IN THE INCOME TAX APPELLATE TRIBUNAL
"B" BENCH, MUMBAI

BEFORE SHRI PAVAN KUMAR GADALE, JM &
MS PADMAVATHY S, AM

I.T.A. No. 2059/Mum/2013
(Assessment Year: 2008-09)

Bajaj Hindusthan Limited Bajaj Bhawan, 2nd Floor, Jamnalal Bajaj Marg, 226, Nariman Point, Mumbai-400021 **PAN : AAACB4351J**	Vs.	**Dy. CIT-3(1)** Aayakar Bhavan, M.K. Road, New Marine Lines, Mumbai - 400020.
Appellant)	:	**Respondent)**

I.T.A. No. 2218/Mum/2013
(Assessment Year: 2008-09)

Dy. CIT-3(1) Room No. 607, 6th Floor, Aayakar Bhavan, M.K. Road, Mumbai - 400020.	Vs.	**Bajaj Hindusthan Limited** Bajaj Bhawan, 2nd Floor, Jamnalal Bajaj Marg, 226, Nariman Point, Mumbai-400021 **PAN : AAACB4351J**
Appellant)	:	**Respondent)**

Appellant/Assessee by	:	Shri Kirit Kamdar, CA
Revenue/Respondent by	:	Shri S. Srinivasu, CIT-DR
Date of Hearing	:	29.04.2024
Date of Pronouncement	:	03.05.2024

O R D E R

Per Padmavathy S, AM:

These appeals of the assessee and the revenue are against the order of the Commissioner of Income Tax (Appeals)-5, Mumbai [for short 'the CIT(A)'] dated 24.12.2012 for the AY 2008-09.

2. The grounds raised by the assessee and the revenue are as under –

Assessee

"1. On the facts and in the circumstances of the case and in law, the Commissioner of Income-tax (Appeals) erred in confirming the action of the Deputy Commissioner of Income-tax in disallowing an amount to the extent of Rs. 2,62,42,364 under section 14A of the Income Tax Act. 1961 ('the Act') treating it as expenditure incurred for earning tax-free income.

2. On the facts and in the circumstances of the case and in law, the Commissioner of Income-tax (Appeals) erred in confirming the action of the Deputy Commissioner of Income-tax in not excluding from the total income, incentives received under the New Sugar Industry Promotion Policy, 2004 as capital receipts not exigible to tax

(a) incentives in the form of exemption from payment of Value Added Tax (VAT) and Central Sales Tax (CST), administrative charges and entry tax aggregating to Rs.6,80,45,988/-

(b) incentives in the form of exemptions and reimbursements aggregating to Rs.77,36,00,966/-.

The appellant hereby reserves the right to add to, alter or amplify the above grounds of appeal, at any time before or at, the time of appeal, so as to enable the Honourable Tribunal to decide the appeal in accordance with law"

Revenue:

"1. Whether on the facts and circumstances of the case and in law, the Ld CIT(A) was justified in allowing relief of Rs. 6,34,96,501/- u/s 14A Rule 8D(2)(ii) & 8D(2)(iii), by admitting fresh evidences furnished by the assessee during the course of appellate proceedings in contravention of Rule 46A of the 11 Rules 1962 without providing any opportunity to the AO to represent the same."

"2. Whether on the facts and circumstances of the case and in law, the Ld CIT (A) was justified in directing the AO to verify the facts relating to exclusion of income of Rs. 7,64,80,000/- admitted in the revised return on account of provision for foreign exchange fluctuation without appreciating the fact that such an issue was never the cause of grievance emanating out of the assessment order passed by the A.O and as such, the direction of the Ld. CIT (A) is beyond his jurisdiction."

"3. Whether on the facts and circumstances of the case and in law, the Ld. CIT (A) was justified in directing the AO to verify the facts relating to exclusion of income of Rs. 7,64,80,000/- admitted in the revised return on account of provision for foreign exchange fluctuation without appreciating the fact that decision of Hon'ble Supreme Court in the case of Goetze India Ltd. [284 ITR 323] held that the AO has no power to entertain a claim for deduction otherwise than by filing of revised return by the assessee.

"The appellant prays that the order of CIT (A) on the above ground be set aside and that of the Assessing Officer be restored."

3. The assessee is a limited company and filed the return of income for AY 2008-09 on 30.09.2018 declaring a loss of Rs.375,47,74,054/-. Subsequently, the assessee filed revised return on 31.03.2010 revising the total loss to Rs.452,98,84,899/-. The assessee field a revised return of income for the reason that (i) revised claim of depreciation to Rs. 432,83,76,036/- against the original depreciation of Rs. 431,74,32,145/- (ii) claim of deduction on account of incentives received under the UP State Sugar Promotion Policy aggregating to Rs. 84,16,46,954/- considering the same as being capital in nature (iii) disallowance of

Rs.7,64,80,000/- on account of provision for FY 2006-07 towards Foreign Exchange Fluctuation reversed during FY 2007-08 (iv) suo-moto disallowance of Rs. 10,00,000/- towards section 14A. The case was selected for scrutiny and the statutory notices were duly served on the assessee. The Assessing Officer (AO) completed the assessment by making the following disallowance –

(i)	Disallowance under section 14A	- Rs. 8,87,38,865/-
(ii)	Subsidy treated as revenue receipt	
	- Reimbursement of society commission and freight.	- Rs. 77,36,00,966/-
	- Exemption from VAT/CST entry tax and admin charges	- Rs. 6,80,45,988/-
(iii)	Community Development Expenses	- Rs. 7,10,075/-

4. Aggrieved the assessee filed further appeal before the CIT(A). The CIT(A) reduced the disallowance under section 14A to Rs. 2,32,42,364/- and sustained the disallowance towards Subsidy treated as revenue receipt. The assessee made a fresh plea before the CIT(A) that in the revised return Rs. 7,64,80,000/- on account of provision for FY 2006-07 towards Foreign Exchange Fluctuation reversed during FY 2007-08 has been inadvertently added and that the same is to be allowed as a deduction. The CIT(A) remitted the issue back to the AO to examine and allow the claim. Aggrieved by the order of the CIT(A) both the assessee and the revenue are in appeal before the Tribunal.

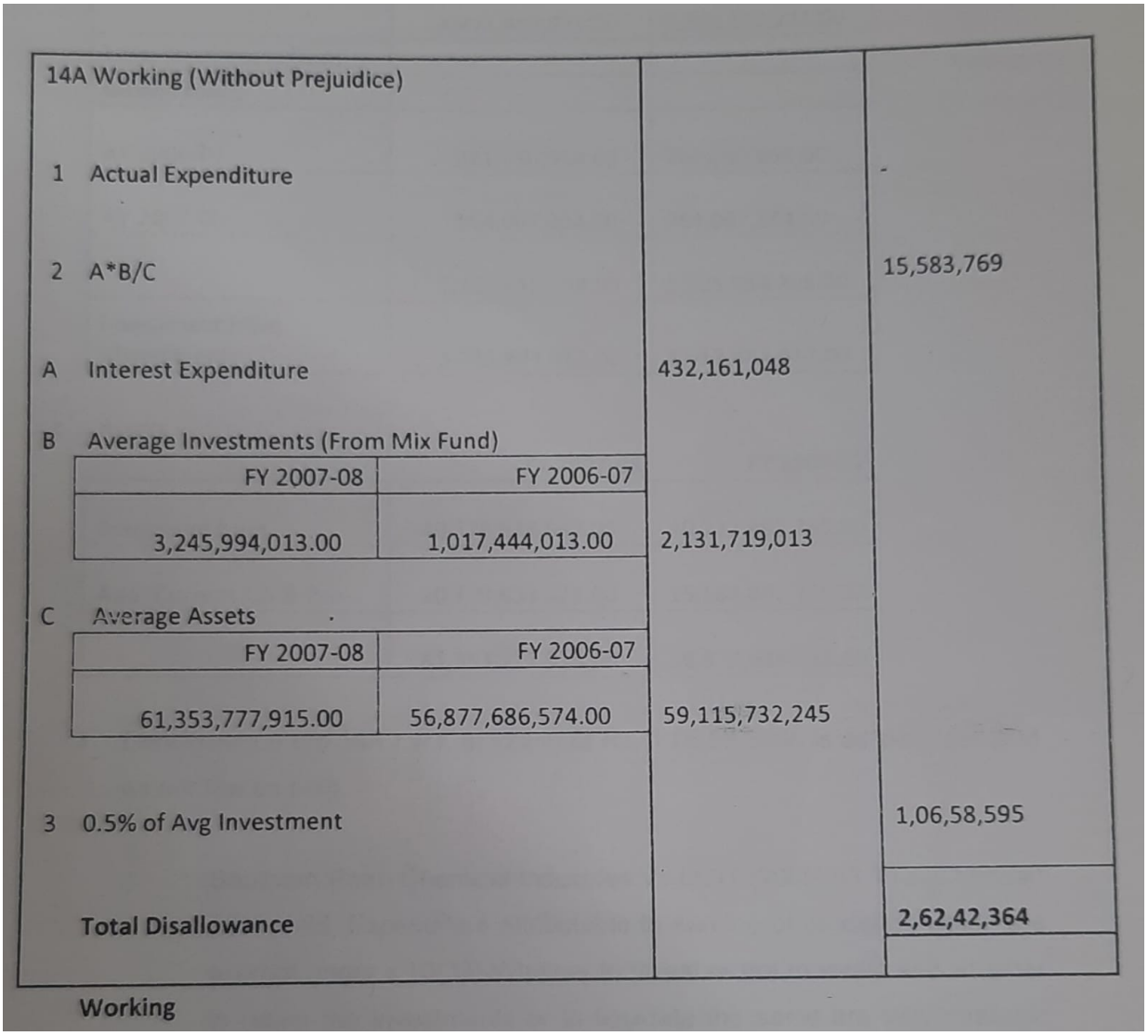
ITA No. 2059/Mum/2013 - Assessee's appeal

Disallowance under section 14A – Ground No.1

5. During the year under consideration the assessee has shown dividend income and income from units amounting to Rs. 19,29,752/- and Rs. 5,25,587/- respectively aggregating to Rs. 24,85,339/-. The AO called on the assessee to explain why the expenditure relatable to exempt income should not be disallowed

as per the provisions of section 14A r.w.r. 8D. The assessee submitted before the AO that it had not incurred any specific expenditure to earn the exempt income and that the investments are not made out of borrowed funds. The assessee further submitted that the investments were made a decade ago and not during the year under consideration. The assessee also submitted that the suo-moto disallowance of Rs. 10,00,000/- is relatable to the exempt income earned and therefore, no further disallowance is warranted. The AO did not accept the submissions of the assessee and held that the assessee ought to have incurred certain indirect expenses for the purpose of managing investments which needs to be disallowed. The AO by relying on various judicial pronouncements invoked section 14A r.w.r. 8D to arrive at a disallowance of Rs. 8,97,38,865/-.

6. Before the CIT(A) the assessee submitted that the investments from which the exempt income is earned is made in the group companies and therefore, no expenditure is incurred towards managing such investments. The CIT(A) called for various details pertaining to the investments made by the assessee to rework the disallowance as under:



14A Working (Without Prejuidice)			
1	Actual Expenditure		-
2	A*B/C		15,583,769
A	Interest Expenditure	432,161,048	
B	Average Investments (From Mix Fund)		
	FY 2007-08: 3,245,994,013.00 / FY 2006-07: 1,017,444,013.00	2,131,719,013	
C	Average Assets		
	FY 2007-08: 61,353,777,915.00 / FY 2006-07: 56,877,686,574.00	59,115,732,245	
3	0.5% of Avg Investment		1,06,58,595
	Total Disallowance		**2,62,42,364**

Working

7. The ld. AR submitted that the AO has not recorded any satisfaction before invoking the provisions of section 14A. The ld. AR further submitted that the workings with regard to the suo-moto disallowance (page no. 8 of PB) have not been considered by the AO and he has not recorded any specific finding with regard to workings submitted. On the disallowance made under Rule 8D(2)(ii) the ld. AR submitted that the own funds of the assessee are much higher than the investments made and therefore, no disallowance is warranted. In this regard our attention is drawn to the financial statements of the assessee in page 219 of PB.

The ld. AR also submitted that the investments yielding exempt income are made in a group company long ago and therefore the assessee is not incurring any expenditure towards managing such expenditure. Accordingly, the ld. AR submitted that the suo-moto disallowance of Rs. 10,00,000/- is sufficient to cover the disallowance under Rule 8D(2 (iii). With regard to the revised calculation done by the CIT(A), the ld. AR submitted that in the said workings the CIT(A) has excluded the exempt earning investments and has considered the movement in other investments in order to make the disallowance. The ld. AR submitted that the investments which is not yielding exempt income cannot be considered for the purpose of making disallowance under Rule 8D(2)(iii) and therefore the disallowance reworked by the CIT(A) is not tenable.

8. The ld. DR on the other hand vehemently argued that the AO has given a detailed finding with regard to why the disallowance under section 14A r.w.r. 8D is to be made in assessee's case. The ld. DR drew our attention to the findings given by the AO in para 7.3 to 7.7 in the assessment order to submit that the AO has recorded a detailed finding as to why he is not satisfied and therefore correctly invoked the provisions of section 14A r.w.r. 8D. The ld. DR further submitted that the investments made by the assessee is huge and therefore the CIT(A) is not correct in considering only the movement during the year for the purpose of reducing the disallowance. Therefore, the ld. DR supported the order of the AO to submit that the disallowance made by the AO should be upheld.

9. We have heard the parties and perused the material on record. The breakup of the exempt income earned by the assessee during the year under consideration is as under:

Sl.No.	Name of Company	Amount
1.	Bajaj Auto Ltd.	19,20,000
2.	Kukund Ltd.	9,752
	Total	**19,29,752**

Sl.No.	Name of Company	Amount
1.	Income of Company	5,25,587
	Total	**5,25,587**

10. We further noticed that the assessee has made a suo-moto disallowance of Rs. 10,00,000/- while filing a revised return of income and before the AO the assessee made the following submission in this regard.

"Reply to point no.4

Details of disallowance of expenses under section 14A are as below:

A. Working of Section 14A disallowance

Proportionate salary of concerned person	*550,385*
Rent	*120,000*
Office Administration	*60,000*
Electricity	*30,000*
Tax	*0*
Office Equipment & Depreciation	*100,000*
Interest	*0*
Misc.	*139,615*
Total	***1,000,000***

B. During the previous year relevant to Ay 2008-09, the company has earned dividend income and Income from units amounting to Rs. 19,29,752 and 5,25,587 respectively. The said Income has been claimed as exempt under section 10 (34) and section 10(35) of the Act while computing The total income

The Company has earned Dividend from Bajaj Auto Limited and Mukand Limited amounting to 1,920,000 and 5,752 respectively. Further the said investments are not made out of the borrowed funds of the Company and have been acquired several decades earlier.

The Company had Reserves of Rs. 1260 crores and Share Capital of Rs.14.14 crores which would be more than adequate to cover the investments made by the Company.

Considering the above facts the Company has estimated an amount of Rs. 10,00,000 an amount of expenditure which may be considered for earning exempting income and has disallowed the same under section 14A of the Act in the revised return of income although it is submitted that no specific, definite and identifiable expenditure has been Incurred for earning exempt income."

11. Rule 8D for computing the disallowance under section 14A came in effect from 24.03.2008 whereby the disallowance towards expenditure incurred for earning exempt income is to be computed as per Rule 8D. The Rule warrants disallowance towards (i) direct expenses incurred towards earning exempt income (ii) interest on borrowed cost for investment earning tax free income (iii) indirect expenses incurred towards earning exempt income. In assessee's case it is an undisputed fact that the assessee has not incurred any direct expenses towards earning exempt income and therefore there is no disallowance under rule 8D(2)(i). Coming to the disallowance under rule 8D(2)(ii), it is argued that it is a well-settled position that where the own funds of the assessee are more than the investments which are earning exempt income then no disallowance under section 8D(2)(ii) is warranted. In assessee's case from the perusal of the financial statements for the year ended 31.03.2008 we noticed that the shareholders funds of the assessee is at Rs. 1260,04,51,173/- whereas the total investments of the assessee is at Rs. 451,71,71,819/-. Therefore, there is merit in the contention of the assessee that since the own funds are more than the investments earning exempt income no disallowance towards interest under Rule 8D(2)(ii) is to be made in assessee's case.

12. With regard to disallowance under Rule 8D(2)(iii) we noticed that the assessee has made a suo-moto disallowance of Rs. 10,00,000/-. The AO has rejected the suo-moto disallowance while invoking section 14A r.w.r.8D. The

relevant paras which the ld. AR argued that the AO ahs recorded the satisfaction is extracted as below:

"7.3 The submissions of the assessee have been carefully considered. It is difficult to accept the hypothesis that the company has not incurred any expenses while planning for the investments made. Investment decisions are very complex in nature. It requires substantial market research, day to day analysis of market trends, and decisions with regard to acquisition, retention, and sale of mutual funds at the most appropriate time It is well known that capital has cost, and that element of cost is represented by interest. Besides, Investment decisions are generally taken in the meetings of the Board of Directors for which administrative expenses are incurred. The exempt income Le dividend, has been earned on account of strategic & planned investments of the company for which the time and application of mind of Sr. Officers/ Directors of the Company was involved. Besides, to keep track on these investments, the staff of the company was also involved for which the assessee company insures salary, perquisites and other administrative expenses, which are directly/ indirectly attributable to the Sr. Officers/staff. Hence, contention of the assessee that no expenses are attributable to earning exempt income, is not acceptable. Further, the assessee has borrowed significant funds & over the years, the losses have accumulated. The assessee is paying interest of 126.33 Crore on various borrowing excluding term loan. Only the term loan can be attributed towards specific project, Plant & Machinery. At the same time, the investment in shares is also very significant and amounts to 451.71 Crore as on 31.3.2008. The assessee has failed to prove that no part of interest bearing funds has been used for making such investment. Therefore, it cannot be ruled out that part of the interest bearing funds have found its way into the investment and thus part of Interest expenses are also relatable to the investments made in shares which give rise to exempt income."

*7.4 to 7.6 *****

7.7 The explanation filed by the assessee is not acceptable, in view of the above referred decisions, and decision of the Hon'ble ITAT, Special Bench, Mumbai in the case of Daga Capital Management Pvt. Ltd. The disallowance of 10 Lacs made by the assessee itself is not found to be acceptable considering the quantum of investment & Interest bearing fund. In this case, the disallowance u/s.14A is required to be made in accordance with the Rule 8D of the I.T. Rules, 1962, which is computed as under:-

The disallowance u/s.14A/Rule 8D shall be aggregate of the following:

1.	*Amount of expenses directly related to such income*	*Amount (Rs.)* *NIL*
2.	*Amount of the Interest expenses indirectly attributable to such income, in accordance with the formula AxB/C, where*	
	A. Total interest expenditure minus direct interest expenditure on such income *Rs. 1263387203 – NIL = Rs. 1263387203 (A)* *B. Average of such investment on the first and last day of previous year* *2288594549 +4517171819 = Rs. 3402883184 (B)* *C. Average of total assets on first and last day of previous year* *56877686574+ 61353777915 = Rs. 59115732245 (C)* *AxB/C =*	*7,2724449*
3.	*0.5% of the 'B' above*	*1,70,14,416*
Total disallowance u/s. 14A		***8,97,38,865***

13. Before proceeding further, we will look at the provisions of section 14Aand Rule 8D which are reproduced as follows:-

> "Section 14A - Expenditure incurred in relation to income not includible in total income.
>
> (1) For the purposes of computing the total income under this Chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to income which does not form part of the total income under this Act.
>
> (2) 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 this 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 this Act.

(3) The provisions of sub-section (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act :]

Provided that nothing contained in this section shall empower the Assessing Officer either to reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year beginning on or before the 1st day of April, 2001.]

Rule 8D.

(1) Where the Assessing Officer, having regard to the accounts of the assessee of a previous year, is not satisfied with—

(a) the correctness of the claim of expenditure made by the assessee; or

(b) the claim made by the assessee that no expenditure has been incurred,

in relation to income which does not form part of the total income under the Act for such previous year, he shall determine the amount of expenditure in relation to such income in accordance with the provisions of sub-rule (2).

(2) The expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts, namely:—

(i) the amount of expenditure directly relating to income which does not form part of total income; and

(ii) an amount equal to half per cent of the annual average of the monthly average of the opening and closing balances of the value of investment, income from which does not or shall not form part of total income :

> **Provided** that the amount referred to in clause (i) and clause (ii) shall not exceed the total expenditure claimed by the assessee."

14. From the combined reading of the above provisions, it is clear that for the purpose of application of section 14 r.w.r 8D(2)(iii) the AO has to record reasons as to why he is not satisfied with the correctness of the claim of expenditure by the assessee. We notice that the Hon'ble Bombay High Court in the case of Principal Commissioner of Income Tax v. Godrej & Boyce Mfg. Co. Ltd. [2023] 149 taxmann.com 222/292 Taxman 497 (Bombay) has considered a similar issue where it has been held that –

In the present case, the assessee had earned an exempt income of Rs. 84,30,37,423/- from shares and mutual funds and submitted a computation of inadmissible expenditure u/s 14A amounting to Rs. 13,66,635/- . The assessee claimed that the disallowance made u/s14A was as per the books of account attributable to earning of exempt income. On a perusal of the assessment order we find that there is no discussion by the AO with regard to the computation of inadmissible expenditure made by the assessee forming part of the return of income. Further, the AO has not recorded any satisfaction that the working of inadmissible expenditure u/s14A is incorrect with regard to the books of account of the assessee. The provision u/s 14(2) does not empower the AO to apply Rule 8D straightaway without considering the correctness of the assessee's claim in respect of expenditure incurred in relation to the exempt income. We agree with the view of the ITAT that in the present case the AO has neither examined the claim in respect of expenditure incurred in relation to exempt income of the assessee nor has recorded any satisfaction with regard to the correctness of assessee's claim with reference to the books of account. Consequently, the disallowance made by

applying the Rule 8D is not only against the statutory mandate but contrary to the legal principles laid down. In our view too, the CIT (A) has rightly deleted the addition made on account of interest expenditure as the assessee had sufficient interest free surplus fund to make the investment and the ITAT has rightly deleted the disallowance made by the AO u/s 14A r.w Rule 8D. Consequently we hold that, the interest expenditure cannot be disallowed u/s 14A r.w. Rule 8D(2)(ii) under any circumstances.

15. In assessee's case from the perusal of the findings as extracted earlier it is clear that the AO before rejecting the suo-moto disallowance has not given any specific error in the computation of suo-moto disallowance but has made a general observation that certain indirect expenses ought to have been incurred by the assessee. We further notice that the AO has not brought anything on record to factually state that the computation of disallowance made by the assessee is not correct. Therefore the enhanced disallowance made without recording satisfaction cannot be sustained Therefore considering the facts and circumstances of the case and the decision of the jurisdictional High Court, we hold that the disallowance made u/s.14A should be restricted to the suo-moto disallowance of Rs.10 lakhs as claimed by the assessee and the enhanced disallowance by the CIT(A) is hereby deleted. This ground of the assessee is allowed.

Subsidy under New Sugar Promotion Policy to be treated as Capital in nature – Ground No.2(a) & (b)

16. The assessee in the revised return of income claimed the subsidies and reimbursements totaling to Rs.84,16,46,954/- given under New Sugar Industry Promotion Policy, 2004 announced by State Government of Uttar Pradesh as not taxable for the reason that the same are capital receipts. The AO called on the

assessee to submit that details pertaining to such claim including the relevant documents, terms and condition of the Scheme etc. The assessee submitted a detailed note on the terms and condition of the scheme to submit that the subsidy received is in the nature of capital receipt for the reason that the object behind giving such subsidy is setting up of new unit / expansion of existing business. However, the AO did not accept the submissions of the assessee and relied on the decision of the Hon'ble Supreme Court in the case of Sahaney Steel and Press works Ltd. & Ors. Vs. CIT (228 ITR 253) to make a disallowance towards subsidy received as reimbursement of Society Commission and Freight and VAT/CST charges. The CIT(A) confirmed the disallowance.

17. The ld. AR submitted that as per the terms of the scheme the subsidy is received as an incentive towards setting up of new sugar factories in private sector to speed up the industrialization of the State of Uttar Pradesh. The ld. AR drew our attention to the detailed submission made before the AO explaining the incentives scheme as per the policy. The ld. AR submitted that the assessee has adjusted the incentives in the revised return of income as capital receipt and has submitted a detailed note which has not been properly appreciated by the AO while denying the claim of the assessee. The ld. AR also submitted that the Co-ordinate Bench of the Tribunal in assessee's own case for AY 2007-08 (ITA No. 5058 & 5208/Mum/2012 dated 12.01.2023) has considered the same issue of treatment of subsidy received in the form of reimbursement and VAT/CST and held that the same are capital receipts. The ld. AR further submitted that the issue for the year under consideration is identical which is substantiated by the fact that the CIT(A) while confirming the disallowance has followed the order of his predecessor for AY 2007-08. Therefore, the ld. AR submitted that the issue is covered by the

above decision of the Co-ordinate Bench and accordingly prayed that the disallowance be deleted.

18. We have heard the parties and perused the material on record. We noticed that the Co-ordinate Bench while considering the same for AY 2007-08 has observed that –

> *"18. Heard both the sides and perused the material on record. Without reiterating the facts as elaborated above the assessee is a public limited company engaged in the manufacturing of sale of sugar. It has set up new sugar plant under the new Sugar Industry Promotion Policy, 2004 announced by the State Government of Uttar Pradesh in the year 2004 for the development and growth of sugar industry in the State of Uttar Pradesh as per the copy of policy placed in the paper book from page no. 125 to 226. Under the object of the New Sugar Industry Policy, 2004 it is stated that from the sugar industry of Uttar Pradesh revenue ofmore than Rs.400 crores is earned by State and Central Government through purchase tax and excise duty. This industry lead to social and economic development of the area in which the industry is located by establishing new sugar mills.There will be increased in the capital and there will be also increased in the revenue for the state in few years. Capital of Rs.2000 crores is required for setting up mills in private sector with capacity of 1 lakh tcd. For this purpose state will have to provide economic concession special packages to industrialists for few years. Hence, the well planned Sugar Industry Promotion Policy is required which attract industrialists from private sector to set up sugar industry in the state. In the New Industries Policy 2004 for capital subsidy, following special incentives will be considered for a period of 10 years from the date of establishment over and above the facilities provide:*
>
> | | | | |
> |---|---|---|---|
> | *1.* | *Entry Tax on sugar* | *2.* | *VAT on Molasses* |
> | *3.* | *Administrative charge on Molasses Registration fees on land* | *4.* | *Stamp duty &* |
> | *5.* | *Purchase tax on cane* | *6* | *Reimbursement of Transportation (Exemption / Reimbursement cost (Cane/Sugar)* |
> | *7.* | *Reimbursement of society Commission* | *8.* | *Reimbursement of State Cess (Excise Share)* |

The scheme and benefit received were given in the submission made by the assessee during the course of assessment are reproduced as under:

"BHL made a capital investment in excess of Rs.500 crores for commissioning various new sugar plants, distilleries and co-generation plants at several location in the state of UP and commenced production before 31' March, 2008.

In terms of the Policy and Notifications issued therein, BHL was granted Eligibility Certificate for five years vide letter dater dated 31' October 2005 on investing in excess of Rs.350 crores under first stage The eligibility was extended upto ten years on investing in excess of Rs.500 crores under second sage vide letter dated 31 January, 2001 Accordingly, BHL has been availing various benefits under the policy:

The various benefits under the Policy can be classified into the following-

A. Subsidy and exemptions of capital nature, which includes:-

i. 10% subsidy on Hexed Capital Investment
ii. Exemption from payment of registration charges on land.
iii. Exemption from payment of stamp duo on land.

B. ***Exemption from collection and deposit which includes****:*

i. Exemption from payment of UPT7 (now vat) and CST on sale of molasses.
ii. Zero rate of Administrative charges on molasses produced by such Units
iv. Exemption from payment of entry tax on sale of non levy sugar produced by such units.

C. Other reimbursements and exemptions, which includes:-

i. Reimbursement of society commission on cane purchase.
ii. Reimbursement of freight subsidy on sugar transportation.
iii. Reimbursement of freight subsidy on transport of sugar cane.
v. Exemption from payment of purchase tax on sugarcane.

In the return of income, the aforesaid incentives granted under the polity were not excluded while computing the total income.

In this regard, it is submitted by BHL that the various incentives envisaged under the Policy are in the nature of the capital receipts and accordingly. not liable to tax. It is further submitted that the following incentives ought to be allowed as a deduction while computing then total income.

1. The receipt of the 10% capital subsidy and exemption of registration charges and stamp duty as mentioned in A' above ought not to be reduced from the cost of assets under section 43(1) of the Act.

2. The following notional amount of incentives referred in 'B' above are in the nature of capital receipts and ought to be reduced while computing the total income.

Incentives	*Rs.*
Exemption from payment of UP7T9nowvvat) and CST on sale of molasses	*1,901,637*
Zero rate of Administrative Charges on molasses produced by such units	*30,215,867*
Exemption from payment of entry tax on sale of non leg sugar produced by such	*36,852,585*
Total	*68,970,08*

4. The incentives in the form of exemptions and reimbursements referred to in 'C' above amounting to Rs.560,779,698 are in the nature of capital receipts not eligible to tax and accordingly, ought to be excluded from the total In this connection on behalf of BHL, we wish to make the following submissions:-

The Government of UP introduced the now Sugar Industry Promotion Policy, 2004, inter alia, with the avowed objective of promotion of establishment of new sugar factories in the private sector to speed up industrialkation of the State. The preamble to the Policy states the proposed objectives as follows.

"to attract private investment in the field of the Cane Development and sugar industry by establishing sugar mills in private sector to augment the industrial Development in the State.

Under the Policy, now sugar factories are given incentives. The period/ quantum of various concessions/ incentives have been linked to the amount of fresh investment made for the establishment of the new sugar mill, although the incentives are to be disbursed after the establishment of the

unit. The salient fatures of the background note to the polig are reproduced hereunder-

"Why new Sugar Industrial Promotion Polity needed?
The total number of sugar factories working in the State is 101 having a total cane crushing capacity of 3 96 lacs TCD out of which 22 sugar mills are under State Sugar Corporation, 27 in Co-operative Sector and 52 sugarmills are established in private sector. It is clear from the basis of the average of the last 5 years that all these sugar factories are able to crush only 41.04% of the total cane produced in the state and the rest is consumed in Gur khandsari. Seed Juice, fodder and chewing.

Percentage of Consumption of Cane in UP

	Sugar Mills	*Other consumption*
Average of 1999-00to 2003-04		*58/96%*
Consumption of Cane %	*48.85%*	*51.15%*

It is this clear that in UP there I savallabilio of sugarcane which can be used as raw material by the sugar mills, however, due to the sickness of the sugar mills belonging to the State Sugar Corporation mid stagnation in the expansion of the production capacity of the sugar mills belonging to the Co-operative sector and due to the lack of availability of the requisite capacity in the sugar mills belonging to the private sector, gradually the State's sugar industry is lagging behind. The sugarcane farmers have to sell their produce to the Handsari/Gur Industry at quite low prices, as a result of which, on the one hand farmers are not able to get adequate price for their produce, on the other hand, contribution to the programmes for the development of the rural areas and welfare of the common people is mostly negligible.

Demand and supply of sugar in the country by 2010-11

It is estimate that in the year 2010-11 the country's total population would be approximately 120.75 crores Due to the increase in the country's per capital average consumption of sugar, till 2010-11, 276.02 lakh tonnes of sugar would be needed for internal consumption. For the target of taking the State's contribution in the country's sugar production from 28.06% in the year 2002-03 to 30% in the year 2010-11, in the State approximately 75 lakh tonne sugar would have to be produced. It is estimated that there would be

substantial increase in the country's average per capita consumption of sugar and in order to satisfy this increase demand the country's two big sugar producing States up and Maharashtra would have to come forward Since in Maharashtra the percentage utilization of sugarcane for producing sugar is at the maximum possible, therefore, UP is the only State when' by increasing the drawal percentage of sugarcane, the increased demand for sugar in the country can be met. Keeping in view the State's limited financial resources, the sick condition of the mills belonging to the Corporation, stagnation in the mills of the Co-operative sector and the inability of the mills in the private sector to completely utilize the sugarcane produced, the need is being felt for encouraging the private sector to invest funds for setting up sugar mills which are of global standards, having sugarcane crushing capacity of 5000 TCD or more. In order to meet the domestic consumption of sugar at 6% GDP growth rate, it would be required to set up mills having approximately one lakh tonne per day capacity and thus create additional capacity. The requirement of sugarcane for this increased capacity can be met by increasing the current drawal percentage of sugarcane from 5 to 7% It must also be clarified that at which ever place a new sugar mill is set up the sugarcane area of that place increases as a result of which there is no possibility of difficulty in sugarcane supply for the increased capacity.

In view of the above, in order to establish new sugar mills in the State the only option is to attract industrialists in the private sector, since in view of the lack of lands the possibility of setting up mills in the Government or the Co-operative sector is negligible in order to set up new sugar mills in the private sector having capacity of one lakh tonnes per day, investment of approximately Rs 2000 crores would be needed. For creating that additional capacity, in the initial years the State Government would be required to provide special economic promotion to the industrialists in the form or special packages."

On the perusal of the aforesaid policy the purpose/ rational behind disbursement of subsidy/ incentive under the Polig and the primary considerations, intention and the objective sought to be achieved by the Polig are summarized as under-

1. Private investment in sugar industry for augmenting the industrial development in the State.

2. Give boost top Sugar Industry which was the only industry in the State dedicated 100% to rural economy, pproipen 0 and development

3. *Increase in sugar production to utilizes the vast cane area in the State.*
4. *Protection of financial interests of cane farmers.*
5. *Rapid rural development and increase in revenues of the Government.*
6. *Generation of employment opportunities."*

19. In terms of the New Promotion Policy of Sugar Industry of Uttar Pradesh Government the assesse company was granted eligibility certificate for 5 years vide letter dated 31.10.2005 on investing in excess of Rs.350 crores under first stage. The eligibility was extended up to 10 years of investing in excess of Rs. 500 crores under 2nd stage. Therefore various benefit under the policy were availed by the assesse as discussed supra in this order. After referring the various clause of the new industry policy the assesse submitted that the various incentives given under the policy were in the nature of capital receipts. The assesse submitted that incentives granted under the policy were in the nature of the capital receipts. In this regard, we have perused the various judicial pronouncements referred by the counsel in the case of CIT Vs. Ponni Sugar & Chemical Ltd. (2008) 174 taxman 87 (SC) it is held that the test is that the character of receipt in the hands of the assesse 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 purpose test. The point of time at which the subsidy is paid is not relevant. The form of subsidy is immaterial. In the case of Everest Industries Ltd. Vs. Joint CIT (2018)19 taxman.com 330 (Mumbai Tribunal) held that sale tax incentive received by the assesse was considered as capital receipt by the A.O same was not required to be reduced from cost of assets for purpose of computing depreciation.

In the case of CIT Vs. Shri Balaji Alloys & Other (2016) 181 CTR (SC) 459 held that excise refund and interest subsidy received by the assesse in pursuance of incentive announced and sanctioned by the Government of India is capital receipt. In the case of Shri Balaji Alloys Vs. CIT (2011) 198 taxman.com 122 (Jammu & Kashmir), it is held that amount of excise refund and interest subsidy received by industrial unit in pursuance of incentives announced in terms of new industrial policy for accelerated industrial development in the State of J & K would be capital receipt in the hands of such Industrial Unit. In the case of CIT Kolhapur Vs.Chaphlekar Brothers Pvt. Ltd. (2017) 88 taxman.com 178 (SC) held that where object of respective subsidy schemes of state of Maharashtra provided for exemption to multiplexes from entertainment duty for a period of 3 years remission for further period of 2 years was to encourage development of Multiple Theatre Complexes, incentive would be held to be capital in nature and

not revenue receipts. In the case of ACIT Vs. Gems Electrotech Ltd. (2016) 71 taxman.com 101 (Ahd Tribunal) wherein held that sale tax and excise duty subsidy received by the assesse for purpose of industrialization was capital receipt. In the case of PCIT Vs. Capgemini India (P) Ltd. (2018) 90 taxmann.com 409 (Bombay) held that grant received by assessee from state govt. in shape of allotment of land for purpose of granting employment for over 3000 people, was to regarded as capital receipts. The ld. Counsel has also furnished similar judicial pronouncements of ITAT Benches. The assessee has also demonstrated that subsidy was granted for setting up sugar industry in general and not for acquisition of any asset, therefore, same also not to be reduced from the cost of asset. The assessee has demonstrated from the material as referred above and furnished before the lower authorities that various incentives were granted under the New Sugar Industry Promotion Policy 2004 for the purpose of development and growth of sugar industry in the state and same has to be considered as capital in nature. Therefore, after considering the facts and judicial findings on the issue as discussed supra, we find the decision of ld. CIT(A) is not justified therefore the ground of appeal of the assessee is allowed."

19. The Coordinate Bench in the above decision has held that various types of incentives (A, B & C listed above) received by the assessee under New Sugar Industry Promotion Policy 2004 has to be considered as capital in nature since the same is given for the purpose of development and growth of sugar industry in the state. From the perusal of the order of the CIT(A) we noticed that he has followed the order for AY 2007-08 in assessee's own case while confirming the disallowance made by the AO. Therefore, there is merit in the contention that the issue is covered by the decision of the Co-ordinate Bench in assessee's own case for AY 2007-08. Further the incentives received by the assessee for the year under consideration, viz., Reimbursement of society commission and freight amounting to Rs. 77,36,00,966/- and exemption from VAT/CST entry tax and admin charges to the tune of Rs. 6,80,45,988/- are received under the same New Sugar Industry Promotion Policy 2004 and therefore respectfully following the above decision of the Co-ordinate Bench, we hold that the disallowance made are not tenable and accordingly be deleted.

20. We notice that the assessee has raised additional ground with regard to adjustment of incentives received under Sugar Industry Promotion Policy to Book Profits under section 115JB in case the same is held in the nature of capital receipt. However the ld.AR during the course of hearing did not press for the admission of the additional ground for the reason that the book profits as per the assessment order is negative and therefore the same is not admitted for adjudication. Nevertheless the assessee is at liberty raise the issue in any other assessment year based on facts and circumstances pertaining to such assessment years.

ITA No. 2218/Mum/2013 - Revenue's appeal

21. Ground No.1 of the revenue appeal pertains to the partial relief given by the CIT(A) towards disallowance under section 14A r.w.r. 8D. We while adjudicating Ground No.1 in assessee's appeal have already given a detailed finding in this regard in the earlier part of this order deleting the enhanced disallowance made by the CIT(A) and restricting disallowance to the suo-moto disallowance of Rs.10 lakhs made by the assessee. Therefore this ground raised by the revenue does not warrant a separate adjudication. Accordingly, this ground of the revenue is dismissed.

22. Ground No. 2 & 3 of the Revenue pertains to Foreign Exchange Fluctuation adjusted by the assessee in the revised return to the tune of Rs. 7,64,80,000/-. The ld. AR in this regard submitted that the assessee in AY 2007-08 had claimed that the gain from foreign exchange fluctuation arising on account reinstatement of ECB and FCCB have to be treated as capital in nature since the borrowing were utilized for the purpose of acquiring fixed assets. The ld. AR further submitted that the said claim was not allowed by the revenue and on further appeal the co-

ordinate bench set-aside the matter back to the AO with a direction to examine the relevant materials after considering the decision of the Hon'ble Supreme Court in the case of Sutlaj Cotton Company Ltd. Vs. CIT (1979) 116 ITR 1 (SC). For the year under consideration i.e. AY 2008-09 it is submitted that the notional gain on foreign exchange fluctuation pertaining to AY 2007-08 is reversed but the same has been inadvertently added by the assessee while filing the return of income. The ld. AR submitted that the above decision of the coordinate bench for AY 2007-08 has a consequential effect in this year since the impugned amount is the reversal of earlier years notional income. Therefore the ld AR prayed that the issue may be remitted back to the AO for verification in accordance with the directions of the co-ordinate bench for AY 2007-08.

23. The ld. DR on the other hand vehemently argued that the foreign exchange fluctuation have been offered as income by the assessee in the AY 2007-08 and later revised its stand stating that it is capital in nature since the loans were borrowed for the purpose of acquiring fixed assets. The ld. DR accordingly argued that the addition made in the year under consideration should be upheld.

24. We have heard the parties and perused the material available on record. We noticed that the Co-ordinate Bench of the Tribunal while considering the issue of gain on foreign exchange fluctuation has held that

> *"25. In this regard, the ld. Counsel submitted that during F.Y. relevant to the year under consideration gain on foreign exchange fluctuation amounting to Rs.7,64,80,000/- arose on account of restatement of ECB and FCCB which had been credited to the profit and loss account. He submitted that the borrowing in the nature of ECB & FCCB were utilized for the purpose of acquiring fixed assets, therefore, the notional gain on foreign exchange fluctuation on restatement of aforesaid loans ought to be excluded while computing the total income. The ld. D.R has contended that no such issue has been brought before the A.O and*

ld.CIT(A) during the course of assessment and appellate proceedings and the claim required verification. In the light of the above facts and circumstances we restore this issue to the file of the assessing officer for deciding the same after verification/examination of relevant material after considering the decision of Hon'ble Supreme Court in the case of Sutlaj Cotton Company Ltd. Vs. CIT (1979) 116 ITR 1 (SC). Therefore, this additional ground of appeal is allowed for statistical purposes."

25. We notice that the amount of Rs. 7,64,80,000/- is added to the loss of the assessee while filing the revised return of income towards the notional income from Foreign exchange fluctuation of earlier year. It is also noticed that the assessee has submitted before the CIT(A) that the said amount has been inadvertently added back while filing revised return of income since the same pertains to reversal of the provision made during the AY 2007-08 which was offered to tax in the earlier year. We further notice that the CIT(A) has given a direction to the AO in this regard to verify the claim of the assessee and allow the claim accordingly. We further notice that in the earlier year i.e. AY 2007-08, the assessee has claimed the forex gain as not taxable and that the said claim was not accepted by the revenue. We also notice that the coordinate bench has remitted the issue back to the AO with a direction to verify/examine of relevant material after considering the decision of Hon'ble Supreme Court in the case of Sutlaj Cotton Company Ltd (supra). Therefore in our considered view the above findings will have impact in reversal made in the year under consideration. Accordingly we deem it fit to remit the issue under consideration for AY 2008-09 to the AO. The AO is directed to examine the facts afresh keeping in mind the directions of the Co-ordinate Bench for AY 2007-08 and allow the claim of the assessee in accordance with law. Needless to say that the assessee be given an opportunity of being heard. It is ordered accordingly. Ground No. 2 & 3 is allowed for statistical purpose.

26. Ground No. 4 & 5 of the Revenue are general and does not warrant a separate adjudication.

27. In the result, the appeal of the assessee in ITA No. 2059/Mum/2013 is allowed and the appeal of Revenue in ITA No. 2218/Mum/2013 is partly allowed.

Order pronounced in the open court on 03-05-2024.

Sd/-	***Sd/-***
(PAVAN KUMAR GADALE)	**(PADMAVATHY S)**
Judicial Member	**Accountant Member**

**SK, Sr. PS*

Copy of the Order forwarded to :

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

BY ORDER,
(Dy./Asstt. Registrar)
ITAT, Mumbai