period of 39 years under the existing lease subject to the payment of rent and observation of other terms and conditions of the lease. The lessee shall not be entitled under any

circumstances for any compensation whatsoever on account of its putting up the new construction in the place of the old.

Acting under the lease agreement the assessee invested a sum of Rs. 1, 62, 835/- in the previous year relevant to the assessment year 1968/69 and Rs. 50, 937/- during the succeeding year in constructing a new building on the said land. The assessee claimed before the Income-tax Officer the expenditure of the said sums of Rs. 1, 62,835/- and Rs. 50, 937/- in the relevant assessment years as capital loss. In the alternative, the assessee claimed depreciation on capital investment; in the alternative, the assessee claimed deduction of the payments as business expenditure or as extra rent for the lease. Ultimately, the Income-tax Tribunal has held that the expenditure of the said two amounts for the construction of a new building is in the nature of business expenditure for proper carrying on of the business of the assessee. The Tribunal has, therefore, treated these amounts as revenue expenditure and allowed a deduction in that regard to the assessee. The claim of the department that the expenditure was capital expenditure and was, therefore, not deductible was negated by the Tribunal.

On the application of the department the Tribunal referred the following question to the High Court for its determination under Section 256(1) of the Income-tax Act, 1961:

"Whether on the fact and in the circumstances of the case the Appellate Tribunal was right in holding that the building expenses of Rs. 1,62,835/- are not liable to be taken into account as deductible expenditure in arriving at the real income of the assessee for the assessment year 1968-69?"

For the next assessment year, a similar question was raised in regard to the second sum of Rs. 50,937/-The High Court has, by the impugned judgment, upheld the view of the Tribunal and has held that the two amounts constitute revenue expenditure for the concerned assessment years and are deductible in order to arrive at the income of the assessee for the said assessment years. The present appeals are filed by the department from the impugned judgment of the High Court.

The assessee in the present case has spent the amounts in question in order to construct a new building after demolishing the old building. The new building, however, from inception was to belong to the lessor and not to the assessee. The assessee, however, had the benefit of the existing lease in respect of the new building at the agreed rent for a period of 39 years. The Tribunal has found, as a fact, that the rent as stipulated in the lease was extremely low. It rental rate for the area in which the building was situated was much higher and would be not less than Rs. 12,000/- as against which the maximum rent the assessee would be paying was only Rs. 2,000/-. This concessional rent was on account of the fact that the new building was constructed by the assessee at its own cost.

In order to decide whether this expenditure is revenue expenditure or capital expenditure, one has to look at the expenditure from a commercial point of view. What advantage did the assessee get by constructing a building which belonged to somebody else and spending money for such construction? The assessee got a long lease of a newly constructed building suitable to its own business at a very concessional rent. The expenditure, therefore, was made in order to secure a long lease of new and more suitable business premises at a lower rent. In other words, the assessee made substantial savings in monthly rent for a period of 39 years by expending these amounts. The saving in expenditure was saving in revenue expenditure in the form of rent. Whatever substitutes for revenue expenditure, should normally be considered as revenue expenditure. Moreover, assessee in the present case did not get any capital asset by spending the said amounts. The assessee, therefore, could not have claimed any depreciation. Looking to the nature of the advantage which the assessee obtained in a commercial sense, expenditure appears to be revenue expenditure.

The test for distinguishing between capital expenditure and revenue expenditure in our country was laid down by this Court in Assam Bengal Cement Co. Ltd. v. Commissioner of Income-tax, West Bengal (27 ITR 34). In that case, the appellant-company had acquired from the Government of Assam lease of certain lime-stone quarries for a period of 20 years for the purpose of manufacture of cement. The lessee had, inter alia, agreed to pay an annual sum during the whole period of the lease as a protection fee and in

consideration of that payment, the lessor undertook not to grant to any person any lease, permit or prospecting license for lime-stone. This Court examined tests laid down in various cases for distinguishing between capital expenditure and revenue expenditure. One of the standard tests now in use was laid down in the case of Atherton v. British Insulated and Helsby Cables Ltd. ([1925] 10 Tax. Cases 155). It said: "When an expenditure is made, not only once and for all but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital." Whether by spending the money any advantage of an enduring nature has been obtained or not will depend upon the facts of each case. Moreover, as the above passage itself provides, this test would not apply if there are special circumstances pointing to the contrary. This Court in the above case summarised the tests as follows :(p. 44):

- 1. Outlay is deemed to be capital when it is made for the initiation of a business, for extension of a business, or for a substantial replacement of equipment.*
- 2. Expenditure may be treated as properly attributable to capital when it is made not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade.....If what is got rid of by a lump sum payment is an annual business expense chargeable against revenue, the lump sum payment should equally be regarded as a*

business expense, but if the lump sum payment brings in a capital asset, then that puts the business on another footing altogether.

3. Whether for the purpose of the expenditure, any capital was withdrawn, or, in other words, whether the object of incurring the expenditure was to employ what was taken in as capital of the business. Again, it is to be seen whether the expenditure incurred was part of the fixed capital of the business or part of its circulating capital. (Underlining ours)

Relying upon the second test enumerated above, learned counsel for the appellant has submitted that the assessee got enduring benefit of a capital nature by spending the amount because the assessee obtained a new building for a period of 39 years. The difficulty, however, in the present case, arises from the fact that this building was never to belong to the assessee. Right from inception, the building was of the ownership of the lessor. Therefore, by spending this money, the assessee did not acquire any capital asset. The only advantage which the assessee derived by spending the money was that it got the lease of a new building at a low rent. From the business point of view, therefore, the assessee got the benefit of reduced rent. The High Court has, therefore, rightly considered this as obtaining a business advantage. The expenditure is, therefore, to be treated as revenue expenditure.

Although there are a number of cases dealing with this question, we will limit ourselves to examining a few cases where the assessee, by expending money, created an asset of an enduring nature. However, the asset so created did not

belong to the assessee. In such a situation the courts have held that the expenditure was for better carrying on of the business of the assessee and could be allowed as revenue expenditure, looking to the circumstances of each of those cases. Thus in Lakshmiji Sugar Mills Co. P. Ltd. v. Commissioner of Income-tax, New Delhi (82 ITR 376) the assessee company was carrying on the business of manufacture and sale of sugar. It paid to the Cane Development Council certain amounts by way of contribution for the construction and development of roads between various sugarcane-producing centers and the sugar factories of the assessee. The roads remained the property of the Government. This Court held that the expenditure was not of a capital nature and had to be allowed as an admissible deduction in computing the profits of the assessee's business. The expenditure was incurred for the purpose of facilitating the running of the assessee's motor vehicles and other means employed for transportation of sugarcane to its factories.

In the case of L.H. Sugar Factory and Oils Mills (P) Ltd. v. Commissioner of Income-tax, U.P. (125 ITR 293), the assessee was carrying on the business of manufacture and sale of sugar. It has its factory in U.P. The assessee paid a contribution towards meeting the cost of construction of roads in the area around its factory under a sugarcane development scheme. The question was whether this amount was deductible in computing the assessee's profits. The Court held that it was. Because although the advantage secured was of long duration, it was not an advantage in the capital field because no tangible or intangible asset was acquired by the assessee; nor was there any addition to or

expansion of the profit making apparatus of the assessee. The amount was contributed for the purpose of facilitating the business of the assessee and making it more efficient and profitable. It was, therefore, revenue expenditure.

In the case of Commissioner of Income-tax, Bombay City- I v. Associated Cement Companies Ltd. (172 ITR 257) the respondent-company entered into an agreement to supply water to the municipality and provide water pipelines as also to supply electricity for street lighting and put up a transmission line for that purpose. The assessee also agreed to concrete the main road from the factory to the railway station. The amounts expended for these purposes were held to be revenue expenditure since the installations and accessories were the assets of the municipality and not of the assessee. The expenditure, therefore, did not result in creating any capital asset for the company. The advantage secured by the respondent was immunity from liability to pay municipal rates and taxes for a period of 15 years. This Court said that had these liabilities been paid, the payments would have been on revenue account. Therefore, the advantage secured was in the field of revenue and not capital.

In the case of Commissioner of Income-tax v. Bombay Dyeing and Manufacturing Co. Ltd. (219 ITF 521) the company contributed to the State Housing Board certain amounts for construction of tenements for its workers. The tenements remained the property of the Housing Board. It was held that the expenditure was incurred wholly and exclusively on the welfare of the employees and, therefore, constituted legitimate business expenditure. As the

assessee company acquired no ownership rights in the tenements, this Court said that the expenditure was incurred merely with a view to carry on the business of the company more efficiently by having a contented labour force.

All these cases have looked upon expenditure which did bring about some kind of an enduring benefit to the company as revenue expenditure when the expenditure did not bring into existence any capital asset for the company. The asset which was created belonged to somebody else and the company derived an enduring business advantage by expending the amount. In all these cases, the expense has been looked upon as having been made for the purpose of conducting the business of the assessee more profitably or more successfully. In the present case also, since the asset created by spending the said amounts did not belong to the assessee but the assessee got the business advantage of using modern premises at a low rent, thus saving considerable revenue expenditure for the next 39 years, both the Tribunal as well as the High Court have rightly come to the conclusion that the expenditure should be looked upon as revenue expenditure.

In the premises, the appeals are dismissed with costs."

14. respectfully following the above said decision, we allow ground No.2 raised by the assessee".

In view of the above, the Appellant submits that the ITAT is to follow assessee's own case decided by coordinate bench for A.Y. 1999-00 dated 27 September 2022 and allow the entire amount incurred on refurbishment of premises. **Considering**

the decision of coordinate bench in assessee's own case for A.Y. 1999-00, this ground of appeal raised by the assessee is allowed and AO is directed to treat the Expenditure on refurbishment of premises and software as revenue expenditure.

Additional /supplementary grounds raised grounds by the Appellant

During the A.Y. under consideration, the Appellant had also raised the following additional / supplementary (revised) grounds before us:

- Supplementary (Revised) ground raised vide letter dated 3 May 2011, revising Ground No. 4 of the Memo of appeal, challenging that provisions of section 115JA of the Act are not applicable to the Appellant.
- Additional ground raised vide letter dated 23 August 2011, submitting that in view of express provisions of Article 26 of the tax treaty between India and UK, provisions of section 44C are not applicable in the Appellant's case.
- Additional ground raised vide letter dated 17 September 2012, submitting that interest on Income-tax refund ought to be excluded from taxable income and should be taxed, if necessary, only when the issue of income-tax refund reaches finality. Without prejudice, interest should be taxable at the rate of 10% under Article 12 of the tax treaty.

Additional ground raised vide letter dated 28 November 2016 out of abundant caution for the allowability of claim of above securities losses in transactions with Bank of Karad and Metropolitan Co-op Bank in A.Y. 1998-99 being the year of withdrawal of suit because the losses were not allowed in AY 1993-94 by the Assessing Officer.

Ground No. 4 and Supplementary ground- non-applicability of section 115JA to the Appellant

Supplementary Ground No. 4A

The Joint Commissioner of the Income tax, Special Range 27, Mumbai erred in law in applying the provisions of section 115JA of the Income-tax Act, 1961, when these provisions are not applicable in the case of banking companies which are exempted from preparing books of accounts in terms of requirements of Schedule VI to the Companies Act, 1956.

Supplementary Ground No. 4B

The Joint Commissioner of Income-tax, Special Range 27, Mumbai erred in law in applying the provisions of section 115JA of the Income-tax Act, 1961, when these provisions are not applicable in case of foreign companies.

4.1 Brief facts:

- In the Bank's appeal, the Appellant raised the ground before us that the Ld. CIT (A) erred in law in confirming the action of the Assessing Officer in applying the provisions of section 115JA of the Act when they were not attracted to the facts of the case.
- Subsequently, the Appellant raised the supplementary ground 4A and 4B that provisions of section 115JA of the Act are not applicable in case of banking companies which are exempted from preparing books of accounts

in terms of requirements of Schedule VI to the Companies Act, 1956. Also, provisions of section 115JA of the Act are not applicable in case of foreign companies.

4.2 Appellant's submissions

- In this connection, the appellant relies on the following decisions wherein it was held that provisions of section 115JA of the Act are not applicable to the Banking companies which are not required to prepare its books of accounts under the Companies Act:
 - Appellant's **own case ITAT order dated 12 April 2019 for A.Y. 1997-98** [2019] (104 taxmann.com 236) – (Mumbai ITAT) [*Para 8, page 95 of the Bank's Appeal Paper book*] which reads as under:

"8. We have considered rival submissions and perused material on record. The main plank of assessee's argument against applicability of section 115JA of the Act is, assessee being a banking company maintaining its accounts under the Banking Regulations Act, 1949, the provision contained under section 115JA of the Act will not apply. Undisputedly, the assessee is a banking company and has opened its branches in India after obtaining permission of the RBI. Therefore, the assessee is governed under the Banking Regulations Act, 1949. Section 115JA of the Act provides for computation of total income chargeable to tax to be an amount equal to 30% of the book profit in case such income is less than

30% of the book profit. However, subsection(2) of section 115JA of the Act mandates that the company for the purpose of section 115JA of the Act has to prepare its Profit & Loss Account in accordance with the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. Undisputedly, the assessee being governed under the Banking Regulations Act, 1949, is not required to prepare its Profit & Loss Account under the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. That being the case, the provisions of section 115JA of the Act are not applicable to the assessee. The Tribunal, Mumbai Bench, in Krung Thai Bank (supra) has held that the provisions of section 115JB of the Act, which is more or less pari-materia to section 115JA of the Act, can only come into play when the assessee is required to prepare its Profit & Loss Account in accordance with the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. It was observed by the Branch that the starting point of computation of minimum alternate tax (MAT) is the result shown by such Profit & Loss Account. Since, in case of Banking Company, the provisions of Schedule-VI of the Companies Act, 1956 are not applicable, as, they are required to prepare their accounts under the provisions of Banking Regulations Act, the provision of section 115JB will not be applicable. The other decisions cited by the learned Sr. Counsel for the assessee also support this view. Further, the Tribunal, Mumbai Bench, in MSEB (supra), has held that since the assessee is not constituted as a company under the Companies Act, 1956, the provisions of section 115JA of the Act cannot be applied.

While doing so, the Bench further observed that since the Assessee Corporation is not required to distribute any dividend, it cannot be considered to be a company under the Companies Act, 1956. The facts involved in assessee's case are more or less identical to the facts of MSEB (supra). In view of the aforesaid, we hold that the provisions of section 115JA of the Act are not applicable to the assessee. This ground is allowed."

- Appellant's **own case ITAT order dated 27 September 2022 for A.Y. 1999-00** [2022] (ITA No. 803/ Mum/ 2009) – (Mumbai ITAT) [*Para 18, page 19*]which reads as under:

"18.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. 1997-98, we allow the ground raised by the assessee".

- CIT vs. Union Bank of India [2019] (105 taxmann.com 253) (Bombay HC) [*para 21, page 110 of the Bank's Appeal Paper book*]

4.3 Accordingly, the Appellant submits that the provisions of section 115JA of the Act are not applicable in the Appellant's case. **We have thoroughly considered the decision rendered by coordinate bench in assessee's own case for A.Y. 1997-98 & 1999-2000 alongwith the principle laid down by the Hon'ble High Courts as discussed (supra) and as the submissions by assessee not controverted by the Revenue, we also agree that provisions of section 115JA of the Act is not**

applicable in the case of assessee being banking company duly regularized by the provisions of Banking Regulations Act, 1949 and is not required to prepare its Profit & Loss Account under the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. In view of the above, ground raised by the assessee is allowed.

Additional ground - non-applicability of section 44C on Head office expenditure in view of Article 26 of the tax treaty

5.1 Additional ground

“The learned Joint Commissioner of Income-tax, Special Range 27, Mumbai (JCIT) erred in restricting the claim of Head Office Expenditure of Rs. 30,70,87,596/- to Rs. 10,38,35,677/- being 5% of the 'Adjusted Total Income' under the provisions of section 44C of the Income Tax Act, 1961 (the Act) having failed to appreciate that section 44C has no application to the Appellant's case. The learned JCIT ought to have held that In view of Article 26 of the Double Tax Avoidance Agreement between India and the United Kingdom ("the DTAA"), section 44C could not have been applied In computing- the Appellant's income for the purposes of the Act.

It is respectfully submitted that in view of express provisions of Article 26 of the DTAA, section 44C will have no application since the provisions of section 44C are discriminatory in favour of an Indian enterprise vis-a-vis Permanent Establishment of a UK enterprises. In this connection, reliance is placed on the

Mumbai tribunal's decision in Metchem Canada Inc. V/s. DCIT [284 ITR (A.T.) 196].”

5.2 Brief facts

- During the financial year under consideration, the Head Office had allocated Head Office Expenditure ('HOE') amounting to INR. 30, 70, 87,596/- to SCB India. In the assessment order, the AO has restricted a deduction to INR 10, 38, 35,677/- (being 5% of Adjusted Total Income) under section 44C of the Act.
- The Appellant has raised the additional ground before us that in view of express provisions of Article 26 of DTAA, section 44C of the Act will have no application since the provisions of section 44C are discriminatory in favour of an Indian enterprise vis-à-vis Permanent Establishment of a UK enterprise.

5.3 Appellant's submissions

- At the outset, the Appellant submits that this issue is covered in favor of the Appellant by the decision of the Co-ordinate bench in the Appellant's own case for the assessment year 1999-2000 wherein the Tribunal following the decision in the case of Metchem Canada Inc. v DCIT 284 ITR (AT) 196 (**Copy of decision is enclosed in the Bank's paper book at page 131**) has held that in view of Article 26 of the India-UK DTAA, provisions of section 44C of the Act will not be applicable to the Appellant (**Copy of A.Y. 1999-00, coordinate bench's order was handed over during the hearing on 27 September 2023) vide page 27, para 22**).

- For the sake of completeness, the submission of the Appellant is as under:-
 - Section 44C of the Act reads as under:

*“Notwithstanding anything to the contrary contained in sections 28 to 43A, **in the case of an assessee, being a non-resident**, no allowance shall be made, in computing the income chargeable under the head "Profits and gains of business or profession", in respect of so much of the expenditure in the nature of head office expenditure as is in excess of the amount computed as hereunder, namely:—*

(a) An amount equal to five per cent of the adjusted total income; or

*(b) ****

(c) The amount of so much of the expenditure in the nature of head office expenditure incurred by the assessee as is attributable to the business or profession of the assessee in India, whichever is the least.”

- Section 44C of the Act specifies that a non-resident may deduct Head Office Expenditure (HOE) while computing the taxable business income of its Permanent Establishment (‘PE’). However, the deduction is limited to five percent of the adjusted total income or expenditure attributable to the PE, whichever is lower. The Appellant submits that this section is applicable only to non-residents and there is no such provision restricting deduction for resident assessee.

- The Appellant submits that as per Section 90(2) of the Act, where the Central Government has entered into an agreement with the Government of any country outside India, then in relation to those assessee to whom such agreement applies, the provision of this Act shall apply to the extent they are more beneficial to the Assessee.
- The Appellant submits that the Appellant is a resident of UK and the India-UK DTAA is applicable. Article 26(2) of the India-UK DTAA reads as follows:

“The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favorably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities in the same circumstances or under the same conditions. This provisions shall not be construed as preventing a Contracting State from charging the profits of a permanent establishment which an enterprise of the other Contracting State has in the first-mentioned State at a rate of tax which is higher than that imposed on the profits of a similar enterprise of the first-mentioned Contracting State, nor as being in conflict with the provisions of paragraph 4 of Article 7 of this Convention.”

- Article 26(2) of the Treaty provides that the taxation in India on the PE of a UK enterprise shall not be less favorably levied than the taxation levied on Indian enterprises carrying on the same activities in the same circumstances or under the same conditions. In other words, Article 26(2) of the Treaty removes those limitations as are relatable solely to the PE of a UK resident (like Section 44C of the Act) but not applicable to an Indian resident carrying on the same activities in the same circumstances or the same conditions. Thus, by virtue of Article 26(2) of the Treaty, it is submitted that the Appellant is entitled to deduct of the total head office expenses that are attributable to the PE's business in India and that the limitation as prescribed under Section 44C of the Act shall not apply because the limitations are discriminatory under Article 26 of the Treaty.
- Article 7(4) of the Treaty for which an exception has been created in Article 26(2) of the Treaty permits a State to attribute profits to a PE therein by an equitable method of apportionment.
- Article 7(5) of the Treaty stipulates that while computing the income of the PE, expenses including executive and general administrative expenses so incurred, whether in the State in which the PE is situated or elsewhere, should be allowed as deduction subject to limitation placed in the provision of the Act. In other words, Article 7(5) of the Treaty allows expenses (whether it is in nature of executive and general

administrative expenses or otherwise) subject to provision of the Act. However, it is submitted that as Article 26(2) of the Treaty is specific provision would override the general provision of Article 7(5) of the Treaty. Further, the Appellant submits that though an exception is created for Article 7(4) of the Treaty in Article 26(2), no such exception is created for Article 7(5). Therefore, it is clear that Article 26(2) would override Article 7(5) of the Treaty. This argument was also specifically considered by the Tribunal in the case of Metchem Canada Inc v DCIT (supra) in para 7 and decided in favour of the Appellant.

OECD Commentary:

- The Appellant further relies on the OECD and UN Model Commentaries which also support the view canvassed by the Appellant that HO expenses should be allowed in full without restriction other than those imposed on resident enterprises. In this regard, the Appellant submits that Article 24(3) of the OECD Model Convention / Commentary, 2017 ('OECD Commentary') is in line with Article 26(2) of the India-UK Treaty. The OECD Commentary explains, *inter alia*, that the purpose of Article 24(3) is to end all discrimination in the treatment of a PE as compared with resident enterprises belonging to the same sector of activities, as regards taxes based on business activities, and especially taxes on business profits (**Para 35**). The OECD Commentary notes that a PE must be accorded (in the source state) the same right as resident enterprises to deduct the trading

expenses that are, in general, authorized by the domestic tax law of the source state. Such deductions should be allowed without any restrictions other than those also imposed on resident enterprises (**Para 40**). The same has been explained in UN Model Commentaries, 2017 (**para 35 and para 40 of Article 24**) (**relevant portions of the OECD commentary and UN Model Commentary are enclosed as Annexure 1**).

Relevant judicial precedents:

In this regard, the Appellant places reliance on the decision of **coordinate bench in its own case for the A.Y. 1999-00 (ITA No. 803/ Mum/2009) [page 27, para 22]**, wherein the coordinate bench had followed the decision in the case of *Metchem Canada Inc v DCIT 284 ITR (AT) 196* and allowed the Head Office expenditure in entirety as per Non- Discrimination clause of Article 26 of tax treaty and not restricting the claim under section 44C of the Act.

- Further, the Appellant submits that Article 26 of the India-UK Treaty is *pari-materia* to Article 24 of India-Canada Treaty. Relevant extracts from ‘Non-discrimination’ Article from India-UK and India-Canada Tax treaty are produced below for easy reference:

Provision	India – UK Treaty	India – Canada Treaty
	<u>Article 26(2)</u>	<u>Article 24(2)</u>

Non-discrimination	“The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities in the same circumstances or under the same conditions.”	“The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities.”
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In view of the above, we observe that the above additional ground involves question of law liable to be admitted. Further, on the basis of the above submissions by assessee, we agree that as decided by the coordinate bench, in the case of assessee that the Head office expenditure is allowed in entirety under the provisions of Article 26 of the tax treaty without the applicability of restriction under section 44C of the Act, **and as the submissions by assessee not controverted by the Revenue, In view of this, ground of appeal of the assessee is allowed following the precedent discussed (supra).**

Additional ground raised vide letter dated 17 September 2012- Taxability of interest on IT refund

6.1 Additional ground:

“Additional Ground No. 2A

The Interest on income-tax refund ought to be excluded from taxable income and should be taxed, if necessary, only when the issue of income-tax refund reaches finality.

Additional Ground No. 2B

In addition and without prejudice to the Additional Ground 2A above, in case it is held that interest on income-tax refund is taxable, it should be taxed only at the rate of 10% in accordance with provision of Article 12 of the Tax Treaty between India and United Kingdom and not at the maximum marginal rate tax.”

6.2 Brief facts:

During the year under consideration, the Appellant has received interest on IT refund of INR 3, 71, 25,438/- for different years.

6.3 Appellant’s submissions

In this connection, the Appellant wish to submit as under:

Interest is taxable in the year of finality / final output of the appellant proceedings

- The Appellant submits that the amount of interest to be taxed in the assessment year under consideration should be the amount of interest on income-tax refund basis the final outcome of the appellate proceedings. In other words, the Appellant submits before us that the AO be directed to tax interest on income-tax refund which is based on the finality / final outcome of the appellate proceedings this is because of the fact that the said interest may get reduced depending upon the final outcome.

Rectification of taxability of interest income due to subsequent development

- The Appellant wish to rely on the decision of Mumbai ITAT in the case of **Avada Trading vs. ACIT (284 ITR (A.T.) 73, (Copy of decision is enclosed in the Bank's paper book at page 176)** wherein it was held that if interest granted under section 244A (1) is varied under sub-section (3) of such section then interest originally granted would be substituted by the reduced/ increased amount as the case may be. Thus, income on account of interest if assessed can be rectified under section 154 of the Act.

Interest is taxable at the rate of 10% if taxable in A.Y. 1998-99

- Further, the Appellant submits that the interest on Income-tax refund received by the Appellant is taxable at the rate of 10% in accordance with provisions of Article 12(3) of the Treaty as the said interest on income-tax refund cannot be said to be effectively connected to a PE / India Branch.

- This issue is covered by the decision of the Jurisdictional High Court/ ITAT in the following cases:
 - ***DIT vs. Credit Agricole Indosuez [2015] [377 ITR 102] [Bom-HC]***(Copy of decision is enclosed in the Bank's paper book at page 143) wherein the Hon'ble Bombay HC upheld the decision/ruling of Delhi ITAT in the case of ***ACIT vs. Clough Engineering Ltd [2011] [11 taxmann.com 70] [Delhi Special Bench]***.
 - ***Covered in Appellant's own case:***

The Appellant submits that in the A.Y. 1999-00, the coordinate bench vide its order dated 27 September 2022 (ITA No. 803/Mum/2009) admitted the similar additional ground relying on the decision of Hon'ble Apex Court in the case of National Thermal Power Co., Limited Vs. CIT 229 ITR 383 as the additional ground is legal and no fresh investigation of facts are required [Page 6, para 6] which read as under:

"6.Considered the rival submissions and material placed on record, we observe that as the said additional grounds are legal grounds, wherein, the facts are on record and facts do not require fresh investigation, following the decision of Ld. Supreme Court in the case of National

Thermal Power Co., Limited v. CIT 229 ITR 383 (SC), we admit the said additional grounds of appeal.”

Further, the coordinate bench in A.Y. 1999-00, by following the coordinate bench decision in the case of Avada Trading Vs. ACIT 284 ITR (A.T) 73 has held that the interest on IT refund would be assessable in the year in which it is granted [Page 36, para 26], which read as under:

“26. Respectfully following the above said decision, additional ground no. (i) is allowed as per the stated direction in the above decision of the Coordinate Bench.”

With regard to the applicable rate, the coordinate bench followed the Bombay HC decision in the case of DIT vs. Credit Agricole Indosuez [377 ITR 102] and held that interest should be taxable as per the DTAA at the rate of 10%. The observation of the Tribunal at page 36, para 27 is as under:

“27. With regard to Additional ground (ii) which is in respect of “interest on tax refund be taxed at 10% as per India-UK Treaty”, we observe that the Hon’ble Bombay High Court in the case of Director of Income-tax (IT) v. Credit Agricole Indosuez [377 ITR 102] held as under: -

“2. at the hearing Mr. Tejveer Singh, learned counsel for the Revenue urges the following questions of law for consideration.

“(1)

(2) Whether, on the facts and in the circumstances of the case and in law, the Ld. ITAT was right in holding that the income chargeable at special rate u/s. 10(15) would be on gross basis and not on net basis?

(3)

(4) Whether, on the facts and in the circumstances of the case and in law, the ITAT has erred in directing the A.O. to tax the interest received u/s 244A at the rate prescribed in Article 12 of DTAA between India and France?

(5)”

.....

“4 Regarding Question 2 – The Tribunal records in the impugned order that the Revenue has before it accepted the position that the exemption under Section 10(15) (iv) (h) of the Act is to be allowed on gross basis and not on net basis. In spite of having accepted that exemption under Section 10(15)(iv)(h) of the Act is to be allowed on gross interest before the Tribunal, the Revenue has proposed to above question for consideration without pointing out in any manner the basis for withdrawing the concession made before the Tribunal. In any case in terms of Section 10(15)(iv)(h) of the Act, it is a self evident position that interest payable by any public sector company is not to form part of the

total income. Further the Tribunal in the impugned order has relied upon its own decision in other cases to hold in favour of the Respondent-assessee and decisions in those cases have not been shown to be inapplicable to the present facts and/or disturbed in appeal. Accordingly, Question 2 does not raise any substantial question of law to be entertained.

.....

6. Regarding Question 4 –

(a) The Tribunal by the impugned order restored the issue of the rate at which interest is to be charged to tax on income-tax refund received under Section 244A of the Act to the Assessing Officer to be decided in the light of Indo-France DTAA and the decision of the Special Bench of the Tribunal in the matter of Assistant Commissioner of Income Tax vs. Clough Engineering Ltd. [130 ITD 137].

(b) The grievance of the Revenue is with the impugned order following the decision of the Special bench in Clough Engineering Ltd. (supra).

(c) However we find that the decision in Clough Engineering (supra) of the Special Bench had been followed by the Tribunal in ITA No.183/Mum/2010 [M/s. DHL Operations B.V., The Netherlands Vs. Dy. Director of Income Tax]. The issue before the Tribunal was the rate of tax on which Income tax refund is to be taxed i.e. on the basis of the Articles of DTAA or under the Act. The Tribunal on examination of the DTAA in the above case concluded that interest on income tax refund is not effectively connected with the PE (Permanent Establishment) either on

asset test or activity test. Therefore, taxable under the Article 11(2) of Indo-Netherlands tax treaty. The Revenue carried the aforesaid decision of M/s. DHL Operations B.V. (supra) in appeal to this Court, being Income Tax Appeal No.431 of 2012. This Court by order dated 17 July 2014 refused to entertain the appeal. In the circumstances no fault can be found with the impugned order of the Tribunal in restoring the issue to the Assessing officer to determine / adopt the rate of tax on refund in the light of the relevant clauses of Indo-France DTAA and the decision of Special Bench in Clough Engineering (supra) Accordingly, question 4 does not raise any substantial question of law so as to be entertained.”

28. Respectfully following the above decision of the Hon’ble. Bombay High Court, we allow the additional ground (ii) raised by the assessee.”

6.4 In view of above, the Appellant submits before us that the above additional ground involves question of law and calls for being admitted. **Further, basis the above submissions, we agreed with the contentions of the assessee that the interest on income tax refund is taxable, once it reaches finality and not in A.Y. 1998-99 i.e., A.Y. under consideration and as the submissions by assessee are not controverted by the Revenue in principle, in view of this, AO is directed to delete the addition made on this count till finality on this issue been attained. In the result, this additional ground of appeal no. 2A is allowed.**

As additional ground no. 2A is already allowed in assessee's favour, **Ground no. 2B became academic now, hence not detracted.**

Additional ground raised vide letter dated 28 November 2016 for claim of loss from securities transactions entered into with Bank of Karad and Metropolitan Co-op Bank in A.Y. 1998-99 (being year of crystallization)

7.1 Brief facts:

- The Appellant has raised additional ground in A.Y. 1998-99 before us that claim of loss from securities transactions with Bank of Karad of INR 383.94 Crores (inadvertently mentioned the amount as INR 283.94 Crores in the additional ground) and with Bank of Metropolitan of INR 19.2 Crores should be allowed in A.Y. 1998-99 as the suit filed by SCB were withdrawn in this year.
- Recently, the Ld. ITAT has allowed the entire securities losses in AY 1993-94 vide its order dated 27 July 2023.

7.2 Submissions

The Appellant seeks a direction that in case, the Department succeed in its appeal before the High Court / supreme Court in assessment year 1993-94 that loss is not allowable in the said year as the loss has not crystallized in the said year, then the Assessing Officer be directed to consider the claim of the

Appellant for allowability of loss in the assessment year 1998-99 being the year in which the steps taken for recovery of the loss have concluded.

We have gone through the submissions of assessee and order of coordinate bench for A.Y. 1993-94, wherein the loss claimed by the assessee has been allowed on its own facts, but as the department is in further appeal before the Hon'ble jurisdictional High Court, We agree with the contentions raised by the assessee, that in case Hon'ble High Court reversed the decision of coordinate bench on the ground of crystallization of loss in A.Y. 1998-99, same will be allowed in current A.Y. under consideration as the same has been settled with the parties and final figure of loss has been crystallized in this year. **In view of this, this ground of appeal is allowed for statistical purposes and AO is directed to allow the same in A.Y. 1998-99, if Hon'ble High Court reversed the decision of coordinate bench for A.Y. 1993-94, then only on the basis of crystallization, same will be allowed in current assessment year.**

In the result, appeal of the assessee is partly allowed.

Department's Appeal (ITA No. 3364/Mum/2006)

Ground 1: Direct expenses incurred outside India

1.1 **Ground:**

1. *On the facts and in the circumstances of the case and in law, the Id. CIT(A) erred in directing to allow the expenses of Rs. 49,31,09,436/- as deduction on the grounds :*

(i) that though expenses have been incurred outside India, these have been incurred for the purpose of business of the assessee in India;

(ii) that the expenses are not capital or personal in nature and therefore allowable u/s. 37(1) of the Act;

(iii) that the expenses incurred on account of the Indian Branch and expatriate salaries are for the services rendered in India and these cannot be considered as Head Office expenses within the ambit of section 44C of the I.T. Act, 1961, ignoring the fact-

(a) that the term Head Office expenditure as defined in Section 44C has a very wide scope and includes all expenses in the nature of salaries, rent, travelling by any employee or other person of any office outside India and such other matters connected with executive and general administration.

(b) that no distinction is made in Section 44C between such expenses, which are for the direct benefit of the Permanent Establishment and expenses on salaries to expatriate employees which are all

expenses of an administrative and executive nature and fall within the definition of 'Head Office expenses', as given in Section 44C of the LT. Act.

1.2 **Brief facts:**

- During the F.Y. under consideration, the Appellant had claimed the deduction of INR 49, 31, 09,436/- on account of direct expenses attributable to the Indian Branches basis the auditor's certificates.

- The expenses incurred were mainly on account followings:
 - Salary paid to expatriate employees who were seconded to India and work exclusively for the Appellant's business in India;
 - Expenses relating to data processing at Singapore for the Appellant's business in India; and
 - Expenses relating to NRI Desk to market deposits from NRI's in Dubai and London.

1.3 **AO's contention (Page 7, para 4.5):**

The AO disallowed the entire expenditure under section 37(1) as expense is not laid-out/incurred wholly and exclusively for purpose of SCB India and not debited in books. Further, the AO treated the expenses as Head Office expenditure under section 44C of the Act and restricted the claim at 5% of adjusted total income.

1.4 **CIT(A)'s decision (Page 10, para 4.5):**

CIT(A) following its own decision in the Appellant's case from A.Y. 1994-95 to A.Y. 1997-98 held that the expenses incurred are exclusively for the purpose of business of the Appellant in India and not in nature of Head Office expenses and allowed the deduction of the expenses under section 37(1) of the Act.

1.5 **Assessee's submission:**

The Assessee submits that this issue is covered in favor of the Assessee by a decision of the Co-ordinate bench of the Tribunal in the Assessee's own case for the assessment year 1999-2000, wherein the Tribunal followed the Assessee's own case Tribunal order of A.Y. 1997-98 and dismissed the ground raised by the Revenue (**Copy of A.Y. 1999-00 ITAT order was handed over during the hearing on 27 September 2023- refer Page 43, para 34**) which reads as under:

"34. 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. 1997-98 and also following rule of consistency, we dismiss the grounds raised by the revenue."

In view of the above, the Assessee/respondent submits before us to follow its own case for A.Y. 1999-00 dated 27 September 2022 and uphold the decision of the Ld. CIT (A) by dismissing the ground raised by the Revenue. We have

gone through the relevant orders of Ld. CIT (A) and coordinate bench for A.Y.'s 1994-95 to 1997-98 and 1999-00 respectively. Continuously this issue is being raised by the revenue, but the same is decided in favour of assessee by the Ld. CIT (A) and coordinate bench as mentioned (supra) and Revenue is not in a position to controvert the same with any decision in their favour by any higher judicial forum. **Hence, following the legal precedent continuously uptill in favour of assessee, Ground raised by the Revenue is dismissed.**

Ground No. 2: Disallowance of expenses incurred under section 14A:

2.1 Ground:

“On the facts and circumstance of the case and in law, the Ld. CIT(A) erred in deleting the addition made on account of allowing exemption to the assessee under section 10(15)(iv) of the Act on net income basis and not on gross.”

2.2 Brief facts:

- During the F.Y. under consideration, the Assessee had claimed the total interest received on tax free securities as exempt u/s. 10(15) (iv) of the income tax Act.

2.3 AO's contentions (Page 14, para 10):

- It cannot be proved that the investments in tax free investments had no nexus to the interest bearing funds;

- SCB is involved in various business activities which are separately identifiable
- Net Interest (post reducing proportionate expenses) and not the gross interest from tax-free securities received was eligible to be exempted u/s. 10(15) (iv) of the Act.
- Unintended benefit of double deduction cannot be allowed to SCB on the plea that separate accounts for various ventures are not prepared and the business is interlinked

2.4 CIT(A)'s decision (Page 18, para 9):

The CIT(A) relied on its decision for A.Y. 1997-98 in the Appellant's own case and directed the AO to delete the disallowance made.

2.5 Assessee's submission:

2.6 The Assessee submits that this issue is covered in favor of the Assessee by a decision of the Co-ordinate bench of the Tribunal in the Assessee's own case for the assessment year 1999-2000, wherein the Tribunal followed the Assessee's own case Tribunal order of A.Y. 1997-98 and dismissed the ground raised by the Revenue **(Copy of AY 1999-00 ITAT order was handed over during the hearing on 27 September 2023-Refer Page 8, para 10)** which reads as under:

"10. 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. 1997-98, we allow ground raised by the assessee"

2.7 In view of the above, the Assessee submits before us to follow its own case for A.Y. 1999-00 dated 27 September 2022 and upheld the decision of the Ld. CIT (A) by dismissing the ground raised by the Revenue. Without prejudice to the above, if the Hon'ble ITAT do not agree with the above plea of the Appellant, it is submitted that the disallowance be restricted to 1% of the exempt income. We have gone through the relevant orders of Ld. CIT (A) and coordinate bench for A.Y.'s 1997-98, 1997-98 & 1999-00 respectively. Continuously this issue is being raised by the revenue, but the same is decided in favour of assessee by the Ld. CIT (A) and coordinate bench as mentioned (supra) and Revenue is not in a position to controvert the same with any decision in their favour by any higher judicial forum. We have gone through the entire material and case laws relied upon. Assessee's own case pertains to A.Y. 1997-98 and A.Y. 1999-00, as there is no change in the facts of the case and law laid down by the Hon'ble Apex court in the case of South Indian Bank Ltd [2021] (130 taxmann.com 178) is squarely applicable to the assessee, we agreed with the plea taken by the assessee and to be just and fair in the matter, disallowance is restricted to 1% of the exempted income. **Ground raised by the revenue is partly allowed.**

Ground No. 3: Penal interest paid to the Reserve Bank of India (RBI) on account of shortfall in SLR balance

3.1 Ground:

“On the facts and in the circumstances of the case and in law, the Id. CIT(A) erred in directing to allow the deduction in respect of interest payment made to the RBI on the grounds:

- *That since there is a shortfall in the CRR balance, the interest is recovered by RBI to compensate for loss of interest on the balance for the period of shortfall.*
- *that the RBI has not yet levied penalty or fine u/s. 46 or 47A of Banking Regulation Act, 1949 or 58B of the RBI Act,1934 and the amount specified in the show-cause notice is not a penalty or fine, ignoring the fact:-*
 - a) *that the RBI has levied interest @3% on the amount of shortfall in CRR balance for the period of shortfall, which actually amounts to levy of penal interest by RBI.*
 - b) *That such payment of interest is a fine or penalty for contravention of guidelines of the RBI.”*

3.2 Brief facts:

During the F.Y. under consideration, the RBI has levied interest of INR 3, 89, 51,202/- under section 24 of the Banking Regulation Act, 1949 for shortfall in the maintenance of SLR for certain fortnights. The alleged shortfall arose as the Bank included certain amount/ transactions in the computation of liability for SLR maintenance.

3.3 AO's contention (Page 27, para 11):

The AO relied on the Appellant's own case Ld. CIT (A) order for A.Y. 1991-92, wherein the Ld. CIT (A) placed reliance on the decision of Hon'ble Apex Court in the case of Prakash Cotton Mills Pvt. Ltd. vs. CIT 201 ITR 684 and held that the payment of penal interest is not compensatory but penal in nature and disallowed the same under section 37(1) of the Act.

3.4 CIT(A)'s decision (Page 23, para 9)

The Ld. CIT(A) followed its decision for the A.Y. 1995-96 in the Appellant's own case, wherein it was held that such payment made to RBI is compensatory in nature and not a penalty or fine and therefore, allowed the interest paid to RBI as business expenditure.

3.5 Assessee's submission:

- The Assessee submits that the coordinate bench in A.Y. 1993-94 (**copy of order handed over during the hearing on 27 September 2023**), allowed the deduction of interest paid to RBI on account of shortfall in CRR balance by following assessee's own case for A.Y. 1992-93 ordered by coordinate bench.
- Further, amongst other decisions, reliance was also placed on the decision of the Hon'ble Bombay HC in the case of CIT vs. Bank of Baroda (ITA No. 4169 of 2009) wherein the Hon'ble Bombay HC held that interest paid to RBI on account of non-maintenance of CRR and SLR is not penalty and accordingly, allowed the interest (**Copy enclosed in the paper book filed for Revenue's appeal at page 179**). The finding of the Hon'ble Bombay HC is as under:

- *“The only question raised by the revenue in this appeal is, whether the interest paid by the assessee for non maintenance of the cash reserve ratio / statutory liquidity ratio as per Section 24 of the Banking Regulation Act, 1949 and Section 42 of the Reserve Bank of India Act, 1934 constitute penalty so as to disallow the interest claim. The Tribunal following the decision in the case of DCIT V/s. Dhanalakshmi Bank Ltd. (Cochin) reported in 76 TTJ 439 held that the interest paid to the RBI was not penalty and accordingly the interest expenditure is allowable. SLP filed by the revenue against similar decision of the Tribunal in the case of Dhanalakshmi Bank Ltd. (supra) has been dismissed by the Apex Court as reported in [2005] 277 I.T.R. (ST) 3. In this view of the matter, we find no merit in the appeal and the same is dismissed with no order as to costs.”* In view of the above, the Assessee submits before us to uphold the decision of the Ld. CIT (A) by dismissing the ground raised by the Revenue. We have gone through the relevant orders of Ld. CIT (A) and coordinate bench for A.Y.'s 1992-93 and 1993-94 respectively. Continuously this issue is being raised by the revenue, but the same is decided in favour of assessee by the Ld. CIT (A) and coordinate bench as mentioned (supra) and Revenue is not in a position to controvert the same with any decision in their favour by any higher judicial forum. **Hence, following the legal precedent continuously uptill in favour of assessee, Ground raised by the Revenue is dismissed.**

4. In the result, the appeal of revenue is partly allowed.

5. To sum up, the appeal of assessee and the appeal of revenue are partly allowed.

Order pronounced in the open court on 13th day of November, 2023.

Sd/-

(VIKAS AWASTHY)
JUDICIAL MEMBER

Mumbai, दिनांक/Dated: 13/11/2023

Dhananjay, Sr. PS

Sd/-

(GAGAN GOYAL)
ACCOUNTANT MEMBER

Copy of the Order forwarded to:

1. अपीलार्थी/The Appellant ,
2. प्रतिवादी/ The Respondent.
3. आयकर आयुक्त CIT
4. विभागीय प्रतिनिधि , आय.अपी.अधि., मुंबई/DR, ITAT,
Mumbai
5. गार्ड फाइल/Guard file.

//True Copy//

BY ORDER,

(Asstt. Registrar)
ITAT, Mumbai