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

BEFORE SHRI OM PRAKASH KANT (ACCOUNTANT MEMBER)
AND
SHRI RAHUL CHAUDHARY (JUDICIAL MEMBER)

ITA No. 7912/MUM/2019
Assessment Year: 2015-16

Tata Chemicals Ltd., 24, Homi Mody Street, Bombay House, Fort, Mumbai-400 001. **PAN NO. AAACT 4059 M** **Appellant**	***Vs.***	Dy. CIT-2(3)(1), Aayakar Bhavan, MK Road, Mumbai-400020. **Respondent**

Assessee by	:	Mr. Nitesh Joshi a/w Mr. Vanish Bhansali & Mr. Samkit Chaudhary
Revenue by	:	Mr. Ajay Chandra, CIT-DR
Date of Hearing	:	06/11/2025
Date of pronouncement	:	04/02/2026

ORDER

PER OM PRAKASH KANT, AM

This appeal by the assessee is directed against final assessment order dated 30.10.2019 passed by the Ld. Dy. Commissioner of Income-tax, Circle-2(3)(1), Mumbai [hereinafter shall be referred as 'the Assessing Officer'] pursuant to the direction of the Ld. Dispute Resolution Panel (in short the ld DRP) dated

30.09.2019. The grounds raised by the assessee are reproduced as under:

1. Transfer Pricing - adjustments:- Rs. 3,62,01,946/-

On the facts and in the circumstances of the case and in law, the learned Assessing Officer grossly erred in adding a sum of Rs. 3,62,01,946/- u/s 92 of the Act, based on the order of the learned Transfer Pricing Officer u/s 92A(3) of the Act, in respect of adjustment on impugned arm's length interest on the preference share capital of the Associated Enterprise, subscribed by the Appellant, by recharacterising preference shares as a loan.

2. Disallowance u/s 14A :- Rs. 4,86,94,253/-

The learned Assessing Officer erred in computing the disallowance u/s 14A as per Rule 8D amounting to Rs. 4,96,40,588/- where the assessee has already disallowed a sum of Rs. 9,46,335/- u/s 14A and erred in disallowing a net sum of Rs. 4,86,94,253/- u/s 14A of the Act.

3. Disallowance of Deduction u/s 80(IA) in respect of captive power plant:- Rs. 40,04,53,625/-

The learned Assessing Officer erred in disallowing the deduction u/s 80(IA) of Rs. 40,04,53,625/- in respect of the captive power plants, by relying on the orders for AYs 2008-09 to 2012-13, and by merely reproducing the following observations from earlier orders:

i. the assessee has inflated the profit from the said unit by notionally computing profits on sale of steam;

ii. the assessee has inflated the profit on sale of power by showing the cost of production at a rate much lower than one as per the Tariff of Gujarat Electricity Board; and

iii. Assessee claimed deduction u/s 80(IA) in respect of the power plant in spite of the fact that the power generated by the assessee was captively used.

4. Disallowance of Interest paid: - Rs. 146,73,00,000/-

The learned Assessing Officer erred disallowing Rs. 146,73,00,000/- in respect of interest expenditure:- an amount of

a. by treating the same as capital expenditure for the acquiring controlling interest in the subsidiary companies,

b. by not following the Supreme Court decision in the case of Core Health Care Ltd. 298 ITR 194) (SC) (2008);

c. by observing that the said investment has no connection of business in the said investment in whatever manner; and

d. The decision of the learned Dispute Resolution Panel, in para 24.3 in this regard is totally contrary to law and must be quashed.

5. Interest Income assessed as "Income from Other Sources":- Rs. 9,55,00,000

The learned Assessing Officer erred in assessing the Income from intercorporate deposits and staff loans, as "Income from Other Sources", instead of income under the head "Business & Profession", totalling to Rs. 9,55,00,000.

6. Post-retirement Medical Benefit:- Rs. 6,37,00,000/-

The learned Assessing Officers erred in disallowing the sum of Rs. 6,37,00,000/-, expenditure in respect of post-retirement medical benefit by considering the same under the provisions of section 43B of the Act to be allowed as deduction only payment basis.

7. Expenditure on In-house Scientific Research and Development, Section 35(2AB):- Rs. 4,24,13,526/-

The learned Assessing Officer erred in disallowing the expenditure on Scientific Research and Development u/s 35(2AB) totaling to Rs. 4,24,13,526/- for all the three units, on the basis of the auditor's certificate which stated that these expenses are beyond the guidelines laid down by DSIR. These guidelines are in contradiction with the provisions of section 35(2AB) of the Act.

8. Provision for bad and doubtful debts: Rs. 9,70,98,738/-

The learned Deputy Commissioner of Income Tax erred in not allowing the claim of provision for bad and doubtful debts, amounting to Rs. 9,70,98,738/-.

9. Foreign tax Credit : Rs. 15,71,220/-

The learned Deputy Commissioner of Income Tax erred in not granting Credit for Taxes withheld in foreign country u/s 91, claimed during assessment: Rs. 15,71,220/-.

2. Briefly stated, facts of the case as culled out from the submission of assessee are that Assessee Company is engaged in the business of manufacturing and sale of inorganic chemicals,

fertilizers and bio-fuels. The assessee company has been established in 1939 having its Headquarter in Mumbai and regional office across India. The assessee operates an inorganic chemical complex at 'Mithapur' in Gujarat and fertilizer complex at 'Babrala' Uttar Pradesh. The assessee company also has a phosphatic fertilizer complex at 'Haldia' in West Bengal. The assessee company manufactures a variety of products like soda-ash, urea and phosphatic fertilizers, cement, caustic soda, bromine, gypsum, salt etc.

2.1 For the year under consideration, the assessee filed its return of income on 27.11.2015 declaring total income of Rs.663,53,31,056/- under the normal provisions of the Income-tax Act, 1961 (in short 'the Act') and book profit of Rs.637,97,00,001/-. Subsequently, the return filed by the assessee was selected for scrutiny and statutory notices under the Act were issued and complied with. The Assessing Officer noticed that international transactions and domestic transactions were carried out by the assessee with its Associated Enterprises (AEs). The Assessing Officer referred the matter of determination of the arm's length price of those international transactions and domestic transactions to the Ld. Transfer Pricing Officer (TPO). The Ld. TPO in his order dated 30.10.2018 passed u/s 92CA(3) of the Act proposed two adjustments. Firstly, the adjustment to guarantee commission of Rs.557,55,275/-. Secondly, adjustment amounting to

Rs.3,62,01,946/- of interest for characterize investment of preference share/share application money as loan transaction, No adjustment regarding domestic transaction of captive power transfer to eligible unit was made. The Assessing Officer after taking into consideration, the transfer pricing adjustment and addition for other issues arising from the records, passed a draft assessment order on 28.12.2018 u/s 144C of the Act proposing various additions and computing total income under normal provisions of the Act at Rs.874,98,49,681/-.

2.2 The assessee filed objections against the said draft assessment order before the Ld. Dispute Resolution Panel (DRP). The Ld. DRP after considering the submission of the assessee issued directions to the Assessing Officer wherein certain objections of the assessee were accepted. Pursuant to the directions of the Ld. DRP, the AO passed final assessment order on 30.10.2019 and computed the total income under normal provisions at Rs.869,35,99,692/-. Aggrieved, the assessee is in appeal before the Tribunal by way of raising grounds as reproduced above.

3. Before us, the Ld. counsel for the assessee filed a Paper Book containing 9 Volumes comprising of factual as well as legal paper books.

Ground No. 1 – Transfer Pricing Adjustment on Preference Share Investment

4. Ground No. 1 of the appeal concerns a transfer pricing adjustment of ₹3,62,01,946/– made by treating the assessee's investment in preference share capital / share application money of its Associated Enterprise ("AE") as a loan transaction and imputing notional interest thereon.

4.1 Briefly stated, facts qua the issue in dispute as submitted by the assessee are that at the beginning of the relevant assessment year, the assessee held 14,84,714 preference shares of Bio Energy Venture-1 (Mauritius) Pvt. Ltd. ("BEV-1"), each having a face value of USD 100 and carrying a non-cumulative dividend of 5%. Of these, 2,19,500 shares were subscribed directly by the assessee, while the balance 12,65,214 shares were acquired pursuant to amalgamation with Home Field International Pvt. Ltd., Mauritius. The total investment stood at USD 148,471,400, equivalent to ₹732.34 crore.

4.2 It was further stated that during the year, the assessee redeemed 67,500 preference shares at face value, receiving ₹39.99 crore. Simultaneously, the assessee subscribed to 51,000 fresh preference shares of USD 100 each, out of which 36,000 shares were allotted for ₹22.13 crore, while the balance 15,000 shares remained as share application money amounting to ₹9.29 crore.

4.3 It was submitted by the assessee that since the investee company suffered a loss during the year, so no dividend was declared by them.

4.4 The assessee in its Transfer Pricing Study Report provided details of group shareholding structure indicating Bio Energy Venture-1 (Mauritius) Private Limited is an investment holding company which has made downstream investments in various operating companies in different countries. The profile and functional analysis of the said associated enterprise has been provided in transfer pricing study.

4.5 In its transfer pricing study, the assessee benchmarked the transactions of subscription and redemption of preference shares under the "other method" prescribed under Rule 10AB, contending that the transactions were carried out at face value and did not give rise to any income chargeable to tax. The transactions were duly disclosed in Form No. 3CEB, and supporting documentation such as share certificates, registers, audited financial statements, and RBI compliance records were furnished. The assessee claimed to have filed before TPO the copy of the compliance made by it with the Reserve Bank of India in connection with the subscription of such preference at a sample basis. Based on above , it was pleaded that said transaction may not be re-characterized as in the nature of loan granted by the assessee to its associated enterprises on

which it was alleged to have earned notional interest at an arm's length basis.

4.6 The Transfer Pricing Officer ("TPO"), however, questioned the commercial rationale of the investment, particularly in light of the AE's loss-making status where the possibility of any return was Nil, the absence of dividend income, and the assessee's simultaneous redemption and fresh subscription of preference shares. The TPO issued a show-cause notice proposing to re-characterise the investment as a loan in substance.

4.7 The assessee explained that the preference shares were redeemable after ten years at the option of the holder, carried a non-cumulative dividend, and were subscribed as a flexible, non-permanent capital structure to meet the funding needs of BEV-1, an investment holding company with downstream subsidiaries. It was further contended that subscription to share capital does not give rise to a debt obligation, nor to taxable income, and therefore could not be re-characterised as a loan. Regarding the justification of subscribing preference share capital, the assessee submitted that it has already contributed 575 million US dollar in its AE by way of permanent share capital through equity share having face value of one USD. The assessee further submitted that it has chosen to provide non-permanent share capital to meet their investment requirement by way of preference share capital. It was further submitted that it was the only investment opportunity with the AE,

the assessee company should receive back such funds by redemption of the preference shares. The assessee company chooses preference share investment for providing non-permanent capital to its AE for assessee's own convenience and flexibility. It was submitted that the assessee company was sole share holder of capital BEV-1 and the assessee company provided the requisite share capital to its AE for the purpose of set up of the AE. The AE BEV-1 is the investment holding company and holds investment in downstream subsidiary in various countries and the AE BEV-1 in terms of provide capital to downstream subsidiary. It was submitted that in view of reason, the capital requirement of AE BEV-1 had to be flexible and the same was provided by the assessee company being sole shareholder through a non-permanent capital in the form of preference share capital. The assessee company further stated that it had not made any specific borrowing for the purpose of investment in preference share of AE. Regarding the show cause that as why the investment in preference share capital of BEV-1 not to be characterized as loan, the assessee company stated that the contribution to the preference share capital does not give rise to debt or loan. Mere subscription to share capital does not give rise to income and such transaction fall outside the scope of section 92 of the Act.

4.8 Upon careful consideration of the submissions advanced by the assessee, the Transfer Pricing Officer was not persuaded to

accept the characterisation of the transaction as an investment in preference share capital. The TPO recorded a clear finding that the transaction, though structured in the form of preference shares, was in substance a loan arrangement, resulting in erosion of the Indian tax base. The reasoning adopted by the TPO may be summarised as under:

(i) Financial Position of the Associated Enterprise

The Associated Enterprise ("AE") was admittedly in a loss-making position. In the immediately preceding year, it incurred losses before tax amounting to USD 68,013,157. In an uncontrolled situation, no independent enterprise would deploy substantial funds in such an entity with a fixed coupon rate of 5% when the likelihood of any return was virtually non-existent.

(ii) Arbitrariness in Face Value of Preference Shares

The assessee failed to furnish any rational basis for fixing the face value of preference shares at USD 100 per share in a loss-making entity, particularly when equity shares of the same AE were issued at a face value of USD 1 per share. This unexplained disparity undermined the assessee's claim that the transaction was conducted at arm's length.

(iii) Inconsistency with Equity Subscription

During the same year, the assessee subscribed to equity shares of the AE at USD 1 per share and claimed such valuation to be at arm's length. Having accepted USD 1 as an arm's length price for equity in a loss-making company, the assessee could not plausibly justify a valuation of USD 100 per preference share in the very same entity. This indicated that a substantial portion of the amount subscribed did not represent genuine share capital, but rather financing in the nature of a loan.

(iv) Irrelevance of Group Relationship

The contention that the AE was a wholly owned subsidiary and therefore an "extended arm" of the assessee was rejected. Transfer pricing analysis proceeds on the fundamental assumption that the related-party relationship is to be disregarded, and the transaction must be examined from the perspective of independent enterprises operating under uncontrolled conditions.

(v) Commercial Irrationality of the Transaction

The decisive question in transfer pricing is whether an unrelated party would have entered into such a transaction. The answer, in the present case, was clearly in the negative. No independent entity would invest substantial sums in non-

convertible preference shares of a loss-making company, with no realistic expectation of dividend or return.

(vi) Borrowing Profile of the Assessee

The assessee itself carried substantial borrowings and incurred interest expenditure at an average rate of approximately 10.8% per annum. It was commercially implausible that an independent enterprise would borrow funds at a high rate of interest and deploy the same, directly or indirectly, in an investment yielding no return.

(vii) Failure to Establish Source of Funds

Although the assessee asserted that the investment was made out of retained earnings and not borrowed funds, it failed to substantiate this claim by producing cash-flow statements or other cogent evidence. Even assuming availability of internal funds, no prudent independent enterprise would invest large sums for no return.

(viii) Base Erosion Concerns

The TPO observed that the arrangement resulted in substantial outflow of funds from India in the guise of preference share capital, without commensurate income, thereby leading to erosion of the Indian tax base.

(ix) Absence of Arm's Length Return

In an arm's length scenario, an investor would expect at least recovery of its cost of funds along with compensation for credit risk. The assessee neither earned nor demonstrated entitlement to any such return. The absence of mandatory income strongly indicated that the transaction was not conducted at arm's length.

(x) Substance Over Form

Though styled as an investment in preference shares, the transaction effectively placed funds at the disposal of the AE for an indefinite period, without commercial safeguards or assured returns. In substance, therefore, it bore all the essential characteristics of a loan.

(xi) Principle of Commercial Rationality

Transfer pricing jurisprudence mandates examination of transactions through the lens of commercial rationality. An arrangement which no independent enterprise would accept under uncontrolled conditions cannot be regarded as arm's length merely because it is clothed in a particular legal form.

(xii) Judicial Support for Re-characterisation

Reliance was placed on the principles recognised by judicial precedent, which permit re-characterisation where the economic substance of a transaction differs from its form, or where the overall arrangement deviates from what independent enterprises would have adopted in a commercially rational manner.

(xiii) Rule of Consistency Not Applicable

The plea of consistency was rejected, it being well settled that each assessment year is independent and that an erroneous approach in earlier years does not preclude corrective action in subsequent years.

(xiv) Failure of Benchmarking by the Assessee

The assessee failed to furnish any reliable method for benchmarking the transaction. In the absence of such benchmarking, and having regard to the true nature of the transaction, it was necessary to benchmark the same as a loan.

4.9 In view of the totality of facts and circumstances, the TPO concluded that the investment, though described as preference share capital in form, constituted a loan in substance. Since no unrelated enterprise would have entered into such an arrangement

under uncontrolled conditions, the transaction was held to be not at arm's length and liable to benchmarking as a loan transaction.

4.10 After holding the transaction of investment in preference share as loan transaction, the Ld. TPO benchmarked the interest. The arm's length value of the interest to be received was determined applying LIBOR + 2% as the arm's length interest rate and computed the interest amounting to Rs.359,70,375/-. The Ld. TPO also calculated interest on the share application money for preference share which was computed to Rs.2,31,571/-. In this manner, the Ld. TPO proposed total adjustment of Rs.3,62,01,946/- for interest on the investment characterized as loan.

4.11 Before the learned Dispute Resolution Panel ("DRP"), the assessee contended that, in earlier assessment years, the Transfer Pricing Officer had sought to impute interest on preference share investments by re-characterising such preference shares as loans, solely on the premise that those shares had been issued upon conversion of loans earlier advanced to the Associated Enterprise ("AE"), namely Home Field International Pvt. Ltd. ("HIPL"). It was submitted that the factual position during the year under consideration stood on an entirely different footing.

4.12 The assessee asserted that the preference shares which had been allotted upon conversion of loans advanced to HIPL were redeemed from time to time and that the entire lot of such shares

stood fully redeemed by the end of financial year 2011–12. Consequently, as on 31.03.2012, no preference shares issued pursuant to loan conversion remained in existence. In this backdrop, it was urged that the very foundation for treating such preference shares as deemed loans no longer survived. Accordingly, the assessee contended that the re-characterisation of the subscription to preference share capital as a loan transaction was impermissible within the scope of section 92B of the Act.

4.13 With specific reference to the preference shares of Bio Energy Venture-1 (Mauritius) Pvt. Ltd. ("BEV-1"), the assessee submitted that it became the owner of 17,28,489 preference shares pursuant to the merger of Wyoming-1 (Mauritius) Pvt. Ltd. with the assessee. As regards the balance 1,85,000 preference shares of BEV-1, it was contended that the same were subscribed in cash ab initio and were not traceable to any earlier loan transaction.

4.14 Upon consideration of the aforesaid submissions, the learned DRP observed that the preference share investment of the assessee required bifurcation into two distinct categories:(i) preference shares alleged to have been issued upon conversion of loans advanced earlier, and (ii) preference shares issued in consideration of cash or equivalent.

4.15 According to the DRP, the determinative issue was whether the preference shares outstanding during the year could be

identified as having arisen out of loan conversion, thereby justifying their treatment as loans for transfer pricing purposes.

4.16 In order to verify the assessee's claim, the ld DRP directed the assessee to furnish complete particulars of the preference share capital, including distinctive numbers, so as to conclusively establish that the preference shares issued upon conversion of loans had, in fact, been redeemed. However, instead of furnishing such identifiable details, the assessee relied upon the application of the FIFO (First-In-First-Out) method to contend that all preference shares arising from loan conversion stood redeemed.

4.17 The ld DRP found such reliance insufficient and held that, in the absence of share-wise identification, it could not be verified whether the preference shares outstanding during the relevant year pertained to those issued upon conversion of loans or to those subscribed in cash or otherwise. Placing reliance on its findings for assessment year 2010–11, the DRP upheld the action of the TPO in re-characterising the preference share investment as a loan transaction.

4.18 The DRP further affirmed the benchmarking of the notional interest by applying LIBOR plus 200 basis points, as adopted by the TPO. The alternative plea of the assessee, seeking application of LIBOR alone on the ground of absence of incremental risk, was also

rejected. Accordingly, the benchmarking at LIBOR plus 2% was confirmed.

4.19 Before us, the learned counsel appearing for the assessee assailed the findings of the Transfer Pricing Officer and advanced the following submissions:

(i) It was submitted that the Associated Enterprise had incurred losses during the previous year relevant to assessment year 2014–15. The absence of dividend income during the year was, therefore, a direct consequence of the AE's financial performance and not indicative of the nature of the transaction. It was urged that the mere fact that no dividend was declared cannot, by itself, justify re-characterisation of a preference share investment as a loan.

(ii) To substantiate that the transaction was one of subscription to preference share capital, the assessee produced contemporaneous documentary evidence, including preference share certificates, the preference shareholders' register, extracts from the audited financial statements of the AE, and regulatory compliances made with the Reserve Bank of India at the time of subscription. These documents, according to the assessee, conclusively established that the true and legal character of the transaction was that of holding preference shares.

It was contended that investment through preference share capital is a legally recognised mode of funding and, when such mode reflects the actual intention and conduct of the parties, it cannot be disregarded or re-characterised. It was further submitted that, for the year under consideration, the provisions of Chapter X-A relating to General Anti-Avoidance Rules were not applicable, and in any event, the revenue authorities had not invoked or applied those provisions.

(iii) The learned counsel further submitted that even in transactions between independent enterprises, capital is often raised through issuance of preference shares, including in cases where the issuing entity has suffered losses. Preference shares, in such situations, serve as a recognised mechanism to infuse capital for sustaining operations. The assessee placed reliance on documentary material placed before the lower authorities to demonstrate the prevalence of such commercial practice.

(iv) With regard to the observation of the TPO that the face value of preference shares ought to have been USD 1 instead of USD 100, based on comparison with equity shares of the same AE, it was submitted that such reasoning was misconceived. The assessee emphasised that both subscription and redemption of the preference shares were effected strictly at face value. Consequently, whether the face value was USD 1 or USD 100 was wholly

irrelevant, as no premium or discount was involved and no additional benefit accrued to either party.

(v) Addressing the observation that the assessee lacked sufficient reserves and had incurred substantial interest expenditure, it was contended that the character of a transaction must be determined with reference to its terms and legal form, and not by reference to the source of funds utilised. In any event, the investment was made out of mixed funds, and the assessee had adequate interest-free owned funds available at its disposal.

(vi) In response to the allegation that the assessee failed to establish that the investment was made out of retained earnings, the learned counsel submitted that the funds deployed in the preference share investment aggregated to ₹732.34 crore, whereas the cash profits earned during the year amounted to ₹830.68 crore. In addition, the assessee's owned funds, comprising share capital and reserves and surplus, stood at ₹6,043.27 crore, thereby amply demonstrating the availability of internal accruals.

(vii) The inference drawn by the TPO that the transaction was, in substance, a loan was assailed as being devoid of factual and legal foundation. It was submitted that the conclusion was contrary to the documentary record as well as settled principles governing transfer pricing.

(viii) Lastly, with regard to the observation that the absence of dividend rendered the transaction akin to a loan, it was submitted that the preference shares carried a non-cumulative dividend at the rate of 5%. The non-receipt of dividend was solely attributable to the absence of distributable surplus in the AE during the year. This circumstance, it was urged, could not alter the essential character of the transaction, which, both in form and in substance, remained one of subscription and holding of preference shares and not of advancing a loan.

4.20 The learned counsel for the assessee further assailed the findings of the Dispute Resolution Panel and submitted that, while disposing of the objections, the DRP merely followed its directions issued for assessment year 2013–14, without appreciating the material distinction in facts. It was pointed out that, in assessment year 2013–14, the assessee held 1,70,005 preference shares in Homefield International Private Limited, Mauritius. In that year, a part of the preference shares had been allotted in consideration of adjustment of loans earlier advanced by the assessee to the said entity. The Transfer Pricing Officer, therefore, treated such portion of the preference share investment—arising out of loan conversion—as being in the nature of a loan and made a transfer pricing adjustment by imputing notional interest thereon. One of the defences raised by the assessee in that year was that the preference shares issued upon conversion of loans had already been redeemed,

for which reliance was placed on the FIFO (First-In-First-Out) method. The DRP, however, held that the assessee had failed to satisfactorily establish such redemption and accordingly sustained the adjustment.

4.21 It was submitted that the DRP erred in mechanically applying the conclusions drawn in assessment year 2013–14 to the year under consideration. The controversy in the present year, it was urged, relates to fresh subscription of preference shares in a different Associated Enterprise, namely Bio Energy Venture-1 (Mauritius) Pvt. Ltd., and not to the conversion of any loan earlier advanced by the assessee into preference share capital. No part of the preference shareholding during the relevant year, according to the assessee, arose from adjustment of any pre-existing loan liability.

4.22 It was further contended that, even assuming such historical facts to be relevant, they could not form the basis for re-characterisation of the present transaction, which was an independent and fresh capital subscription, both in form and in substance.

4.23 The learned counsel for the assessee submitted that the investment in preference shares did not constitute an "international transaction" within the meaning of the Act and, therefore, the Revenue lacked jurisdiction to re-characterise the same. It was

further urged that the transaction of subscription to preference share capital was clearly on capital account and did not give rise to any income, real or notional.

4.24 It was contended that, for the assessment year under consideration, the statute did not contain any enabling provision permitting re-characterisation of a bona fide capital transaction in the absence of invocation of Chapter X-A dealing with General Anti-Avoidance Rules. According to the assessee, none of the statutory preconditions for application of the said provisions stood satisfied, nor had the revenue authorities sought to invoke them.

4.25 In support of these submissions, reliance was placed on judicial precedents, including the decision of the Hon'ble Bombay High Court in *PCIT v. Aegis Ltd.* [(2019) 102 taxmann.com 495], as also the decision in *PCIT v. Tops Group Electronic Systems Ltd.* (Income-tax Appeal No. 1721 of 2016). The learned counsel further relied upon the decision of the Coordinate Bench of the Tribunal in *SVK Power and Infrastructure Ltd. v. DCIT* [(2023) 150 taxmann.com 534 (Visakhapatnam)], wherein it was held that share application money advanced for subscription to preference shares could not be re-characterised as a loan, and that no notional interest could be imputed thereon. It was submitted that the said decision, being founded upon the judgment of the Hon'ble Bombay High Court in *Aegis Ltd.* (supra), squarely supported the assessee's case.

4.26 Per contra, the learned Departmental Representative supported the orders of the lower authorities and submitted that the assessee had failed to justify the commercial rationale for investing in preference shares carrying a fixed dividend of 5% in a loss-making entity, where there was no realistic expectation of any dividend income. It was further contended that the assessee had not been able to establish that the preference shares outstanding during the year were unconnected with earlier loan transactions, and that, in substance, the investment represented conversion of loans into preference share capital with a view to avoid interest liability.

4.27 According to the learned Departmental Representative, the true nature of the transaction was that of financing, and the Transfer Pricing Officer was therefore justified in re-characterising the same as a loan transaction and benchmarking the notional interest thereon by applying LIBOR with an appropriate mark-up.

4.28 We have carefully considered the rival submissions and perused the material placed on record. At the outset, the objection raised by the assessee as to whether the investment in preference shares constitutes an international transaction does not merit acceptance. The assessee itself treated the impugned transaction as an international transaction in its transfer pricing documentation and benchmarked the same by applying the "other method" prescribed under Rule 10AB of the Income-tax Rules, 1962. It was

the assessee's own case that the subscription of ordinary and preference shares at par represented their arm's length value and that redemption of preference shares at par was justified, having regard to the absence of accumulated profits in the Associated Enterprise ("AE").

4.29 However, the Transfer Pricing Officer, upon examination of the surrounding facts and circumstances, characterised the investment in preference shares as a colourable device for infusing funds into the AE by converting loans into preference share capital. Proceeding on this premise, the TPO treated the transaction as one of lending and benchmarked the same accordingly by applying the Comparable Uncontrolled Price (CUP) method. In this view of the matter, the argument advanced by the learned counsel for the assessee questioning the very existence of an international transaction becomes academic and is liable to be rejected.

4.30 The assessee placed reliance on the judgment of the Hon'ble Bombay High Court in *PCIT v. Aegis Ltd.* [(2019) 102 taxmann.com 495], contending that subscription to preference share capital cannot be re-characterised as a loan transaction and that the Transfer Pricing Officer is not entitled to question the commercial expediency of such investment. There can be no quarrel with the legal principle enunciated therein. However, its application is necessarily contingent upon the assessee being able to establish, on facts, that the transaction is genuine in form and substance.

4.31 In the present case, in earlier years, the assessee converted outstanding loans of AE into preference shares, which has been characterized as loan transaction by the Revenue/Income-tax Authorities. During the year, the Dispute Resolution Panel specifically called upon the assessee to furnish a clear bifurcation of the preference share investment between that arising from conversion of earlier loans and that made by way of fresh cash subscription. Despite such opportunity, the assessee failed to produce cogent and verifiable material to substantiate its claim. In the absence of such bifurcation, the DRP was constrained to conclude that the preference shares outstanding during the year were traceable to earlier loan transactions.

4.32 In such circumstances, the inference drawn by the Revenue authorities that the transaction lacked commercial justification and was structured primarily to avoid interest liability cannot be said to be unreasonable. Where the assessee fails to discharge the burden of establishing the true nature and origin of the transaction, the Revenue is entitled to look beyond the form and examine its real substance. Viewed thus, the transaction assumes the character of a sham arrangement, rendering the ratio of *Aegis Ltd.* (supra) inapplicable to the facts of the present case.

4.33 Similarly, reliance placed on the decision in *PCIT v. Tops Group Electronic Systems Ltd.(supra)* is misplaced, as that case pertained to investment in equity shares and did not involve

conversion of loans into preference share capital. The factual matrix in the present case is materially distinct. The other decisions cited on behalf of the assessee are likewise distinguishable on facts and do not advance the assessee's case.

4.34 In view of the foregoing discussion, we find no infirmity in the order of the Dispute Resolution Panel affirming the action of the Transfer Pricing Officer in re-characterising the preference share investment as a loan transaction and benchmarking the same accordingly.

4.35 Consequently, Ground No. 1 raised by the assessee stands **dismissed**.

5. The next ground No. 2 of the appeal of the assessee relate to disallowance u/s 14A of the Act.

5.1 The facts in brief qua the issue in dispute are that the assessee shown investment of Rs.870.63 crores as on 31.03.2015 in investments capable of yielding exempted income and claimed to have earned exempted income of Rs.100,31,76,746/- from said investments. The assessee *suo-motu* disallowed a sum of Rs.9,46,335/- as expenditure related to the exempted income. The detail of such *suo-motu* disallowance filed by the assessee is reproduced as under:

Allocation of expenses		***Amount in Rs.***
Salary of CFO		*27,135,096*
Salary of Vice President & Group Corp. Controller		*10,291,805*
Salay of Dy. GM – Treasury		*3,414,602*
Salary of other staff in Treasury Dept		*9,037,784*
Total		***49,879,287***
1% of salary of CFO, Deputy CFO & Head Treasury		*408,415*
5% of salary of staff		*451,889*
Total	*A*	*860,304*
Other Overheads(10% of total above)	*B*	*86,030*
Total disallowance u/s 14A	***A+B***	***946,335***

5.2 Before the ld Assessing Officer, the assessee submitted that no direct expenditure had been incurred for earning the exempt income. As regards indirect expenditure, it was contended that the disallowance had been computed on a reasonable and scientific basis by allocating a small and proportionate part of the salaries of senior management and treasury personnel involved in investment-related functions, together with related overheads.

5.3 It was further submitted that this methodology had been consistently followed by the assessee over the years and had been accepted by the Revenue as well as by appellate authorities up to assessment year 2007–08. It was pointed out that the period up to assessment year 2007–08 fell prior to the insertion of Rule 8D of the Income-tax Rules, 1962, and during that period, the settled legal position was that disallowance under section 14A was to be made on a reasonable basis. The assessee's method, having been accepted as reasonable in earlier years, ought not to be disturbed in the absence of any material change.

5.4 The assessee further contended that Rule 8D could be invoked only where the Assessing Officer, having regard to the accounts of the assessee, records an objective dissatisfaction with the correctness of the claim made by the assessee. It was submitted that the rule cannot be applied mechanically and that a finding of actual incurrence of expenditure for earning exempt income is a sine qua non for making a disallowance under section 14A. Such satisfaction, it was urged, must be arrived at objectively, in good faith, and upon due consideration of the relevant facts and circumstances.

5.5 In support of its case, the assessee also furnished details demonstrating that it possessed substantial own funds, far in excess of the investments capable of yielding exempt income, as under:

Rs. in crores

Particulars	***31.03.2014***	***31.03.2015***	***Average***
Own Funds	*8563.28*	*9103.46*	*8833.40*
Relevant Investments	*863.66*	*870.63*	*867.15*

5.6 It was accordingly submitted that, since adequate interest-free funds were available with the assessee, no part of the interest expenditure incurred on specific borrowings could be attributed to investments yielding exempt income. The assessee contended that, in such circumstances, the provisions of section 14A had no application insofar as interest expenditure was concerned, as it could not be said that borrowed funds were utilised for making tax-free investments.

5.7 The contentions advanced by the assessee were, however, not accepted by the Assessing Officer. The Assessing Officer was not satisfied with the correctness of the assessee's suo motu disallowance under section 14A of the Act. Upon examining the accounts, he recorded his dissatisfaction with the claim made by the assessee and proceeded to invoke Rule 8D of the Income-tax Rules, 1962,

5.8 The Assessing Officer observed that section 14A read with Rule 8D mandates disallowance of expenditure incurred in relation to income which does not form part of the total income, once the Assessing Officer is satisfied that such expenditure has in fact been incurred but has not been properly disallowed by the assessee. The disallowance, according to him, is attracted even where the assessee asserts that no expenditure has been incurred for earning exempt income.

5.9 It was noted that the assessee held average investments of Rs. 867.14 crores in instruments yielding exempt income. According to the Assessing Officer, management of such substantial investments necessarily entails incurrence of expenditure. Investments of this magnitude, he reasoned, cannot be undertaken or managed without specialised knowledge, market analysis, and continuous monitoring, all of which involve deployment of skilled personnel and consumption of organisational resources.

5.10 The Assessing Officer further observed that the assessee would invariably receive periodic reports; daily, fortnightly, and monthly, relating to the performance of investments, requiring informed and timely decision-making with respect to deployment and redemption of funds. Such activities, in his view, inevitably involve expenditure on staff time, conveyance, travel, communication, stationery, and other administrative overheads. Although such expenditure may not

be readily quantifiable with precision, a reasonable estimate is required to be made for the purposes of section 14A.

5.11 Relying upon the decision of the *ITAT special Bench, Mumbai in the case of M/s. Daga capital management Pvt. Ltd. (ITANo. 8057/ Mum/03),.* and the judgment of the jurisdictional High Court in *Godrej & Boyce Manufacturing Co. Ltd.(supra)*, the Assessing Officer held that Rule 8D was mandatorily applicable for the assessment year under consideration and that the method prescribed therein was binding. He further observed that, post introduction of Rule 8D, the discretion available to the Assessing Officer to estimate expenditure on a reasonable basis stood replaced by a statutory formula, rendering past assessments irrelevant. Being thus satisfied, the Assessing Officer proceeded to compute the disallowance under section 14A read with Rule 8D as under:

	Description	***Amount [Rs. in crore] as per Rule 8D(2)***	***Addition [Rs. in crore]***
(i)	*the amount of expenditure directly relating to income which does not form part of total income;*	*Nil*	*Nil*

(ii)	*in a case where the assessee has incurred expenditure by way of interest during the previous year which is not directly attributable to any particular income or receipt, an amount computed in accordance with the following formula, namely :—* $A \times \frac{B}{C}$ *Where* *amount of expenditure by way of interest* A *other than the amount of interest included in clause (i) incurred during the previous year ;*	*8.34*	*0.63*
	B the average of value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year ;	*867.14*	
	C the average of total assets as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year ;	*11513.66*	

(iii)	*an amount equal to one-half per cent of the average of the value of investment, income from which does not or shall not form part of the total income, as appearing in the balance sheet of the assessee, on the first day and the last day of the previous year.*	*4.34*	*4.34*
	Total Disallowance under Section 14A		*04.96*

5.12 Thus, the total disallowance under section 14A read with Rule 8D was computed at ₹4,96,40,588/–. After granting credit for the suo motu disallowance of ₹9,46,335/– already made by the assessee, the Assessing Officer made a net addition of ₹4,86,94,253/– to the total income.

5.13 In this manner, the Assessing Officer disallowed a sum of ₹4,96,40,588/– under section 14A of the Act and, after adjusting the amount already disallowed by the assessee, added a net sum of ₹4,86,94,253/– to the assessee's income.

5.14 Before the Ld. DRP, the assessee reiterated the submissions which were made before the Ld. Assessing Officer. Before the learned DRP, the assessee filed computation under rule 8D without prejudice which is reproduced as under and requested for restricting the disallowance under 8D to Rs 4.34 crores:

> ***"e. It may be pointed out that the Ld. CIT(A) in its order dt 06.03.2019, for A Y 2014 15, (refer PB-7C, pg 11 para 6.3) has held as under: -***

"Under such facts and circumstances, a presumption would come into play that the assessee had made investments from their own funds as has been held by the Hon'ble Bombay High Court in the case of HDFC Bank Ltd. 366 IIR 505 and accordingly, no disallowance can be made under clause (ii) of Rule 8D(2) of rules in such facts and circumstances of the case. It is seen from the working of disallowance made by the AO at para 4.2 that she has not made any disallowance under clause (i) of Rule 8D(2) and the disallowance as per clause (ii) has been worked out at Rs. 0.93 crores. The said disallowance made under clause (ii) of Rule 8D(2) is directed to be deleted in view of the facts of assessee having own funds far in excess of the investments capable of yielding exempt income and in view of the decision of Hon'ble Bombay High Court in the case of HDFC Bank Ltd.

Therefore, the working of Rule 8D, on the basis of which the disallowance has been made should be reduced by Rs. 0.63 Crs. Accordingly, without prejudice to our contention that Rule 8D is not applicable, the disallowance as per Rule 8D should be restricted to Rs 4.34 Cr."

5.15 The Ld. DRP following the finding of the DRP in assessment year 2012-13 and 2013-14 rejected the objection of the assessee and upheld the disallowance made by the Assessing Officer u/s 14A of the Act. The relevant finding of the Ld. DRP is reproduced as under:

"15.1 This issue has come up before DRP in A.Y.2012-13 and 2013-14. DRP directions contained in the order for A.Y.2012-13, which was followed in A.Y.2013-14, is reproduced below :-

8.1 It is noted by the DRP that this issue has also been considered by the earlier DRP's and in the immediately preceding year i.e. A.Y. 2011-12, it was held as under:-

"5.1 It is noted by the DRP that this issue has also been considered by the DRP in the immediately preceding year i.e. A.Y. 2010-11. The DRP in Para 6.4 on Page 25 has upheld application of Rule 8D in the case of the assessee company.

5.2 The financials of the assessee company reveals that for the current year under consideration the borrowing cost debited in the books of account is Rs. 350.83 Crores. The assessee company has raised loans, both unsecured & secured during the year under consideration, which stands at Rs. 5699.74 Crore as on 31.3.2011. Also, the DRP has noted that the assessee company has earned substantial exempt income, during the year under consideration, the details of which are as under: -

Dividend Income	*Rs. 75,34,73,172*
Long term Capital gains	*Rs. 16,75,14,792*
Total	*Rs. 92,09,87,965*

5.3 The DRP has noted that on the basis of the facts of the case, the A.O. has recorded its non-satisfaction with the correctness of the claim made by the assessee company, as mandated by sub-section (2) of section 144. After giving such a categorical finding, the A.O. proceeded with calculating the disallowance as per the prescribed Rule 8D, as the assessee company's case fell under sub-section (3) of section 14A of the I.T. Act 1961. The provisions of sub- section (3) of section 14A clearly states that Rule 8D shall also apply in a case, where the assessee company claims that no expenditure has been incurred.

5.4 In this regard, it is important to reproduce the contents of Section 14A, which are as below :-

"144. 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 Ist day of April, 2001."

5.5 It is amply clear from the above provisions that the main operating portion is sub-section (1) of Section 14A and the subsequent amendments has not changed the wordings of sub section (1). The Finance Act, 2006 has introduced w.e.f. 1.4.2007, sub section (2) and sub section (3) of section 14A. The sub section (2) of Section 14A basically lays down the manner in which the disallowance u/s 14A has to be calculated, read with Rule 8D of the I.T Rules, 1962. Further, sub section (3) of Section 14A only clarifies that even if the assessee claims that no expenditure has been incurred in relation to the exempt income then also, sub section (2) of section 14A can be applied. The legislature in its own wisdom, to remove the subjectivity involved in the calculation of disallowance under section 144 has standardized the amount of disallowance to be made under section 144. This amendment was necessary as the Assessing Officers were making disallowances u/s 14A on estimate basis without any scientific and logical reasoning. It is precisely for this reason that Rule 8D has been inserted w.e.f. 24.3.2008.

5.6 In the case of Godrej & Boyce Mfg. Co. Ltd. Vs. DCIT & Anr., (2010) 328 ITR 0081, the Hon'ble Bombay High Court has held that if the AO is not satisfied with the claim of the assessee, then the legislature directs him to follow the method that has been prescribed. The relevant portion of the judgment of the Hon'ble Bombay High Court is reproduced below:-

The following principles would emerge from s. 14A: (a) the mandate of s. 14A is to prevent claims for deduction of expenditure in relation to income which does not form part of the total income of the assessee; (b) sec. 14A(1) is enacted to ensure that only expenses incurred in respect of earning taxable income are allowed; (c) the principle of apportionment of expenses is widened by s. 14A to include even the apportionment of expenditure between taxable and non-taxable income of an indivisible

business; (d) the basic principle of taxation is to tax net income. This principle applies even for the purposes of s. 14A and expenses towards non-taxable income must be excluded; (e) once a proximate cause for disallowance is established---which is the relationship of the expenditure with income which does not form part of the total income- a disallowance has to be effected. All expenditure incurred in relation to income which does not form part of the total income under the provisions of the Act has to be disallowed under s. 144. Income which does not form part of the total income is broadly adverted to as exempt income as an abbreviated appellation. Under sub-s. (2), the AO is required to determine the amount of expenditure incurred by an assessee in relation to such income which does not form part of the total income under the Act in accordance with such method as may be prescribed. The method, having regard to the meaning of the expression 'prescribed' in s. 2(33), must be prescribed by rules made under the Act. What merits emphasis is that the jurisdiction of the AO to determine the expenditure incurred in relation to such income which does not form part of the total income, in accordance with the prescribed method, arises if the AO is not satisfied with the correctness of the claim of the assessee in respect of the expenditure which the assessee claims to have incurred in relation to income which does not form part of the total income. Moreover, the satisfaction of the AO has to be arrived at, having regard to the accounts of the assessee. Hence, sub-s. (2) does not ipso facto enable the AO to apply the method prescribed by the rules straightaway without considering whether the claim made by the assessee in respect of the expenditure incurred in relation to income which does not form part of the total income is correct. The AO must, in the first instance, determine whether the claim of the assessee in that regard is correct and the determination must be made having regard to the accounts of the assessee. The satisfaction of the AO must be arrived at on an objective basis. It is only when the AO is not satisfied with the claim of the assessee, that the legislature directs him to follow the method that may be prescribed. Sub-s. (3) of s. 14A provides for the application of sub-s. (2) also to a situation where the assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under the Act. CIT vs. Walfort Share & Stock Brokers (P) Ltd. (2010) 233 CTR (SC) 42: (2010) 41 DTR (SC) 233 relied on."

5.7 The provisions of section 14A read with Rule 8D ensure that the tax incentive to certain incomes like dividend should not be used to reduce the tax payable on taxable income by debiting

expenses incurred to earn non-taxable income against the taxable income. Similar views have been echoed by the Hon'ble Bombay High Court in the case of Godrej & Boyce Mfg. Co. Ltd. Vs. DCIT & Anr., (2010) 328 ITR 0081, wherein it was held as under:-

> *"Sec. 14A represents a serious attempt on the part of Parliament to ensure that the tax incentive to certain incomes should not he used to reduce the tax payable on taxable income by debiting expenses incurred to earn non-taxable income against the taxable income. In other words, what s. 14A effectuates is that a shareholder should not get the benefit both of an exemption under s. 10(33) and also a deduction in respect of the expenditure laid out towards earning tax-free income. If the dividend income had not been exempt under s. 10(33), the Revenue would have. taxed such dividend income and the assessee would have been entitled to a deduction in respect of its expenditure in relation to that income. Dividend income does not form part of the total income under s. 10(33). Sec. 14A ensures that the shareholder whose income from dividend is not included in the total income of a previous year shall not claim a deduction in respect of the expenditure incurred in relation to earning such income. Sec. 14A is founded on a valid rationale that the basic principle of taxation is to tax net income that is to say, gross income minus the expenditure. On that analogy the exemption is also in respect of net income and expenses allowed can only be in relation to the earning of taxable income. Therefore, the submission of the assessee that an absurdity would result on the application of the literal interpretation of s. 14A cannot be accepted."*

5.8 The provisions of section 14A read with Rule 8D is an attempt on the part of the legislature to remove the subjectivity in the calculation of expenditure to be disallowed and thus introduce uniformity. It has been held in the case of Godrej & Boyce Mfg. Co. Ltd. Vs. DCIT & Anr., (2010) 328 ITR 0081 by the Hon'ble Bombay High Court as under:-

> *"Sub-s. (2) of s. 14A prescribes a uniform method for determining the amount of expenditure incurred in relation to income which does not form part of the total income only in a situation where the AO, 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. It therefore merits emphasis that sub-s. (2) of s. 14A does not authorize or empower the AO to apply the prescribed method irrespective of the nature of the claim made by the assessee. The AO has to first consider the correctness of the claim of the assessee*

having regard to the accounts of the assessee. The satisfaction of the AO has to be objectively arrived at on the basis of those accounts and after considering all the relevant facts and circumstances. The application of the prescribed method arises in a situation where the claim made by the assessee in respect of expenditure which is relatable to the earning of income which does not form part of the total income under the Act is found to be incorrect. In such a situation a method had to be devised for apportioning the expenditure incurred by the assessee between what is incurred in relation to the earning of taxable income and that which is incurred in relation to the earning of non-taxable income. As a matter of fact, the Memorandum Explaining the Provisions of the Finance Bill, 2006 and the CBDT Circular No. 14 of 2006, dt. 28th Dec., 2006 state that since the existing provisions of s. 14A did not provide a method of computing the expenditure incurred in relation to income which did not form part of the total income, there was a considerable dispute between taxpayers and the Department on the method of determining such expenditure. It was in this background that sub-s. (2) was inserted so as to provide a uniform method applicable where the AO is not satisfied with the correctness of the claim of the assessee. Sub-s. (3) clarifies that the application of the method would be attracted even to a situation where the assessee has claimed that no expenditure at all was incurred in relation to the earning of non-taxable income. Parliament has provided an adequate safeguard to the invocation of the power to determine the expenditure incurred in relation to the earning of non- taxable income by adoption of the prescribed method. The invocation of the power is made conditional on the objective satisfaction of the AO in regard to the correctness of the claim of the assessee, having regard to the accounts of the assessee. A decision by the AO has to be arrived at in good faith on relevant considerations. The AO must furnish to the assessee a reasonable opportunity to show cause on the correctness of the claim made by him. In the event that the AO is not satisfied with the correctness of the claim made by the assessee, he must record reasons for his conclusion. These safeguards which are implicit in the requirements of fairness and fair procedure under Art. 14 must be observed by the AO when he arrives at his satisfaction under sub-s. (2) of s. 14A.-M.A. Rasheed vs. State of Kerala AIR 1974 SC 2249 relied on."

5.9 In the case of Godrej & Boyce Mfg. Co. Ltd. Vs. DCIT & Anr., (2010) 328 ITR 0081, the Hon'ble Bombay High Court has clearly held that the provisions of sub-ss. (2) and (3) of s. 14A are constitutionally valid and further provisions of Rule 8D are

not ultra-vires to the provisions of s. 14A, and do not offend Art. 14 of the Constitution. It was further held by the Hon'ble Bombay High Court that in view of clear enunciation in the Memorandum Explaining the provisions of the Finance Bill, 2006 and further clarification by CBDT, vide Circular No. 14 of 2006, the sub-section (2) of section 14A is applicable from asst. yr. 2007-08 onwards, and the provisions of Rule 8D, which have been notified w.e.f. 24th March, 2008 are applicable with effect from A.Y. 2008-09.

5.10 In the case of ACIT Vs. Citicorp Finance (India) Ltd. (2007) 108 ITD 0457, the Hon'ble ITAT Mumbai 'C' Bench has held that it is not correct to say that dividend income can be earned by incurring no or nominal expenses and all expenses connected with such exempt income have to be disallowed under s. 14A regardless of whether they are direct or indirect, fixed or variable and managerial or financial. The relevant observations of the Hon'ble ITAT in this regard are as below:-

> *"Sec. 14A clearly makes a distinction between exempt income and taxable income. It treats both of them as separate classes for computation of income after allocation of expenditure relating thereto and mandates that no deduction in respect of any expenditure shall be allowed against taxable income which is incurred in relation to exempi income. The underlying object is to compute both the exempt income and taxable income correctly, which is possible only after the expenditure incurred in relation thereto is allocated to them. In other words, s. 14A bars the deduction of expenditure incurred in relation to exempt income out of taxable income, as this would have the effect of artificially inflating the exempt income and thereby deflating the taxable income. The prohibition for allowing the deduction under s. 14A for and from usst. yr. 1962-63 is "in respect of expenditure incurred by the assessee in relation to income" which does not form part of the total income. The term "expenditure" occurring in s. 14A would take in its sweep not only direct expenditure but also all forms of expenditure regardless of whether they are fixed, variable, direct, indirect, administrative, managerial or financial. The phraseology used in s. 14A prohibiting the deduction in respect of expenditure incurred by the assessee in relation to exempt income is thus wide enough to cover all forms of expenses provided they have some connection with the exempt income. This is based on the principle that expenses must be allocated to that income to which they are connected to avoid distortions in the computation of both taxable as well as exempt income.*
>
> *(Paras 11 & 12)*

It is difficult to accept the hypothesis that one can earn substantial dividend income without incurring any expenses whatsoever including management or administrative expenses. By same logic, it is equally difficult to accept that the only expenses involved in earning the dividend income are those incurred on collection of dividend or on encashing a few dividend warrants. A company cannot earn dividend without its existence and management. Investment decisions are very complex in nature. They require substantial market research, day-to-day analysis of market trends and decisions with regard to acquisition, retention and sale of shares at the most appropriate time. They require huge investment in shares and consequential blocking of funds. 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. It is therefore not correct to say that dividend income can be earned by incurring no or nominal expenditure. All expenses connected with the exempt income have to be disallowed under s. 14A regardless of whether they are direct or indirect, fixed or variable and managerial or financial in accordance with law. In this connection, the provisions of sub-s. (2) or (3) of s. 14A inserted by the Finance Act, 2006 deserve to be noted. The procedure for computation of disallowance has now been provided in sub-ss. (2) and (3) of s. 14A. It is no longer open to the AO to apply his discretion in computing the disallowance or make ad hoc disallowance under s. 14A. Substantive provisions are contained in sub- s. (1) of s. 14A prohibiting deduction in respect of expenditure incurred in relation to exempt income while procedural provisions regarding computation of the aforesaid disallowance are contained in sub-ss. (2) and (3) thereof. Sub-ss. (2) and (3) seek to achieve the underlying object of s. 144(1) that any expenditure incurred in relation to exempt income should not be allowed deduction. It is fairly well-settled by a catena of decisions that procedural provisions apply to all pending matters and that the rule against retrospectivity does not hit them. AO is statutorily required to compute the disallowance in the manner provided by sub-ss. (2) and (3) of s. 14A. Therefore the orders passed by the CIT(A) and the AO in this behalf are set aside and the matter is restored to the AO for a fresh examination and decision in the light of the provisions of s. 141 including sub-ss. (2) and (3) thereof, in accordance with law. Southern Petro Chemical Industries vs. Dy. CIT (2005) 93 TTJ (Chennai) 161, Harish Krishnakant Bhatt vs. ITO (2004) 85 TTJ (Ahd) 872: (2004) 91 ITD 311 (Ahd), Dy. CIT vs. S.G.

Investments & Industries Ltd. (2004) 84 TTJ (Kol) 143: (2004) 89 ITD 44 (Kol) and Asstt. CIT vs. Premier Consolidated Capital Trust (I) Ltd. (2004) 83 TTJ (Mumbai) 843 relied on.

(Paras 13 to 15 & 17)"

5.11 The plea of the assessee company that no finance cost has been incurred for investing in the shares of group companies is also not borne out from the facts on record. The utilization of the secured and unsecured loans raised by the assessée company during the year under consideration has not been filed during the course of the proceedings. The assessee company has not given any allocation of expenses between the various business activities, namely exempt and taxable. In view of this, it is a fit case which attracts the provisions of Section 14A read with Rule 8D.

5.12 The provisions of Section 14A clearly make a distinction between exempt income and taxable income. It treats both of them as separate classes for the purposes of computation of income and mandates that no deduction in respect of any expenditure shall be allowed against taxable income, which is incurred in relation to exempt income. The underlying object is to compute both the exempt income and taxable income separately and correctly, which is possible only after the expenditure incurred in relation to each category of income is allocated properly.

5.13 In other words, Section 14A bars the deduction of expenditure incurred in relation to exempt income out of taxable income as this would have the effect of artificially inflating the exempt income and thereby deflating the taxable income. The term "expenditure" occurring in section 14A takes into its sweep not only direct expenditure but also all forms of expenditure, regardless of whether they are fixed, variable, direct, indirect, administrative, managerial or financial. The phraseology used in section 14A prohibiting the deduction in respect of expenditure incurred by the assessee in relation to exempt income is thus wide enough to cover all forms of expenses provided they have a bearing with the exempt income. This is based on the principle that expenses must be allocated to that income to which they are connected to avoid distortions in the computation of both taxable as well as exempt income.

5.14 It is difficult to accept the hypothesis that one can earn exempt income without incurring any expenses. By same logic, it is equally difficult to accept that the only expense involved in earning the dividend income are those incurred on collection of dividend or on en-cashing a few dividend warrants. A company cannot earn dividend without the active involvement and participation of the management. Investment decisions are very

complex in nature and needs special attention of the top management. They require substantial market research, analysis of market trends and decisions are required to be made with regard to acquisition, retention and sale of such shares/investments at the most appropriate time. They require huge investment and consequential blocking of funds. 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 Board meetings of the company for which administrative expenses are incurred. So, it will not be correct to assume that dividend income can be earned by incurring nil or nominal expenditure. Such expenses, relating to the investments made for earning exempt income have to be disallowed as per section 144 of the Income Tax Act. Further, the intention of the legislature was not to allow any expenditure against the tax free income. Therefore, section 14A was inserted by the Finance Act, 2001 with retrospective effect from 1.4.1962.

5.15 The term "expenditure" has been defined at page 598 of Black's Law Dictionary (Seventh Edition) as: "1. The act or process of paying out disbursement. 2. A sum paid out". There, the term "expense" has been defined at the same page of the aforesaid dictionary as follows: "An expenditure of money, time, labor, or resources to accomplish a result; esp., business expenditure chargeable against revenue for a specific period- expense." The "expense has many forms, namely accrued expense, administrative expense, business expense, capital expense, capitalized expense, current expense, deferred expense, funeral expense, general administrative expense, medical expense, moving expense, operating expense, ordinary and necessary expense, organizational expense, out-of-pocket expense, prepaid expense, travel expense. The term "expenditure" occurring in section 14A would thus take in its sweep not only direct expenditure but also all forms of expenditure.

5.16 The term "incur" has been defined at page 771 of the aforesaid dictionary as follows: "incur, to suffer to bring on oneself (a liability or expense)." One of the meanings given to the word "relate" under the head "Law" at page 2534 in "The New Shorter Oxford English Dictionary" (1993 Edition) is "Have some connection with, be connected to." The phraseology used in section 14A prohibiting the deduction in respect of expenditure incurred by the assessee in relation to exempt income is thus wide enough to cover all form of expenses provided they have some connection with the exempt income.

5.17 This is also required as per the matching principle of accountancy. In Taparia Tools Ltd. Vs. Jt. CIT (2003) 260 ITR

102, the Hon'ble High Court has explained the matching principle as follows:-

"Under this matching concept, revenue and income earned during an accounting period, irrespective of actual cash in-flow, is required to be compared with expenses incurred during the. same period, irrespective of actual out-flow of cash. In this case, the assessee is following the mercantile system of accounting. This matching concept is very relevant to compute taxable income"

5.18 In view of the above factual and legal position and following the DRP's order for A.Y. 2010-11 on this issue, the disallowance made by the A.O. u/s 14A amounting Rs. 8,44,38,527/- is upheld and the objection raised by the assessee company is rejected."

8.2 In view of the above factual and legal position and following the DRP's order for A.Y. 2011-12 on this issue, the disallowance made by the A.O. u/s 14A is upheld and the ground of objection raised by the assessee company is rejected."

15.2 Material facts remaining same during the year under reference, following the views and findings of the DRP on this issue in earlier years, we upheld the disallowance made by the AO u/s.14A. The ground of objection is rejected accordingly."

5.18 Elaborating further, the learned counsel submitted that the assessee had, on its own accord, disallowed a sum of ₹9,46,335 as administrative expenditure attributable to earning exempt income. Such disallowance was computed by allocating a reasonable percentage of the salaries of the CFO, Deputy CFO, Head of Treasury, and other treasury staff, together with an allocation of overheads to the extent of 10%. Before rejecting this computation and resorting to Rule 8D, it was incumbent upon the Assessing Officer to record a clear, objective, and reasoned dissatisfaction with the assessee's claim.

5.19 It was emphasised that any deficiency in the recording of such dissatisfaction cannot be cured at the appellate stage, as the validity of invocation of Rule 8D must be tested solely on the reasons recorded by the Assessing Officer. The satisfaction so recorded is subject to judicial scrutiny and cannot be supplemented or improved upon subsequently.

5.20 The learned counsel further submitted that, prior to the insertion of Rule 8D, disallowance under section 14A was required to be made on a reasonable basis. For assessment years up to 2007–08, the method adopted by the assessee, namely, allocation of a proportion of salary costs of key managerial and treasury personnel along with overheads, had been consistently accepted by the Revenue and affirmed by appellate authorities. It was contended that a method found to be reasonable and acceptable in earlier years could not, in the absence of any material change in facts, be rejected as unsatisfactory in subsequent years.

5.21 With reference to the investment schedule, it was submitted that there was no substantial change in the investment portfolio during the relevant year, except for a reduction in shareholding in Oriental Hotels Ltd. and a reclassification of certain investments from current to non-current. Dividend receipts were credited electronically, and no significant administrative effort was required for such activity. In these circumstances, the allocation of administrative expenses made by the assessee was asserted to be fair and reasonable.

5.22 It was further contended that, apart from making broad and presumptive observations, neither the Assessing Officer nor the Dispute Resolution Panel recorded any specific finding as to why the *suo-motu* disallowance made by the assessee was incorrect. Despite acknowledging the fact of such disallowance in the assessment order, the Assessing Officer proceeded, while recording satisfaction, on an erroneous premise that no disallowance had been made at all. Reliance was placed on the Special Bench decision in *Daga Capital Management Pvt. Ltd.(supra)* to invoke Rule 8D mechanically, without due application of mind to the assessee's accounts or computation. Such an approach, it was submitted, was contrary to law and vitiated the disallowance.

5.23 In support of the proposition that recording of objective satisfaction is a mandatory jurisdictional requirement before invoking Rule 8D, the learned counsel placed reliance on authoritative judicial pronouncements. Reference was made to the judgment of the Hon'ble Supreme Court in *Godrej & Boyce Manufacturing Co. Ltd.(supra)*, wherein it was held that Rule 8D can be applied only after the Assessing Officer records satisfaction, having regard to the accounts of the assessee, that the claim made by the assessee is not correct.

5.24 Reliance was also placed on the decision of the Hon'ble Supreme Court in Maxopp Investment Ltd. v. CIT (2018) 402 ITR 640(SC) which reiterated that where the assessee has made a *suo-*

motu disallowance, the Assessing Officer must record a reasoned dissatisfaction before rejecting such claim and applying Rule 8D.

5.25 The learned counsel further drew support from decisions of the jurisdictional High Court and of various coordinate benches of the Tribunal, including PCIT v. Bombay Stock Exchange Ltd. (2020) 113 taxmann.com 303 ; PCIT v. Tata Capital Ltd. (2024) 161 taxmann.com 557and CIT v. Sesa Goa Ltd. (2021) 436 ITR 17; VIP Industries Ltd. v. DCIT in ITA No.4135/Mum/2023 ; M/s Greatship (India) Ltd. v. NFAC in ITA No. 650/Mum/2022 for AY 2017-18 and HDFC Bank Ltd., Mumbai-ITAT, AY 2002-03 TO 2020-21, order dt. 28.01.2025 , wherein it has been consistently held that a mechanical or presumptive invocation of Rule 8D, without objective satisfaction based on the assessee's accounts, is unsustainable in law. Applying these principles to the facts of the present case, it was submitted that the Assessing Officer having failed to record the requisite satisfaction, the disallowance under section 14A ought to be restricted to the amount of *suo-motu* disallowance made by the assessee.

5.26 On the contrary, the Ld. DR relied on the order of the lower authorities.

5.27 We have heard rival submissions of the parties and perused the relevant materials on record. The principal contention of the assessee that the Assessing Officer failed to record

dissatisfaction with regard to the suo motu disallowance made under section 14A cannot be accepted. A perusal of paragraph 4.1 of the assessment order clearly reveals that the Assessing Officer recorded reasons for his dissatisfaction. He observed that investments of the magnitude held by the assessee cannot be managed without incurring inherent expenditure towards market analysis, specialised expertise, and continuous monitoring. He further noted that such activities necessarily involve generation and evaluation of daily, fortnightly, and monthly reports to facilitate informed decisions regarding deployment and redemption of investments. The Assessing Officer also referred to various heads of expenditure and observed that, though such costs may not be capable of precise quantification, their incurrence was inevitable. He, therefore, found the overhead allocation adopted by the assessee to be unsatisfactory and proceeded to invoke Rule 8D, placing reliance on the decision of the Special Bench of the Tribunal in *Daga Capital Management Pvt. Ltd.(supra)*

5.28 Consequently, the Assessing Officer computed disallowance of interest under Rule 8D(2)(ii) at ₹62,83,338 and disallowance of administrative expenditure under Rule 8D(2)(iii) at ₹4,33,57,250, aggregating to ₹4,96,40,588. After reducing the suo motu disallowance of ₹9,46,335 already made by the assessee, a net addition of ₹4,86,94,253 was made.

5.29 On examination of the suo motu disallowance made by the assessee, we find that no rational or cogent basis was furnished for restricting the salary cost of the CFO, Deputy CFO, and Head of Treasury to 1%. The allocation appears to have been made purly on an ad hoc and arbitrary basis, unsupported by any evidence such as work allocation or time spent on investment-related activities. Similarly, no basis was explained for estimating 5% of the salary of certain employees, nor were the names or roles of such employees identified. Further, no justification was provided for allocating overheads at 10% of the salary so apportioned. In the absence of any rational or scientific basis, the estimation adopted by the assessee cannot be accepted as reasonable.

5.30 In these circumstances, we find no infirmity in the rejection of the assessee's contention that no dissatisfaction had been recorded by the Assessing Officer. The judicial precedents relied upon by the assessee are distinguishable on facts, as in the present case the Assessing Officer has recorded a reasoned and objective dissatisfaction with the assessee's claim.

5.31 As regards the plea of consistency, it is well settled that the principle of res judicata has no application to income-tax proceedings and each assessment year is a separate and independent unit. The quantum of investments and the extent of investment activity may vary from year to year. Therefore, the acceptance of a particular method of disallowance in earlier years

does not preclude examination of the claim on its own merits in the year under consideration.

5.32 However, insofar as disallowance of interest expenditure under Rule 8D(2)(ii) is concerned, we find merit in the assessee's contention. The Hon'ble Bombay High Court in *CIT v. Reliance Utilities and Power Ltd.* [(2009) 313 ITR 340 (Bom)] has held that where an assessee possesses sufficient interest-free funds exceeding the value of investments, a presumption arises that such investments were made out of own funds, and no disallowance of interest is warranted. In the present case, the assessee has demonstrated availability of interest-free funds far in excess of the investments made. Accordingly, no disallowance under Rule 8D(2)(ii) can be sustained.

5.33 With regard to disallowance of administrative expenditure under Rule 8D(2)(iii), the same is liable to be made. However, the Special Bench of the Tribunal in *ACIT v. Vireet Investment Pvt. Ltd.* [(2017) 58 ITR (T) 313 (SB)] has held that, for the purpose of computing disallowance under Rule 8D(2)(iii), only those investments which have actually yielded exempt income during the relevant previous year are to be considered. Respectfully following the said decision, we direct the Assessing Officer to recompute the disallowance under Rule 8D(2)(iii) in accordance with law. In the result, the ground no. 2 of appeal raised by the assessee is **partly allowed for statistical purposes**..

6. The ground No. 3 of the appeal relates to disallowance of deduction under section 80IA of the Act. Before us, the Ld. counsel for the assessee also raised an additional grounds concerning the deduction u/s 80IA of the Act, which is reproduced as under:

> *1. That the profits eligible for deduction under section 80-IA of the Income-tax Act, 1961 in respect of transfer of steam from the 80-IA eligible undertaking ought to have been computed by taking its market value instead of cost.*

6.1 Having carefully heard the rival submissions on the question of admissibility of the additional ground and upon a holistic consideration of the material placed on record, we proceed to determine whether the assessee has made out a legally sustainable case for its admission.

6.2 The Ld. counsel for the assessee has referred to the decision of the Hon'ble Supreme Court in the case of National Thermal Power Co. Ltd. v. CIT reported in 229 ITR 383 (SC). In the said case the assessee had raised an additional ground urging that interest earned by it on deposit placed during construction period should be reduced from the capital work in progress and need not be separately reflected as income. In paragraph 3 thereof, the Hon'ble Court has noted that the said additional ground was raised by the assessee as it learned that the interest income was not taxable in view of two orders of the Special Benches of the Tribunal in the cases of Arasan Aluminum Industries (P) Ltd (supra) & Nagarjuna Steels Ltd. (supra). **In the case, though the facts as necessary for**

adjudicating the additional ground formed part of the record, the Hon'ble Supreme Court held that if where investigation of fresh facts is required, the appellate authorities have discretion to allow or not to allow a new ground to be raised. The relevant finding of the Hon'ble Supreme Court is reproduced as under:

> *"5. Under section 254 of the Income-tax Act, 1961, the Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit. The power of the Tribunal in dealing with appeals is, thus, expressed in the widest possible terms. The purpose of the assessment proceedings before the taxing authorities is to assess correctly the tax liability of an assessee in accordance with law. If, for example, as a result of a judicial decision given while the appeal is pending before the Tribunal, it is found that a non-taxable item is taxed or a permissible deduction is denied, we do not see any reason why the assessee should be prevented from raising that question before the Tribunal for the first time, so long as the relevant facts are on record in respect of that item. We do not see any reason to restrict the power of the Tribunal under section 254 only to decide the grounds which arise from the order of the Commissioner(Appeals). Both the assessee as well as the Department have a right to file an appeal/cross-objections before the Tribunal. We fail to see why the Tribunal should be prevented from considering questions of law arising in assessment proceedings although not raised earlier.*
>
> *6. In the case of Jute Corpn. of India Ltd. v. CIT [1991] 187 ITR 688, this Court, while dealing with the powers of the AAC, observed that an appellate authority has all the powers which the original*

authority may have in deciding the question before it subject to the restrictions or limitations, if any, prescribed by the statutory provisions. In the absence of any statutory provision, the appellate authority is vested with all the plenary powers which the subordinate authority may have in the matter. There is no good reason to justify curtailment of the power of the AAC in entertaining an additional ground raised by the assessee in seeking modification of the order of assessment passed by the ITO. This Court further observed that there may be several factors justifying the raising of a new plea in an appeal and each case has to be considered on its own facts. The AAC must be satisfied that the ground raised was bona fide and that the same could not have been raised earlier for good reasons. The AAC should exercise his discretion in permitting or not permitting the assessee to raise an additional ground in accordance with law and reason. The same observations would apply to appeals before the Tribunal also.

7. The view that the Tribunal is confined only to issues arising out of the appeal before the Commissioner (Appeals) takes too narrow a view of the powers of the Tribunal - vide, e.g., CIT v. Anand Prasad [1981] 128 ITR 388/ 5 Taxman 308 (Delhi), CIT v. Karamchand Premchand (P.) Ltd. [1969] 74 ITR 254 (Guj.) and CIT v. Cellulose Products of India Ltd. [1985] 151 ITR 499/[1984] 19 Taxman 278 (Guj.) (FB). Undoubtedly, the Tribunal will have the discretion to allow or not allow a new ground to be raised. But where the Tribunal is only required to consider a question of law arising from the facts which are on record in the assessment proceedings we fail to see why such a question should not be allowed to be raised when

it is necessary to consider that question in order to correctly assess the tax liability of an assessee.

8. The reframed question, therefore, is answered in the affirmative, i.e., the Tribunal has jurisdiction to examine a question of law which arises from the facts as found by the authorities below and having a bearing on the tax liability of the assessee. We remand the proceedings to the Tribunal for consideration of the new grounds raised by the assessee on the merits."

6.3 Therefore, the fundamental principle which has been laid down is that the appellate authority must be satisfied that the ground raised was bonafide and the same could not have been raised earlier for good reasons.

6.4 Further, the Ld. counsel for the assessee referred to the decision of the Hon'ble Supreme Court in the case of Jute Corporation of India Ltd. v. CIT [1991] 187 ITR 688 (SC). , wherein Hon'ble Supreme Court was concerned with a case where assessee claimed deduction in respect of liability towards purchase tax when its appeal was pending before the AAC. The said claim had been made based on judgment of the Supreme Court in the case of Kedarnath Jute Mfg. Co. Ltd v. CIT (1971) 82 ITR 363. After analysing the powers of the appellate authority as per section 251 of the Act **in paragraph -3** the Hon'ble Supreme Court observed

".....The Act does not contain any express provision debarring an assessee from raising an additional ground in appeal and there is no provision in the Act placing restriction on the power of the appellate

authority in entertaining an additional ground in appeal. In the absence of any statutory provision, general principle relating to the amplitude of appellate authority's power being co-terminus with that of the initial authority should normally be applicable. But this question for the purposes of the Act has been an intricate and vexed one. There is no uniformity in the judicial opinion on this question".

6.5 Thereafter, **in para 6** while dealing with an earlier judgment of the Apex Court in Gurjargravures (P) Ltd., the Hon'ble Court observed as under:

".....The above observations do not rule out a case for raising an additional ground before the AAC if the ground so raised could not have been raised at that particular stage when the return was filed or when the assessment order was made or that the ground became available on account of change of circumstances or law. There maybe several factors justifying raising of such new plea in appeal, and each case has to be considered on its own facts. If the AAC is satisfied he would be acting within his jurisdiction in considering the question so raised in all its aspects. ***Of course, while permitting the assessee to raise an additional ground, the AAC should exercise his discretion in accordance with law and reason.*** *He must be satisfied that the ground raised was bona fide and that the same could not have been raised earlier for good reasons. The satisfaction of the AAC depends upon the facts and circumstances of each case and no rigid principles or any hard and fast rule can be laid down for this purpose."*

6.6 Thus the ratio of the above decision is that discretion of permitting or not permitting an additional ground by the appellate

authority has to be in accordance with law and reasons. We note that the Hon'ble Supreme Court in the case of National Thermal Power Co. Ltd. (supra) has considered the decision of the Hon'ble Supreme Court in the case Jute Corporation of India Ltd. (supra).

6.7 We find that the Hon'ble Bombay High Court in the case of Ultratech Cement Ltd. v. Additional CIT reported in 81 taxmann.com 74 (Bombay) upheld the conclusion reached by the Tribunal in that case rejecting the admission of the additional ground for deduction u/s 80IA of the Act raised based on the finding in another year. The Hon'ble High Court **in paragraphs 22 and 23** while dealing with the Full Bench judgment in the case of Ahmedabad Electricity Co. Ltd. v. CIT (1993) 199 ITR 351, noted that additional ground in the case before the Full Bench, had been raised in view of a judgment of the Bombay High Court in the case of Amalgamated Electricity Co. Ltd.(supra), wherein, it was held that deduction had to be allowed in respect of amounts transferred to contingency reserve and dividend control reserve. Referring to the aforesaid judgment of the Apex Court in the case of Jute Corporation of India Ltd. (supra), it is observed

> "*.....The Full Bench observed that the Apex Court in Jute Corporation of India Ltd. (supra) made reference to the decision of the Apex Court in Addl. CIT v. Gurjargravures (P.) Ltd. [1978] 111 ITR 1, and held that it does not prohibit the raising of an additional ground before the appellate authority, when the ground so raised could not have been raised before the Assessing Officer or the ground now becomes available in view of*

changed circumstances such as a decision of a Court allowing a particular deduction.

23. Therefore, before an additional ground is allowed to be raised, the appellate authority must be satisfied that the ground raised could not have been raised earlier for good reasons. The underlying basis for allowing the raising the additional ground in the case of Ahmedabad Electricity Co. Ltd. (supra) was the subsequent decision rendered by this Court in Amalgamated Electricity Co. Ltd. (supra) when appeal was pending. As held by the subsequent decisions of the Apex Court in National Thermal Power Corporation Ltd. (supra), a judicial decision when an appeal is pending will entitle raising of additional ground."

6.8 Thereafter, **in paragraph 27**, the Hon'ble Court has further observed as under:

"27. *There can be no dispute that whether or not to allow an additional ground to be raised before the appellate authority is to be decided by the appellate authority in exercise of its discretion considering the facts and circumstances of the case before it. Where only a pure question of law arises from facts which are already on record, then there is no reason why the appellate authority should not consider the question of law so as to determine the correct tax liability of an assessee in accordance with law. However, where evidence is to be examined and that is not on record, then it will be considered only if the parties seeking to raise the additional ground satisfies the authority concerned that for good and sufficient reasons, the ground could not be raised before the lower authorities. In the present facts, no such ground has been made out by the Appellant before the Tribunal....."*

6.9 Therefore, whether an assessee has been able to make out a case showing good and sufficient reasons for not raising the ground before the lower authorities would be relevant.

6.10 In view of the above decisions, it is evident that if no investigation of the fresh facts is required, then additional ground should normally be accepted by the appellate authorities but where facts relating to the issue raised in the additional ground are not available on record and investigation of the fresh facts is required, the party seeking to raise the additional ground has to satisfy the authority that for good and sufficient reason, the ground could not raised before the lower authorities.

6.11 At the outset, it is beyond dispute that the power of the Tribunal under section 254 of the Income-tax Act, 1961, is wide and enabling, intended to advance the cause of correct determination of tax liability in accordance with law. Equally well settled, however, is the principle that the exercise of such power is **discretionary and not automatic**, and must be guided by **judicial discipline, bona fides of the party seeking indulgence, and the stage and manner in which the plea is sought to be introduced**.

6.12 Before us, the Ld. counsel for the assessee submitted that the assessee has two captive power plants at Mithapur in Gujarat being Power plant - 'Turbine ECT-11 & LPT-10' and 'Turbine TT-12'. The assessee submitted that the first power plant commenced its

operation on 07.01.2002 and the assessee claimed deduction under section 80-IA in respect of the profits derived from the said plant from AY 2009-10. The second power plant commenced its operations on 14.09.2009 and deduction under the said section has been claimed from AY 2013-14. The Form 10CCB i.e. form prescribed for deduction u/s 80IA , including the audited financial statements of the first unit are available at pages 164 to 177 of Paper Book 2, wherein, the Profit and Loss Account is at page 172 and the computation of income in respect thereof is at page 169 and the said Form is available at pages 164 to 167. Along with the audited financial statements Notes to accounts have also been annexed, wherein, in Note 4 it has been clarified that "*The sale of steam generated by the power plant has been recorded at cost of producing the same.* ***The sale of steam could not be recorded at fair market value as there is no ready market for steam i.e., steam is not a marketable product under the facts and circumstances of the company.*** *Similarly cost of steam consumed is also booked at its cost of production."* In Note 3 thereof, it is explained that sale of power has been recorded at an amount equivalent cost of power if such power would have been purchased from the local state electricity board that is Gujarat State Electricity Board. Form 10CCB including the audited financial statements of the second unit are at pages 178 to 191 of Paper Book 2, wherein, the Profit and Loss Account is at page 187**,** the computation of income in respect thereof is at page 184 and the said Form is at

pages 178 to 181. Similar notes, with respect to method of computation of transfer value for sale of power and sale of steam is also placed in the notes to the audited financial statements of the second unit. It is submitted that, insofar as the disclosure as made in the audited financial statement is concerned, it has continued to remain the same year after year.

6.13 By its letter dated 06.02.2024, the assessee raised an additional ground of appeal urging that for the purposes of computing profits eligible for deduction under section 80-IA of the Act, the transfer of steam has to be computed by taking its market value instead of cost.

6.14 The assessee invited our attention to the application dated 06.02.2024 filed by before the Tribunal on 07.02.2024 *inter-alia* pointing out *that in the course of appeal hearing for AY 2019-20, on 01.01.2024, one of the issues raised by the Hon'ble Bench was why the market price prevailing on the Indian Energy Exchange should not be considered for the purpose of valuing the transfer of power by the eligible undertaking. While carrying out research on the aforesaid aspect, in the month of January 2024, it came across the Tribunal order in the case of Nectar Lifesciences Ltd. v. DCIT in ITA No. 1497/Chd/2019 pronounced on 17.02.2022 by Chandigarh Bench of the Tribunal (**see pages 509 to 526 of Paper Book-7**). After due consultation with its Counsel and the Chartered Accountants, it*

decided to file the additional ground which came to be filed along with the aforesaid application.

6.15 Based thereon, the assessee submitted that, prior to January 2024 it genuinely believed that though the sale of steam had to be recorded at fair market value, it had to record the same at cost of producing the same in the absence of a readily available market value. The ld Counsel for the assessee before us referred to the decision of Coordinate Bench of Tribunal in the case of assessee for AY 2019-20, where also similar additional ground was raised , which has been admitted by the Tribunal. The relevant finding of the Tribunal is reproduced as under:

> *"15. We heard the parties and perused the material on record. The assessee through additional ground is claiming that in respect of transfer of steam from the 80-IA eligible undertaking ought to have been computed by taking its market value instead of cost. From the perusal of the financial statements of the assessee (page 3 of paper book) it is clear that the assessee has accounted the steam consumed from eligible units at cost and has stated in the Notes forming part of Accounts (page 9 of paper book) that the steam consumed is booked at cost since steam is not a marketable product. The contention of the assessee is that the deduction claimed under section 80IA in the return of income includes steam also wherein the cost and the revenue are same resulting in zero claim. Therefore through additional ground it is contended that the sale value needs to be considered at market value and this claim is based on the decision of the Chandigarh Bench of the Tribunal in the case of*

Nectar Lifesciences Ltd (supra). Revenue's contention is that the assessee itself has admitted that steam is not a marketable product thereby the deduction under section 80IA could not have been made and accordingly it is a fresh claim not made neither in the return of income nor in the relevant form claiming 80IA. Therefore it is argued that the additional ground should not be accepted.

16. We notice from the perusal of record that the steam and power have been considered together while arriving at the profits eligible for deduction under section 80IA and the assessee in Form 3CEB has considered the transfer of steam at cost as being at arm's length by stating that the market value steam cannot be determined as there is no open market for steam. Accordingly we see merit in the contention that the claim made through additional ground is a not fresh one but is only an incremental claim towards transfer at market value instead of cost. Now coming to the issue of whether a claim which was not made before the lower authorities can be made for the first time before the Tribunal through additional ground we rely on the decision of the Hon'ble Supreme Court in the case of National Thermal Power Co. Ltd. vs CIT ([1998] 97 Taxman 358 (SC)) where it has been held that –

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17. In the given case, the issue raised in additional ground i.e. the claim of deduction under section 80IA towards transfer of steam on the basis of market value is legal issue and that relevant facts pertaining to the same except how to determine the market value of steam are already part of the records. The next question is whether there is any bona fide reason for raising this additional ground

before the Tribunal. The assessee in the submissions has stated that the additional ground is raised based on the decision of the Tribunal which the assessee was not aware of at the time of assessment or at the time of appellate proceeding before DRP. We are of the considered view that the assessee has a reasonable cause for not raising the issue before the lower authorities and therefore we are inclined to admit the additional ground for adjudication by placing reliance on the decisions of the Apex Court in the case of National Thermal Power Co. Ltd (supra) and Jute Corpn. of India Ltd (supra)"

6.16 Based on above submissions, the ld Counsel for the assessee prayed that Tribunal may be pleased to admit this additional ground and remit the issue back to AO for consideration of the market value to be taken for sale of steam.

6.17 The assessee in the return of income filed, while claiming deduction u/s 80IA of the Act from captive power plant, bifurcated its cost of the captive power plant in two parts, first part as cost for generation of electricity and second part as cost for generation of steam. While valuing the sale price of electricity transferred from captive power plant to other units , the assessee valued at rates of Gujrat Electricity Board at which the assessee used to buy electricity , but the value of steam was done at cost only as according to the assessee , there was no market for steam and therefore, there can't be a market value for the same.

6.18 The Ld. counsel has further submitted that when it came across the decision of the Chandigarh Bench in the case of Nectar

Lifesciences Limited in ITA No. 1497/Chd/2019 pronounced on 17.02.2022 considered to claim deduction for transfer of estimate market value under the provisions of section 80IA of the Act.

6.19 The jurisprudence consistently laid down by the Hon'ble Supreme Court makes a clear distinction between:(i) a pure question of law arising from admitted facts already on record; (ii) a mixed question of fact and law where all material facts are available on record; and(iii) cases where adjudication of the new plea would require investigation of fresh facts. In the third category, the appellate authority is justified in declining admission unless the party demonstrates **good, sufficient, and bona fide reasons** for not having raised the plea earlier.

6.20 Applying the aforesaid principles to the facts before us, we find that the additional ground sought to be raised by the assessee does not fall within the first or second category. The assessee has, throughout, consciously treated the transfer of steam from its captive power plant at cost, categorically stating in its audited financial statements that steam is not a marketable product and that no ascertainable market value exists. The annual report of the company with detailed notes to account considering the steam as non marketable commodity was duly approved by the Board of Directors and presented to its shareholders. This treatment was consistently adopted in the return of income as well as during the

assessment proceedings and formed the very foundation of the claim under section 80-IA.

6.21 The additional ground now raised seeks to fundamentally alter this position by contending that the transfer of steam ought to be valued at market value. Such a plea necessarily entails examination of technical, commercial, and factual aspects relating to the alleged marketability of steam and the method of determining its market value—issues which were neither examined by the Assessing Officer nor form part of the existing record.

6.23 Significantly, the assessee has failed to demonstrate any compelling or sufficient reason explaining why this plea could not have been raised earlier. The reliance placed on a subsequent order of a coordinate bench does not, in the facts of the present case, constitute a change in law or a binding judicial development warranting admission of a new ground. The plea sought to be raised is not a correction of an inadvertent legal omission but an attempt to re-engineer the computation mechanism consciously adopted by the assessee itself.

6.24 We also find merit in the Revenue's contention that the generation of steam is not an independent profit-earning activity but an integral part of the electricity generation process. The subsequent attempt to ascribe a notional market value to such transfer, after having consistently treated it at cost, cannot be

regarded as a bona fide plea raised in the interest of correct legal adjudication.

6.25 The captive power plant generate electricity where turbine is rotated by force of steam and thus generation of steam is prime requirement of electricity generation and it is not the case the assessee is separately generating steam, for use as a power source so as to mark the cost of steam separately. In our opinion it seems that the assessee has done this bifurcation of cost so that it can create more profit in generation of electricity. So there is no bonafide intention on the part of the assessee in raising the additional ground. The assessee itself has considered the transfer of the steam from its captive power plant to another unit at cost and now want to transfer the same at the fair market value which was neither determined at the stage of filing return of income or at the stage of the assessment proceedings.

6.26 In these circumstances, we are not satisfied that the assessee has discharged the burden cast upon it to justify admission of the additional ground. The discretion vested in this Tribunal, when exercised in accordance with settled principles of law, does not warrant admission of additional ground.

6.27 Accordingly, the additional ground raised by the assessee is held to be **devoid of bona fides and unsupported by good and**

sufficient reasons for its non-raising before the lower authorities. The same is, therefore, **declined admission**.

6.28 We also note the assessee filed a copy of additional evidence in relation to the issue of valuation of steam comprising of Engineers' Certificate. The ld DR objected admission of said additional evidences. He submitted as under:

> *Assessee has, vide application dated 30.07.2024, submitted Chartered Engineer's certificate as an additional evidence. By filing additional evidence assessee seeks to revise the sale price of the steam. Vide the Chartred Engineer's certificate it is submitted that rather than Enthalpy or heat content of a steam, the steam's "Available Energy to do the work", also called as Gibbs free energy or 'G', needs to be taken in consideration to determine the pricing of steam. Based on the Gibbs – Helmholz law, the G is computed for each stream of steam. This Gibbs free energy is converted into equivalent Kilowatt hours (Kwh). And by applying the prevalent rate of Gujrat Electricity Board for Kilowatt hour, the pricing of steam is determined.*
>
> *It is humbly prayed that the said proposition is false and liable to be rejected for the following reasons:*
>
> *i. Firstly, the Gibb's free energy or Availability or Exergy, as referred in Chartered Engineer's certificate, represents the ideal or maximum useful work that can be obtained from a given stream of steam as it is brought to equilibrium with its surroundings. The only way to achieve such ideal or maximum useful work is by employing Carnot Cycle which uses reversible thermodynamic processes. In other words, a theoretical and idealized heat engine working on the Carnot cycle, which employs reversible thermodynamic processes, can only generate such maximum possible useful work represented by 'G'. Since Carnot Cycle represents a theoretical ideal cycle therefore same is impossible to execute. Therefore, in reality, the Rankine cycle is used as a practical, real-world cycle that approximates steam power plants. The*

important point to note here is that the efficiency of Rankine cycle is quite less than Carnot Cycle.

ii. Secondly, in real-world power plants, the Rankine cycle faces various inefficiencies such as under:

Irreversible Processes: *Friction in the turbine and pump, heat losses during the process (e.g., heat transfer to the surroundings), and non-isentropic expansion/compression reduce efficiency.*

Pressure Drops: *Pressure losses in the boiler, condenser, and piping reduce the overall efficiency.*

Turbine and Pump Efficiencies: *The real turbine and pump have efficiencies quite less than 100%, meaning they don't deliver the theoretical amount of work.*

Heat Losses: *Heat is lost to the surroundings during the heating and cooling processes.*

Thus, the efficiency of actual steam cycle or steam power plant running on Rankine cycle is just nearly 30% of that of Carnot Cycle. ***In other words, actual useful work extracted from a given stream of steam is only around 30% as compared to maximum possible work that can be extracted, as represented by 'G' i.e. Exergy or Availability of steam.***

iii. In absolute contrast to the above scientific and practical analysis, what assessee is proposing to say that fair market value of steam should be taken at 'G' i.e. 100% of Exergy or Availability of steam. In other words, through additional evidence assessee is submitting that the given stream of steam should be valued by considering that it will deliver work output at ideal 100% efficiency which just cannot be acceptable even by general common logic. The above analysis clearly proves the impossibility of claim which assessee seeks to make at this stage. Therefore, the additional evidence should not be accepted as it is beyond scientific possibilities governing the process of steam power plants.

iv. Further for example if we consider the case of Turbine TT – 12. From the details submitted by the assessee, it is seen that ***the steam at pressure of 1550 psig and temperature of 900 Degree Farhenite generates 6,22,26,000 units of electricity. Then, the pertinent question is how the same amount of steam at pressure of just***

15 to 20 psig and temperature of 350 degree Farhenite can generate 8,30,30,415 units of electricity? *(152.40 * 5,44,819 = 8,30,30,415).* ***In other words the steam at 1550 psig and 900 Degree Farhenite generates electricity worth Rs.38.2 Crores. And how the same amount of steam at just 15 to 20 psig and 350 degree Farhenite can generate electricity worth Rs. 51 Crores?***

v. *In other words, on relying on the computation of Chartered Engineer, the value of G for steam at 1550 psig and 900 Degree Farhenite comes around 589 BTU per lb, which, if converted further, as per the computation of Chartered Engineer, to the equivalent units of Electricity, the same comes around 20,83,40,000 units of Electricity. In other words, the "Available energy to do the work" for a steam of the given quantity of 5,44,819 metric tonns at 1550 psig and 900 Degree Farhenite is around 20,83,40,000 units of Electricity. However, the actual units of electricity generated is only 6,22,26,000 units of electricity. Thus, assessee's own example makes it clear that the actual efficiency of useful work or energy extracted as compared to maximum possible work output is just around 30%. Further at lesser pressure and temperature like 20 psig and 350 degree Farhenite, the thermal efficiency will be even less than 30%. Same is the situation with respect to claim of assessee in regard to other turbine. In such scenario claim of assessee that the maximum work potential of steam should be taken for its valuation is* ***just cannot be acceptable.*** *In other words 100 Kwh of electricity is equivalent to almost 100Kwh of useful work. However, whether steam with G value of 100 Kwh i.e. maximum work potential of 100 Kwh can generate electricity of 100Kwh. Certainly not. It can generate maximum useful work up to 30 % of G value only.*

In view of the above the additional evidence and additional ground filed by assessee be rejected in toto.

6.29 But, since we have already rejected the application of the assessee for raising additional ground, the request of the assessee for admitting additional evidence in relation to the issue does not survive and accordingly also rejected.

7. We now take up Ground No. 3 of the appeal, which pertains to the disallowance of deduction of ₹40,04,53,625/- claimed by the assessee under section 80-IA of the Income-tax Act, 1961, in respect of its captive power plants.

7.1 The Assessing Officer was of the view that the assessee had artificially inflated the profits of the eligible undertaking by notionally treating the generation of steam part of activity eligible for deduction under section 80-IA.

7.2 Before the Assessing Officer, the assessee explained that it had initially set up a power plant comprising HPB-3 and TT-9 during assessment year 1996–97 with a generation capacity of 17.25 MW, which was commissioned on 11 May 1995. Since the period of eligibility for deduction in respect of this plant had already expired, no deduction was claimed in the year under consideration in respect thereof.

7.3 It was further submitted that during assessment year 2002–03, a new power plant comprising ECT-11 and LPT-10 was commissioned, and deduction under section 80-IA was claimed for the first time in assessment year 2009–10. The year under appeal being the seventh year of the eligible period, the assessee claimed deduction of ₹26,75,65,520/- in respect of this plant while filing the revised return of income.

7.4 The assessee further submitted that another power plant comprising TT-12 commenced power generation during assessment year 2010–11. Since depreciation at the rate of 80% was allowable and the unit incurred losses in the initial years, no deduction was claimed in those years. Deduction under section 80-IA was first claimed in assessment year 2013–14 after set-off of past losses. The year under consideration being the third year of such claim, the assessee claimed deduction of ₹13,28,88,105/- in respect of this unit in the revised return of income. It was submitted that audit reports and audit certificates in Form No. 10CCB, as prescribed under the Income-tax Rules, 1962, were duly furnished.

7.5 The assessee explained the process of electricity generation by submitting that boilers produce steam at very high pressure(1550 Unit), which is passed through turbines to reduce pressure. As the steam passes through the turbines, electricity is generated. The steam, after reduction in pressure(450, 120, 20 and 15 Units), is thereafter utilised in the chemical plant for production of soda ash. After its utilisation, the steam condenses and is recycled as feed water for fresh steam generation.

7.6 According to the assessee, the captive power plant supplies both electricity and steam to the chemical unit. It was contended that separate accounts were maintained for boilers and turbines, which together constituted the eligible power generation unit within the meaning of section 80-IA.

7.7 It was further submitted that valuation of outputs of the eligible undertaking was carried out on the basis of market value or cost, as the case may be. Since steam was not a marketable commodity, its transfer to the chemical plant was recorded at cost. Electricity, however, was valued at the rate at which the assessee would have otherwise purchased power from the Gujarat Electricity Board.

7.8 The assessee also submitted that the allocation of costs between steam and electricity was based on thermodynamic principles, reflecting the work potential of steam at various pressure levels, and that such allocation was scientifically justified. The cost relationship was worked out for a steam at various pressure and for electricity, having relationship as under:

450 psig steam	*Rs. 1.000 X per Tones*
120 psig steam	*Rs. 0.764 X per Tones*
50 psig steam	*Rs. 0.683 X per Tones*
15/20 psig steam	*Rs. 0.524 X per Tones*
Electricity	*Rs.0.0032 X per Tones*

7.9 It was further contended that the eligibility of deduction under section 80-IA in respect of electricity generation had already been examined and accepted by the Assessing Officer as well as by appellate authorities in earlier years and, therefore, could not be reopened in the year under consideration.

7.10 Regarding the steam the assessee again submitted that it was not a marketable product and therefore transfer of the steam to other units was considered at cost. The assessee provided detailed note No. 4 and note No. 6/7 to form No. 10CCB. For the contention that production of a steam is a generation of power and eligible for relief under section 80IA, the assessee relied on the decision of DCW Ltd (037 SOT 0322) and Maharaja Shree Ummed Mills Ltd (29 SOT 278) Jaipur Tribunal, Shree Cements Ltd (Jodhpur ITAT.

7.11 The Assessing Officer, however, declined to accept the assessee's contentions and followed the consistent stand taken by the Revenue in earlier assessment years from 2008–09 to 2014–15. He observed that there was no independent cost attributable to generation of steam and that the entire cost of the captive power plant, including boilers and turbines, was incurred for the generation of electricity.

7.12 According to the Assessing Officer, once the entire cost of the plant was allocated to electricity generation, the profit derived from generation of electricity, after reducing the cost of generation from the market value adopted by the assessee, would be nil. Consequently, the deduction allowable under section 80-IA in respect of power generation was also computed at nil.

7.13 On this reasoning, the Assessing Officer denied the deduction claimed by the assessee under section 80-IA of the Act.

7.14 The learned DRP also following its consistent stand, sustained the finding of the Assessing Officer.

7.15 The learned counsel for the assessee, however, extensively argued this ground of appeal and continued his argument on this issue even at the time of the rejoinder. The ld counsel instead of addressing on the cost of electricity generation, which was disputed by the ld AO, he focused his arguments on what should be fair market value of electrical power generated and transferred by the captive power plant to other units of the assessee.

7.16 The learned counsel submitted that assessee is eligible for deduction under section 80 IA in respect of a captive power plant. Though issue was neither contested by the ld AO nor by ld DRP.

7.17 The learned counsel submitted that the assessee's entitlement to deduction under section 80-IA in respect of captive power generation is no longer res integra and, in fact, was not disputed either by the Assessing Officer or by the Dispute Resolution Panel. In this regard, reliance was placed on the orders of the Tribunal in the assessee's own case for assessment years 2006–07 and 2007–08, wherein the entire history of the issue from assessment years 2001–02 to 2005–06 had been examined. It was pointed out that the Tribunal, after considering the judgments of the Madras High Court in the case of Tamilnadu Petro Products Ltd. v. ACIT reported in (2011) 51 DTR (Mad) 67 and the Delhi High Court in CIT vs

Orient Abrassive Ltd. (order dated 31.07.2014) in ITA Nos. 991/2010 and Ors upheld the assessee's claim. The same view was reiterated by the Tribunal for assessment year 2008–09.

7.18 It was further submitted that the legislative intent underlying section 80-IA(8) is explicit. The provision contemplates transfer of goods or services from the eligible undertaking to other businesses of the assessee and mandates that such transfer be valued at market value for the purpose of computing eligible profits. Thus, the statute itself recognises captive consumption. The only statutory requirement is that the valuation must reflect market value. Reliance was placed on the decision of the Hon'ble Bombay High Court in *CIT v. Reliance Industries Ltd.* [(2020) 421 ITR 686], wherein deduction under section 80-IA in respect of power generated by a captive unit was upheld.

7.19 In view of the above, the ld Counsel urged that the Tribunal may be pleased to hold that the Appellant is entitled to claim deduction in respect of captive power plants

7.20 The ld Counsel further argued that why the market value adopted by the assessee while claiming deduction u/s 80IA for transfer of electrical power from captive power plant to other units is correct.

7.21 On the issue of determination of market value of power, the learned counsel submitted that the assessee had correctly adopted

the average rate at which the Gujarat Electricity Board supplies power to its consumers. It was contended that section 80-IA(8), read with the Explanation thereto, permits determination of market value either as the price which the goods would ordinarily fetch in the open market [clause (i)] or, where the transaction is a specified domestic transaction, at the arm's length price in terms of section 92F(ii) [clause (ii)].

7.22 The learned counsel pointed out that the Tribunal, in the assessee's own case for assessment years 2006–07 and 2007–08 (order dated 31.03.2023), had approved adoption of the rate at which power was supplied by the Gujarat Electricity Board to the assessee. The same view was followed for assessment year 2008–09 by order dated 10.11.2023.

7.23 The ld Counsel submitted that this issue again arose in the case of assessee for AY 2017-18, wherein, after treating the transaction to be a specified domestic transaction, the AO had made a reference to the TPO for determination of arms' length price of this transaction. In its Order dated 10.10.2023 the Tribunal has summarized the findings of the TPO The TPO had carried out a FAR analysis of the said transaction to reject its claim. The ld DRP adopted the rate at which power was supplied by Torrent Power Limited to the Gujarat Electricity Board based on determination of such rate by the Gujarat Electricity Regulatory Commission. The Tribunal analyzed the Explanation below Section 80-IA(8) to hold

that the clauses therein give a choice to the assessee to compute the market value of such goods as they would ordinarily fetch in the open market as per clause (i) or by determination of its arms' length price as per section 92F(ii) in accordance with clause(ii). Based thereon and the Judgements of the Jurisdictional High Court in the case of CIT v. Reliance Industries Limited (supra) and the Gujarat High Court in PCIT v. Gujarat Fluorochemicals Limited, The Tribunal upheld the determination of market value as done by the assessee and held that the price charged by Torrent Power Limited for supplying electricity to Gujarat Electricity Board based on such determination by the Gujarat Electricity Regulatory Commission would not be permissible.

7.24 Ld Counsel further submitted that this issue has also been considered by the Tribunal in the appellant's own case for the AY 2019-20 where, by its order dated 28.05.2024, it has again upheld the said position. For the said year again, a reference had been made by the AO to TPO who had determined the arms' length price by adopting the power purchase cost as charged by Gujarat Urja Vikas Nigam Limited for purchasing power from Coal based thermal power generating units in Gujarat. The Tribunal relied upon its earlier order for the AY 2017-18. In paragraph 8 reliance has been placed on judgement of the Hon'ble Supreme Court in the case of CIT v. Jindal Steel & Power Limited (2024) 460 ITR 162. Thereafter, in paragraph 9, the Tribunal concluded that the rates at which

transactions are executed on the Indian Energy Exchange cannot be regarded as a valid comparable for the present purposes. Lastly, in paragraph 10, , assuming that clause (ii) of the Explanation below section 80-IA(8) is applicable, the rate at which the Gujarat Electricity Board supplied power to its customers had been regarded as a valid external CUP for the purposes of determination of arms length price in accordance with the transfer pricing provisions.

7.25 The ld Counsel submitted that in view of the above, it is submitted that both for the earlier as well as the later years and considering either of the clauses of the Explanation below section 80-IA(8), the Tribunal in the appellant's own case has upheld the determination of market value for supply of power in the manner as done by it.

7.26 He reffered to the decision of the Hon'ble Supreme Court in *Jindal Steel & Power Limited, where the hon'ble Court* construed the expression "open market" to mean a price discovered through voluntary interaction between a willing buyer and a willing seller in the normal course of trade, governed solely by the forces of demand and supply and free from statutory or regulatory compulsion. The Court held that a price fixed under a regulatory regime, where the seller has no freedom of choice as to the purchaser and no scope for negotiation, cannot partake the character of an open market price. Where the assessee is statutorily constrained to sell surplus power

only to the State Electricity Board at a tariff unilaterally determined, such price is merely a contracted or imposed price. The absence of competition, bargaining power, and commercial autonomy negates the essential attributes of an open market. Consequently, the tariff fixed by the Electricity Regulatory Commission was held to be an impermissible benchmark for determining open market value.

7.27 He further refffered to the decision of Hon'ble Bombay High Court in *CIT v. Reliance Infrastructure Limited*. In the said case, the Tribunal, after an elaborate analysis, rejected the adoption of the tariff determined by the State Electricity Regulatory Commission as representing the open market price, as discussed in paragraphs 41 to 45 of its order. The Hon'ble High Court, while examining the matter in appeal, expressly affirmed the said findings and, in paragraph 6 of its judgment, upheld the reasoning and conclusion arrived at by the Tribunal.

7.28 The ld Counsel submitted that aforesaid view has subsequently been reiterated and followed by the Hon'ble Bombay High Court in *CIT v. Reliance Industries Ltd.* [(2019) 102 Taxmann.com 372], wherein, in paragraph 7 of the judgment, the Court once again approved the principle that a tariff fixed under a regulatory framework cannot be equated with a price discovered in an open and competitive market.

7.29 The ld Counsel further submitted that in the assessee's own case for Assessment Year 2017–18, while repelling the reliance placed by the Dispute Resolution Panel on the tariff at which M/s Torrent Power Ltd. was supplying electricity to the Gujarat Electricity Board, the Tribunal, in paragraphs 17 and 18 of its order, recorded cogent findings. The Tribunal observed that there was no material to establish that M/s Torrent Power Ltd. was supplying electricity to any entity other than the Gujarat Electricity Board and that the entire sale was confined to a single purchaser. In such a situation, where the sale is exclusively to one entity and the price and attendant conditions are wholly influenced by that entity, even if routed through a regulatory mechanism, the transaction assumes the character of a controlled and tainted transaction. Relying upon the statutory deeming provision contained in section 92A(2)(i) of the Act, the Tribunal held that such price, being influenced by the purchaser, cannot constitute a valid comparable for the purpose of determining the arm's length price. It was accordingly concluded that the tariff at which the Gujarat Electricity Board purchased power from M/s Torrent Power Ltd. was not an appropriate benchmark. The Tribunal thus upheld the price of ₹6.90 per unit, being the price available in the open market and also the price at which the assessee itself procured power from the Gujarat Electricity Board, as representing the true market value. The said position has been consistently followed by the Tribunal in the Appellant's own case for Assessment Year 2019–20.

7.30 He further submitted that in any event, in the present case, the Assessing Officer had made a reference to the Transfer Pricing Officer for determination of the arm's length price of the specified domestic transactions reported in Form No. 3CEB. Pursuant thereto, the Transfer Pricing Officer issued a notice dated 03.11.2017 calling for detailed information. In response, and during the course of the transfer pricing proceedings, the assessee furnished comprehensive submissions dated 30.08.2018 and 18.09.2018, wherein it placed on record the particulars of all specified domestic transactions, the benchmarking methodology adopted for each such transaction, including for the preceding three years, as well as the audited financial statements of the two eligible units claiming deduction under section 80-IA of the Act. Upon due examination of the material so furnished, the Transfer Pricing Officer passed an order dated 30.10.2018 proposing adjustments only in respect of commission on corporate guarantee and interest on preference shares treated as loans. Significantly, no adjustment whatsoever was suggested in respect of the sale of power and sale of steam transactions reported in Form No. 3CEB, thereby evidencing the Transfer Pricing Officer's acceptance of such transactions as being at arm's length. Once this factual position is accepted, and as rightly conceded by the learned Departmental Representative, the provisions of clause (iii) of the Explanation below section 80A(6) or clause (ii) of the Explanation below section 80-IA(8) alone would govern the field. Inasmuch as the arm's length price of the specified

domestic transactions, including the supply of power and steam by the eligible units to the chemical manufacturing unit, has already been examined and accepted by the Transfer Pricing Officer, no further adjustment on this count is legally permissible.

7.31 The ld Counsel relied on various decisions, including following:

(i) CIT v. Godawari Power & Ispat Limited (2014) 42 taxmann.com 551 (Chhattisgarh)

(ii) PCIT v. Gujarat Alkalies & Chemicals Limited (2017) 395 ITR 247 Gujarat High Court

(iii) PCIT v. Gujarat Fluorochemicals Limited being orders dated 17.06.2019 Gujarat High Court

(iv) PCIT v. DCM Shriram Limited (2025) 170 taxmann.com 631 Delhi High Court

7.32 The learned Departmental Representative, opposing the contentions advanced on behalf of the assessee, submitted that the reliance placed on earlier judicial precedents approving adoption of the tariff charged by the State Electricity Board to its consumers as the market value of power is no longer justified in view of subsequent statutory amendments. It was urged that clause (ii) of the Explanation below section 80-IA(8), inserted by the Finance Act, 2012 with effect from 1 April 2013, and sub-section (6) of section

80A, inserted by the Finance (No. 2) Act, 2009 with retrospective effect from 1 April 2009, have materially altered the legal position.

7.33 Referring to clause (i) of the Explanation below section 80A(6), the learned Departmental Representative submitted that, since the transaction in question relates to transfer of power from the captive power plant to the assessee's manufacturing unit, the market value must be determined as the price which such goods would fetch if sold by the eligible undertaking in the open market, subject to statutory or regulatory restrictions, if any. On this basis, it was contended that the tariff determined by the Electricity Regulatory Commission, in terms of sections 61 and 45 of the Electricity Act, 2003, constitutes the appropriate benchmark for determining market value.

7.34 It was further submitted that, on a functional analysis, the assessee is engaged only in generation of electricity and does not perform the functions of transmission and distribution. Therefore, the rate at which a power distribution company supplies electricity to consumers, which includes costs of transmission and distribution infrastructure, cannot be applied to the present case. Reliance was placed on the decision of the Jaipur Bench of the Tribunal in Shree Cement Ltd. v. ACIT in ITA No. 162/JP/2016 and Others wherein, after considering the amendments introduced by section 80A(6), the matter was remanded to the Assessing Officer for fresh determination of market value.

7.35 The learned Departmental Representative also relied upon the decision of the Hyderabad Bench of the Tribunal in Sanghi Industries Ltd. v. DCIT in ITA (TP) No. 104/Hyd/2022 (order dated 23.01.2025), to submit that the price charged by electricity boards to consumers includes transmission and distribution costs, whereas no such costs are incurred in the internal transfer of power from a captive power plant to the assessee's own units. It was urged that, in the absence of such costs, the fair market value of electricity supplied internally cannot be equated with the price paid by the assessee to the electricity board.

7.36 It was further contended that, after the insertion of the Explanation to section 80-IA(8), determination of market value must ordinarily proceed on the basis of the arm's length price of the domestic transaction. However, it was argued that clause (iii) of the Explanation below section 80A(6) and clause (ii) of the Explanation below section 80-IA(8), which deem the arm's length price to be the market value in the case of specified domestic transactions, would apply only where a reference has in fact been made to the Transfer Pricing Officer for determination of such arm's length price. According to the learned Departmental Representative, in cases where no such reference has been made, the only permissible mode of determining market value is under clause (i) of the Explanation below section 80A(6).

7.37 In rejoinder, the learned counsel for the assessee assailed the submissions advanced by the learned Departmental Representative. At the threshold, it was submitted that the arguments now urged by the Revenue do not emanate from either the assessment order or the order passed by the Dispute Resolution Panel. None of the issues presently canvassed by the Revenue were raised during the assessment proceedings or before the DRP. It was contended that such contentions have been raised for the first time before the Tribunal, and that too in an appeal preferred by the assessee. The learned counsel submitted that the Tribunal, being an appellate authority, is required to adjudicate only upon the controversy as it arises from the orders impugned before it. Neither the respondent nor the Tribunal can be permitted to enlarge the scope of the dispute beyond what was adjudicated by the lower authorities.

7.38 On merits, and without prejudice to the above preliminary objection, the learned counsel submitted that even assuming—without admitting—that sub-section (6) of section 80A, as inserted by the Finance (No. 2) Act, 2009, applies to the present case, the adoption of market value based on the tariff determined by the State Electricity Regulatory Commission for purchase of power by distribution companies would still be legally untenable. Clause (i) of the Explanation below section 80A(6) defines “market value” to mean the price which the goods or services would fetch if sold in the open market, subject to statutory or regulatory restrictions, if

any. It was emphasised that the governing test remains the price discoverable in the open market, and regulatory constraints, if relevant, can only be incidental to such determination and not determinative of it.

7.39 The learned counsel further clarified that the hearing had earlier been adjourned at the instance of the assessee only to enable filing of a comprehensive rejoinder in the light of the impending decision of the Hon'ble Third Member in the case of Aditya Birla Nuvo Ltd. (since amalgamated with Grasim Industries Ltd.) v. DCIT which had been heard but was then awaiting pronouncement.

7.40 In response, the learned Departmental Representative reiterated his reliance on the decision of the Hyderabad Bench in *Sanghi Industries Ltd.(supra)* and on the submissions earlier advanced before the Hon'ble Third Member in *Aditya Birla Nuvo Ltd.(supra)*, contending that a captive power plant is comparable to a power generating company selling electricity to a distribution licensee, and that the conclusion reached by the Third Member—namely, that the appropriate comparable is the rate at which power is supplied by the distribution company to the consumer—is erroneous. Reference was made to the amendments introduced by insertion of section 80A(6) with retrospective effect from 01.04.2009 and further amendments made by the Finance Act, 2012, to urge

that the Third Member had overlooked the rules governing determination of arm's length price.

7.41 After pronouncement of the Third Member decision in *Aditya Birla Nuvo Ltd.*, the assessee filed a detailed written rejoinder. It was submitted therein that the controversy relating to valuation of power and steam stands concluded at the threshold by application of the transfer pricing provisions. The transfer of power and steam from the captive power plants to the manufacturing unit constitutes a specified domestic transaction, which was duly benchmarked in accordance with Chapter X of the Act. It was pointed out that the Comparable Uncontrolled Price (CUP) method was adopted in Form No. 3CEB, and that the Assessing Officer had made a reference to the Transfer Pricing Officer under section 92CA(1). Upon detailed examination, the Transfer Pricing Officer accepted the arm's length nature of the transactions relating to sale of power and steam and proposed adjustments only in respect of unrelated international transactions. It was contended that once the arm's length price has been so accepted, the Assessing Officer is statutorily bound by such determination in view of section 92CA(4), and no further adjustment or recomputation is permissible.

7.42 It was further submitted that the arm's length price so determined corresponds to the "market value" as defined in the Explanations to sections 80A(6) and 80-IA(8). Consequently, the first limb of section 80-IA(8) stands satisfied, and recourse to any

alternative mechanism for determining market value does not arise. Reliance was placed on Tribunal precedents holding that where the arm's length price is accepted under transfer pricing provisions, the computation under section 80-IA must necessarily proceed on that basis.

7.43 Without prejudice, it was reiterated that the Revenue's arguments travel beyond the findings recorded by the Assessing Officer, the Transfer Pricing Officer, and the DRP, which is impermissible in appellate proceedings. On merits, it was urged that the settled judicial position, consistently affirmed by the Supreme Court and various High Courts, is that the appropriate comparable for determining market value of captive power is the rate at which electricity is supplied by the State Electricity Board or distribution licensee to consumers, and not the rate at which power is sold by a generating company to a distribution company. The latter transaction, it was contended, is regulated, non-competitive, and does not represent an open market price.

7.44 Addressing the Revenue's reliance on statutory amendments, the assessee submitted that the fundamental principle governing "market value"—namely, the price which goods would fetch in the open market—remains unchanged both before and after the amendments. It was pointed out that several judicial decisions rendered for post-amendment assessment years have consistently applied this principle after considering the amended provisions.

7.45 The assessee placed strong reliance on the decision of the Hon'ble Third Member in *Aditya Birla Nuvo Ltd.*, contending that the very issues now sought to be raised by the Revenue had been considered and rejected therein. It was submitted that a Third Member decision is binding on a Division Bench and carries precedential value akin to that of a Special Bench. The Third Member, it was emphasised, had comprehensively examined the amended statutory provisions, Rule 10B, and the regulatory framework under the Electricity Act, and had conclusively held that captive power plants are not comparable to power generating companies supplying electricity to distribution licensees.

7.46 With respect to steam, the assessee submitted that the Revenue's characterisation of steam as a low-pressure by-product is factually incorrect. The captive power plant was established with the dual objective of generating electricity and steam, both of which are required for the manufacturing operations. It was pointed out that the audited notes do not state that steam is non-marketable on account of low pressure, and that steam at varying pressures was supplied, as evidenced by technical certificates placed on record.

7.47 Lastly, it was submitted that steam is recognised as an independent product under the GST tariff and is commercially supplied by independent entities, as demonstrated by sample invoices produced before the Tribunal. On this basis, the assessee contended that steam is a marketable commodity and that its

valuation cannot be rejected on the premise that it lacks commercial character.

7.48 We have heard rival submission of the parties and perused the relevant material on record.

7.49 The deduction under section 80-IA claimed by the assessee in respect of its captive power plant was disallowed by the Assessing Officer on the ground that the assessee had artificially bifurcated the cost of production into two components, one relating to generation of electricity and the other relating to generation of steam, and, by such bifurcation, had created an artificial profit from generation of electricity. According to the Assessing Officer, if the entire cost of the captive power plant, including the cost attributed by the assessee to steam, were taken together, the eligible undertaking would result in a loss and, consequently, no deduction under section 80-IA would be admissible.

7.50 It is undisputed that the assessee computed the deduction on the basis of separate profit and loss accounts prepared for the eligible units and that, while electricity transferred to other units was valued at fair market value, steam was valued at cost. The bifurcation of costs between electricity and steam was made on the basis of a methodology disclosed in the notes to accounts, which was stated to be founded on internal estimates and assumptions.

7.51 Before us, however, the learned counsel for the assessee did not seriously address the issue of correctness or scientific validity of the cost bifurcation adopted by the assessee. Instead, the emphasis of the submissions was on the determination of the fair market value of electricity transferred by the captive power plant to the assessee's other units. The hearing was even deferred at the request of the assessee to await the decision of the Hon'ble Third Member in *Aditya Birla Nuvo Ltd (supra).*

7.52 Although extensive submissions were advanced on the issue of determination of market value of electricity, such discussion was necessitated only because of the manner in which the parties addressed the issue; however, upon examination of the assessment record, we find that the disallowance does not rest on valuation of electricity but solely on allocation of costs.

7.53 We find, however, that in the present case the Transfer Pricing Officer has not proposed any adjustment in respect of the domestic transaction relating to transfer of electricity from the captive power plant. Correspondingly, the Assessing Officer has also not made any addition or disallowance on the ground of incorrect determination of fair market value of electricity. In such circumstances, the elaborate submissions advanced by both sides on the issue of fair market value of electricity are purely academic and do not arise for adjudication in the present appeal. Judicial time cannot be

expended on issues which have no bearing on the outcome of the dispute before us.

7.54 Thus, the real and only issue that survives for consideration is whether the assessee was justified in bifurcating the cost of the captive power plant between electricity and steam, and in attributing a separate cost to steam so as to compute profits from generation of electricity. It would be relevant to refer to the necessary bare facts in relation to claim of deduction under section 80IA of the act by the assessee.

7.55 The assessee has filed form no. 10CCB in relation to Turbine ECT-11 and LPT-10, which is available on paperbook page 164 to 167. According to the clause 27 of said report, total sale of the undertaking has been reported at ₹ 1, 24, 33, 30, 986/- (including steam). In clause 29 profit and gains derived by the undertaking from eligible business has been reported at ₹ 26, 75, 65, 520/- and in clause 30 equivalent amount of ₹ 26, 75, 65, 520/-has been claimed as deduction under section 80IA of the act. On pages 168 of the paperbook, inspection report by the Chief Electrical Inspector, Gandhinagar is placed on record, wherein he has mentioned inspection of two Turbo Generators namely LPT-10(13MW) and ECT-11 (7.1 MW) and permission was granted under rule 47A of the Indian electricity rules, 1956 to charge the above two Turbo Generators. On paper book page 169 detail of computation of income for the year under consideration has been

reported. On page 170 of the paperbook, the auditor report is available, wherein he has prepared balance-sheet as well as profit and loss account for the relevant units. For issue in dispute in hand, the profit and loss account and relevant schedule is important. The assessee has reported sale of electricity at ₹ 568, 322, 532/-and sale of the steam at ₹ 675, 008, 454/-. In this manner total sale of the undertaking has been reported at Rs.1, 243, 330, 986/-. For ready reference, said profit and loss account is reproduced as under:

"TATA CHEMICALS LIMITED
Power Plant ECT - 11 & LPT - 10
Profit & Loss Account for the year ended 31st March 2015

Particulars	***Schedules***	***Amount (Rs.)***
Income		
Sale of Electricity	*1*	*568,322,532*
Sale of Steam	*2*	*675,008,454*
Total Income (A)		***1,243,330,986***
Expenses		
Manufacturing expenses	*3*	*962,413,193*
Administrative & Other Overheads	*4*	*6,555,506*
Depreciation	*5*	*24,179,494*
Total Expenses (B)		***993,148,193***
Net Profit (A-B)		***250,182,793***

7.56 Further on page 173 and 174 details of various schedules to the profit and loss account is reproduced as under:

TATA CHEMICALS LIMITED
Power Plant ECT - 11 & LPT - 10 for the year ended 31st March 2015

Schedule 1: Sale of Electricity

Particulars	*Amount (Rs.)*
a. Electricity generated and captively consumed [Units]	*97,750,700*
b. Applicable GEB rate (as per detailed working given below)*	*Rs. 5.8140 per unit (approx)*
*c. Sale value of electricity (a*b) (Approx)*	*568,322,532*

** Gujarat Electricity Board*

Detailed working for GEB Rate

Particulars	*Units Kwh*	*GEB Rate*	*Sale Amount (Rs.)*
a. Sale of ECT-11	*35,768,600*	*5.7609*	*206,059,544*
b. Sale of LPT-10	*61,982,100*	*5.8446*	*362,262,987*
Total	***97,750,700***		***568,322,532***
Applicable GEB rate (total sale amount / total units) (approx)			***5.8140***

Schedule 2: Sale of Steam

Particulars	*Units*	*Rate*	*Amount (Rs.)*
a. Steam generated and captively consumed			
120# Steam	*181,775*	*717.9796*	*130,510,742*
50# Steam	*366,158*	*641.8587*	*235,021,707*
20# Steam	*628,459*	*492.4363*	*309,476,005*
Total Sale Value (approx)			***675,008,454***

TATA CHEMICALS LIMITED
Power Plant ECT - 11 & LPT - 10
for the year ended 31st March 2015

Serial no.	***Particulars***	***Unit of measurement***	***Quantity***	***Rate Rs./unit***	***Value***
	Schedule 3: Manufacturing Expenses				
	Cost of Running Turbine for Generation of Low Pressure Steam & Electricity (Power)				
a	***Raw Material consumption***				
	Steam (Refer Note 2 below)	*KL*	*1,160,998*	*829.7371*	*963,323,155*

	Total (a)				***963,323,155***
b	***Fuel & Other Direct material cost***				
	Power	*KWH*	*289,200*	*3.0072*	*869,695*
	Less: Condensed Treated Water	*KL*	*37,946*	*46.8997*	*(1,779,657)*
	Total (b)				***(909,962)***
	Total Manufacturing Cost of Steam & Electricity Generation [a+b] (A)				***962,413,193***
	Schedule 4: Administrative & Other overheads				
c	***Employee Cost & Other Overheads***				
	Employee Cost				*1,290,349*
	Stores & Spares Consumed				*(886,834)*
	Repairs & Maintenances				*1,826,052*
	Administrative Overheads				*4,325,940*
	Total (B)				***6,555,506***
	Total Cost of Producing Electricity & Steam (A+B)				***968,968,699***
a	***Outputs & their cost (Approx) (Refer Note 1 below)***				
b	*Steam 120#*	*MT*	*181,775*	*717.9796*	*130,510,742*
c	*Steam 50#*	*MT*	*366,158*	*641.8587*	*235,021,707*
d	*Steam 20#*	*MT*	*628,459*	*492.4363*	*309,476,005*
	Electricity (Power)	*KWH*	*97,750,700*	*3.0072*	*293,960,245*
	Total Cost				***968,968,699***

Note 1: *Please refer note no. 6 of Notes to accounts for cost allocation between steam & electricity.*

Note 2: Average cost of generating steam 450#

	Summary Steam 450#	*Rate*	*Quantity*	*Amount (Rs.)*

a	*TT 9*	*743.1848*	*1,729,805*	*1,285,564,815*
b	*TT 5 & TT 7*	*852.9213*	*2,114,582*	*1,803,572,117*
c	*IBIL & B&W*	*1,055.5312*	*104,154*	*109,937,796*
d	*PRDS*	*967.6309*	*559,680*	*541,563,652*
	Total	***829.7371***	***4,508,221***	***3,740,638,380***

7.57 In the above schedules, issue of significance is basis of allocation of the cost between steam and electricity. In this regard, the auditor has filed notes to account, for ready reference, said notes to account is reproduced as under:

"Tata Chemicals Limited
Power Plant ECT - 11 & LPT - 10
Financial Year ended 31st March 2015

Notes to Accounts

1. *.....*

2. *.....*

3. *For the year, the sales figure for electricity is derived by multiplying units of electricity produced by the power plant with the fair market transfer price of Rs. 5.8140 per unit (approx). The rate of Rs. 5.8140 per unit of power is derived as an equivalent cost of power per unit if the power would have been purchased from local state electricity board i.e. Gujarat State Electricity Board. This is done as per provision in section 80-IA(8) which provides for adoption of fair market value for goods transferred to other business of the assessee. Kindly refer Schedule-I for the same.*

4. ***The sale of steam generated by the power plant has been recorded at cost of producing the same. The sale of the same could not be recorded at fair market value as there is no ready market for steam i.e. steam is not a marketable product under the facts and circumstances of the company. Similarly cost of steam consumed is also booked at its cost of production.***

5. *The cost items contained in Schedule 3 (c) to the profit and loss statement (under the head "Employee cost and other Overheads") include costs directly attributable to Turbines ECT-11 and LPT-10 and also include allocation to ECT- 11 and LPT-10 of the general costs attributable to all the Turbines located at Mithapur - Gujarat. The turbine-wise allocation of the general costs under various heads is made on the basis of quantity of power generated by each turbine.*

6. ***The total cost of producing electricity and steam amounting Rs. 96,89,68,699/- (excluding depreciation) has been allocated to steam generated and electricity power generated based on the given thermodynamic measure of work potential of steam and of electricity at a given state, cost relationships have been worked out for steam at various pressure and for electricity. These relationships are as under:***

Pressure of steam generated	***Relationship (in Rs.)***
450 psig steam	*1.000 x per Tonne*
120 psig steam	*0.764 x per Tonne*
50 psig steam	*0.683 x per Tonne*
15 / 20 psig steam	*0.524 x per Tonne*
Electricity	*0.0032 x per Tonne*

Please refer Schedule 3 to Profit and Loss statement for cost allocation between Power & Steam.

7. *.....*

8. *The Head Office account shows a debit balance of Rs. 311,67,18,098/- because the surplus arising out of power supply to the other units of the company has been debited to Head office account.*

7.58 Similar form No.10CCB and details of computation of profit and loss account and bifurcations of the cost of electricity and steam in respect of power plat TT-12 , Mithapur are placed on PB 178 191. For the sake of brevity, we are not reproducing details in respect of the second power plant as the basis of distribution of the cost for steam and electricity is same for both the plants which has been taken on the basis of the audit report of the same auditor.

7.59 Before us the learned counsel for the assessee referred to note 6 of the notes to account available on PB-176, which has been reproduced above. When specifically called upon to substantiate the scientific basis for such allocation, including the quantum of steam generated at different pressure levels and the methodology for converting steam pressure into tonnage or cost, the assessee failed to place any documentary evidence on record. No technical report, contemporaneous records, or certification from any statutory or technical authority was produced either before the lower authorities

or before us. Even the notes to accounts do not disclose any verifiable or scientific basis for the figures adopted.

7.60 On the other hand, the Revenue has consistently contended that in a thermal captive power plant, high-pressure steam is generated primarily for the purpose of rotating the turbine to generate electricity. The steam enters at very pressure into turbine, After rotating the turbine, steams which comes out of turbine is merely residual steam of low pressure. Such residual steam is not generated independently, nor does it involve any separate or identifiable cost of production. The assessee has also not demonstrated, with supporting evidence, the precise manner or extent to which such residual steam was used in chemical processing. The ld DR brought our attention to the profit and loss account available on paperbook page 172 and submitted that sale value of the steam has been shown that ₹ 675, 008, 454/-, which is even much higher than the sale of electricity reported by the assessee at ₹ 568, 322, 532/-. According to him, this even defies the basic purpose for which captive power plant was installed. In view of him, entire cost of production was towards electricity generation and after removing the quantum of sale of the steam, the result would be loss as cost of the production of the unit is ₹ 993, 148, 193/-.

7.61 We find considerable force in this submission. In a turbine-based power generation system, steam is an intermediate medium

for conversion of thermal energy into mechanical energy, and thereafter into electrical energy. The generation of steam is integrally and inseparably linked to electricity generation. The use, if any, of residual steam after it has performed its primary function does not warrant attribution of a separate cost unless supported by cogent technical and financial evidence. In the absence of such evidence, the bifurcation of cost adopted by the assessee is clearly artificial and self-serving. We also note that the value attributed by the assessee to steam exceeds the value attributed to electricity, which prima facie defies commercial logic and the very purpose for which a captive power plant is ordinarily installed. Once the artificially attributed value of steam is excluded, the eligible undertaking results in a loss, as rightly concluded by the Assessing Officer.

7.62 From the records we are also not able to understand whether the left over steam at low pressure has been used by the assessee as a source of power or for chemical reaction as a chemical component. In such circumstances the basis of artificially assigning the cost to the generation of the steam cannot be permitted to the assessee.

7.63 The learned DR made another argument to convey that the steam generated from the plant is not power and therefore not entitled for deduction under section 80IA of the Act. He submitted that the power as defined in textbook of physics is the rate at which

work is done or energy is transferred, converted or used over time. It measures how fast the system performs task calculated at work divided by time. The SI unit for measurement of power is watt defined as one joule per second. He further submitted that electrical power is the rate at which electrical energy is transferred , consumed or converted into other forms like heat, or light or mechanical energy) within the circuit per unit time, which is measured in watts. He submitted that fundamental formula for measure of the electric power is voltage multiplied by current. He submitted that while both the chemical processing as well as power generation used both the same medium of the steam but they achieve different goals. He submitted that in chemical processing steam's primary heat transfer medium used for heating, distillation and a sterilization, whereas in power generation steam is a working fluid used to convert thermal energy into mechanical energy (spinning of turbine), which is not in case of steam used in chemical reaction. Accordingly, he submitted that leftover steam used by the assessee for chemical reaction if any is not entitled for direction under section 80 IA of the Act as same is not source of power entitled for deduction under section 80 IA the Act.

7.64 We have considered submissions advanced by the ld DR based on the scientific distinction between electrical power generation and use of steam in chemical processing. Though this aspect was not

specifically urged by the assessee and is not determinative of the present controversy, we find the conceptual distinction to be sound.

7.65 Further, we also note that the meaning of word 'power' used in section in Section 80-IA(4)(iv)(a) cannot be read in isolation. It must be read alongside clause (iv)(b), which speaks of undertakings that start "transmission or distribution by laying a network of new transmission or distribution lines." This language is uniquely and exclusively applicable to the electrical power sector. Electricity is transmitted over long distances through a grid. The inclusion of clause (b) acts as a contextual illuminator, clarifying that Parliament's focus was on the electrical grid and its components. Interpreting "power" to include "steam power" renders the specific language of clause (b) incongruous and out of place, violating the principle of harmonious construction. Every tax incentive provision is enacted with a specific economic objective. The objective of Section 80-IA was to overcome the critical shortage of electrical power in the country by encouraging private investment in power plants. The Memorandum explaining the provisions of the Finance Bill, 1993, which introduced this incentive, consistently refers to boosting "power generation" in the context of the national infrastructure deficit. To extend this benefit to a standard piece of industrial equipment like a steam generation would be to completely divorce the provision from its intended purpose. It would transform a targeted infrastructure incentive into an unintended,

general industrial subsidy for any process involving heat exchange. This could not have been the intent of Parliament. In this reference , it is relevant to reproduce part of budget speech of 1993-94 of Hon'ble Finance Minister on **27th February, 1993, as under:**

> *5 7 . Electricity is a critical input for the future growth of our economy. I therefore propose to introduce a five-year tax holiday in respect of profits and gains of new industrial undertakings set up anywhere in India for either generation or generation and distribution of power. The five-year tax holiday will begin from the year of generation of power.*
> *5 8 . The five-year tax holiday, in both these cases, will be part of section 80- IA of the Income-tax Act. At the end of the five-year period, these units will be entitled to the existing deduction under section 80-IA for the remaining period.*

7.66 Thus, the reference of 'power' in budget speech was in relation with electrical power only.

7.67 Nevertheless, since the issue before us is confined to cost attribution and not eligibility of steam per se, we refrain from expressing any final opinion on that aspect.

7.68 In view of the above facts and analysis, we hold that the Assessing Officer was justified in attributing the entire cost of the captive power plant to generation of electricity and in rejecting the artificial bifurcation adopted by the assessee. Once the correct cost is taken into account, the eligible undertaking results in a loss and no deduction under section 80-IA is admissible. The assessee accordingly dismissed.

Ground No. 4: Disallowance of interest claim under section 36(1)(iii) of the Act.

8. The ground No. 4 relate to disallowance of interest paid of Rs.146,73,00,000/-.

8.1 Briefly stated, the facts relevant to the issue are that the Assessing Officer noticed that the assessee had debited interest expenditure of ₹186.79 crores to its profit and loss account, which, *inter-alia*, included interest of ₹146,72,82,057/- incurred on External Commercial Borrowings (ECB) and Non-Convertible Debentures (NCDs) . These borrowings had been utilised for making investment in the assessee's overseas subsidiary. According to the Assessing Officer, the income, if any, arising from such foreign investments or subsidiaries was neither taxable in India nor were those entities resident in India. On this premise, the assessee was called upon to explain as to why the corresponding interest expenditure should not be treated as capital in nature and disallowed.

8.2 Before the Assessing Officer, the assessee contended that the interest expenditure was incurred wholly and exclusively for the purposes of its business and was, therefore, allowable as a deduction under section 36(1)(iii) of the Act. In the alternative, it was submitted that the investments were capable of yielding dividend income taxable in India and, therefore, even if the

expenditure was not considered allowable as business expenditure, the same would be deductible under section 57 of the Act.

8.3 The assessee explained that the borrowings had been raised in the financial year 2008-09 for the purpose of acquiring General Chemical Industrial Products Inc. (GCIP), USA, a major player in the global soda ash market, for a total consideration of approximately ₹4,036 crores. It was submitted that this acquisition enabled the assessee to consolidate its position as the second-largest soda ash producer in the world and marked a significant milestone in the growth of its soda ash business. The acquisition opened new markets in North and South America and other regions, at a time when global demand for soda ash was steadily increasing. The assessee further highlighted that the acquisition of cost-effective natural soda ash assets provided it with a distinct competitive advantage in the global market.

8.4 It was contended that the overseas subsidiary was engaged in the same line of business as the assessee and that the investment had been made as a measure of commercial expediency and for furtherance of the assessee's own business interests. Emphasis was placed on the provisions of section 36(1)(iii) of the Act to submit that the said section permits deduction of interest on borrowed capital so long as the borrowing is for the purposes of business, without drawing any distinction between capital borrowed for revenue purposes and capital purposes.

8.5 The assessee placed reliance on the decision of the Hon'ble Supreme Court in *DCIT v. Core Health Care Ltd.* (298 ITR 194), wherein it is held that interest on borrowed capital is allowable under section 36(1)(iii) irrespective of whether the borrowing is utilised for acquisition of a capital asset or otherwise, so long as the borrowing is for business purposes. It was further submitted that the expression "for the purposes of the business" is wider in scope than the expression "for the purpose of earning profits" and includes all acts incidental to the carrying on of business. According to the assessee, the earning of dividend income was merely incidental or ancillary to the principal business objective, and therefore the allowability of interest under section 36(1)(iii) could not be denied.

8.6 Without prejudice, the assessee alternatively claimed that interest incurred on borrowed funds utilised for investment in shares, yielding dividend income chargeable to tax, was allowable as a deduction under section 57(iii) of the Act.

8.7 It was also pointed out that a similar issue had arisen in the assessee's own case for the first time in assessment year 2009-10. Although the Assessing Officer had disallowed the claim, the Dispute Resolution Panel, by its directions dated 27.12.2013, accepted the assessee's contention and held that the investment had infused synergy into the overall business of the assessee. Relying on the judgments of the Hon'ble Supreme Court in *Core*

Health Care Ltd. (supra) and of the jurisdictional High Court in *CIT v. Lokhandwala Construction Industries Ltd.* (260 ITR 579), the DRP held that the distinction between utilisation of borrowed funds for capital or revenue purposes was irrelevant for the purposes of section 36(1)(iii).

8.8 The assessee submitted that although the Revenue had preferred appeals against such directions for certain earlier years, which were pending before the Tribunal, the same issue continued to arise in subsequent years as well. From assessment year 2012-13 onwards, in view of the statutory limitation on the Revenue's right to appeal against final assessment orders passed in conformity with the DRP's directions, the issue was decided against the assessee only to keep the matter alive, and such view was followed for later years including assessment years 2013-14 and 2014-15. The assessee's appeals for those years were stated to be pending adjudication before the Tribunal.

8.9 The Assessing Officer, however, did not accept the assessee's explanation. According to him, the investments were reflected in the books of account as capital investments and not as stock-in-trade. He observed that the borrowed funds had been utilised for acquiring and maintaining controlling interest in the overseas subsidiaries, rather than for carrying on the assessee's business. Emphasis was laid on the classification of the shares as investments in the books of account, which, according to the

Assessing Officer, indicated that investment in shares was not the business of the assessee. It was further held that the expenditure was not incurred for the purposes of business and was, therefore, not allowable under section 36(1)(iii) of the Act.

8.10 The Assessing Officer further held that dividend income, if any, arising from the subsidiaries would be assessable under the head "Income from other sources". Placing reliance on the decision of the jurisdictional High Court in *CIT v. R. Amritaben Shah* (238 ITR 777), it was held that interest expenditure incurred for acquiring controlling interest could not be allowed as a deduction under section 57(iii) of the Act, since such expenditure was not incurred wholly and exclusively for the purpose of earning dividend income. Accordingly, the Assessing Officer concluded that the interest expenditure of ₹146,72,85,057/- was capital in nature, disallowed the same, and added it back to the total income of the assessee. Penalty proceedings under section 271(1)(c) of the Act were also initiated. The relevant finding of the Assessing Officer is reproduced as under:

> *" 5.3 The explanation of the assessee has been considered however the same is not acceptable. The assessee has purchased the shares foreign investments/ subsidiary/JVs. Since the assessee is not earning any income from the under the head business and profession from the said investment, the same cannot be treated as a business expense. The interest expenditure has been incurred towards the capital borrowed to make investment in a subsidiary. If investment in shares was the business of the assessee, the assessee would have categorized the above investments in its books as stock-in-*

trade. The fact that the assessee is showing the above shares, acquired, as investment in its books is also one of the indicators that the assessee is not involved in the business of investment. In fact it is seen that the aforesaid investment has been made only for the purpose of maintaining controlling interest in the said subsidiary company and not with a motive of business consideration, including capital appreciation. Using the borrowed funds for making investment with a motive of acquiring and maintaining controlling interest cannot be held to be business of the assessee company. Considering the above it is conclusively held that making investment or acquiring shares is not the business of the assessee. There is no connection of business in the said investment in whatever manner. Considering that the above investment is not for the purpose of the business, the cost of making investment cannot be allowed as business expenditure.

5.4 The only income from the subsidiary is dividend income. Since, dividend income is taxable as income from other sources, the allowability of interest expenditure under Section 57 has to be considered. In the present case, the main motive of the assessee is not to earn dividend income but to acquire the controlling stake in subsidiary. Since the interest expenditure is incurred to obtaining a controlling interest in a foreign company, the allowability of interest expenditure u/s 57 is also not possible. Reliance is placed on the ratio of the judgment in the case of CIT Vs R.Amritaben Shah reported in 238 ITR 777 (Bombay High Court) which held that expenditure incurred for the purpose of controlling interest is not an allowable expenditure u/s.57(iii) of the Act. The court held as under:

"Section 57(iii) provides that in order to get deduction the expenditure should be incurred wholly and exclusively for the purpose 'of making or earning income from other sources' and that it should not be in the nature of capital expenditure. Section 58(1)(a) further provides that no deduction shall be allowed in case the expenditure is in the nature of personal expenses of the assessee. In the instant case, there was no dispute that shares in question were purchased by the assessee for the purpose of acquiring controlling interest in the company and not for earning dividend. That being so, the expenditure incurred by way of interest on loan taken by the assessee for the said purpose could not be held to be an expenditure incurred wholly and exclusively for the purpose of earning income by way of dividends. From the nature of transaction, it was clear that the expenditure was not for the purpose of earning income by way of dividends but for the purpose of acquiring controlling interest in the company and, therefore, it would not be allowable as a deduction under Section

57(iii)"

5.5 In the present case, interest expense is claimed incurred for the purpose of acquiring controlling interest. Hence, in view of the above discussions, interest amounting to ***Rs. 146,72,85,057/- is disallowed as capital expenditure and is accordingly added back to the total income of the assessee.*** *Penalty proceedings u/s 271(1)(c) of the IT Act is initiated for furnishing inaccurate particulars of income.*

8.11 The ld DRP affirmed the view of the ld AO. The only reasons given by ld DRP is that proceeding before them are continuation of assessment proceedings. Since, the Revenue cannot file an appeal against the final assessment order passed pursuant to the directions given by the DRP and with a view to keep the issue alive they have taken a different view for the year under consideration as compared to AYs 2009-10 to 2011-12

8.12 Before us the assessee submitted that the interest expenditure incurred on borrowings utilised for acquiring controlling interest in its overseas subsidiary, GCIP, USA, is squarely allowable under section 36(1)(iii) of the Act.

8.13 At the outset, it is contended that where borrowings are made on grounds of business and commercial expediency for acquisition of controlling or strategic interest in a company engaged in the same or allied line of business, the allowability of interest is to be examined under section 36(1)(iii) and not under section 57(iii). The decisive test is whether the capital is borrowed "for the purposes of business". Once this condition is satisfied, the nature of the asset

acquired—whether capital or revenue—and the form in which it is held, namely as investment or otherwise, are wholly irrelevant.

8.14 It was submitted that in the assessee's own case for Assessment Year 2017-18, this very issue has already been examined and conclusively decided by the Tribunal while setting aside the revisionary order passed under section 263 of the Act. The Tribunal recorded a categorical finding that the borrowings were utilised for acquisition of overseas subsidiaries in the same line of business, that the interest expenditure was incurred wholly for business purposes, and that the Assessing Officer had taken a permissible view. The said decision pertains to the same transaction and the same nature of borrowings, and therefore, on the principle of consistency alone, the present claim deserves to be allowed.

8.15 The assessee further submits that the legal position on this issue is no longer *res-integra*. It stands consistently affirmed by the Hon'ble Supreme Court and various High Courts that, for the purposes of section 36(1)(iii), what is relevant is the purpose of borrowing and not the purpose of investment or the character of the asset acquired. Interest on borrowed capital is allowable so long as the borrowing is for business purposes, even if the funds are utilised for acquiring capital assets or strategic investments, including shares held as investments. The acquisition of controlling interest to expand, protects, or promotes business operation has repeatedly been held to constitute a valid business purpose.

8.16 It is also well settled that section 36(1)(iii) does not draw any distinction between capital borrowed for acquiring a revenue asset and capital borrowed for acquiring a capital asset. The section is a complete code in itself. Unlike section 57(iii), it does not require that the dominant or immediate object of expenditure should be earning of income. Therefore, where borrowings are made for business expansion, acquisition of subsidiaries, or strengthening of business operations, the interest thereon is allowable as a business deduction notwithstanding that dividend income may be incidental or even absent.

8.17 The assessee submits that the reliance sometimes placed by the Revenue on decisions rendered in the context of section 57(iii) is misplaced. Those decisions turn on a materially different statutory test, namely that the expenditure must be incurred wholly and exclusively for earning income chargeable under the head "Income from other sources". Such a restrictive test has no application while considering deduction under section 36(1)(iii), which uses the broader expression "for the purposes of business".

8.18 As regards the proviso to section 36(1)(iii), it is submitted that the same is inapplicable to the facts of the present case. The proviso is attracted only where interest is paid on capital borrowed for acquisition of a tangible asset for extension of business, for the period up to the date such asset is first put to use. Acquisition of controlling interest in a subsidiary by purchase of shares does not

fall within the mischief of the proviso. In any event, even assuming the proviso applies, the shares had already been acquired in earlier years and stood "put to use" immediately upon acquisition, as the business benefits and strategic control flowed from that very date. Hence, no disallowance can be made in the year under consideration.

8.19 In view of the aforesaid facts and the settled legal position, the assessee submits that the interest paid on borrowings utilised for acquiring controlling interest in GCIP, USA, having been incurred wholly and exclusively for business and commercial expediency, is fully allowable under section 36(1)(iii) of the Act. The disallowance made by the Assessing Officer, therefore, deserves to be deleted and the ground of appeal allowed.

8.20 The ld counsel in support of his contentions relied on various decision including decisions in the case of CIT v. Srishti Securities Pvt. Ltd. (2010) 321 ITR 498 (Bom) and CIT v. Modi Private Limited (1995) 79 Taxmann 428 (Bom)

8.21 Per contra the ld CIT (DR) contended that the funds have been borrowed admittedly for purchasing shares of foreign subsidiaries. The shares of the foreign subsidiaries company yield dividend income and are capable of only earning dividend income. Dividend from a foreign subsidiary is taxable u/s.56 under the head 'Income from Other Sources'. The ld DR submitted that the taxability of any

receipt which falls under a particular head of income can only be determined by giving allowable deductions under that head of income only and not under any other head.

8.22 The Ld. DR submitted that assessee is not in the business of investments and it has been made as capital investment into the shareholding of subsidiaries which are independent entities separate from the assessee. They have their own business and paying taxes into the relevant countries. He submitted that if assessee is claiming the deduction u/s 36(1)(iii) then one has to see whether the assessee is declaring any income from such investments under the relevant head of the profit and gains of business or profession, since the deduction u/s 36(1)(iii) is falling under the provisions related to profit and gains of business or profession. He submitted that interest expenditure has to be considered for allowance subject to as under which 'head' the income generated therefrom is being offered by the assessee in the return of income. He submitted that if income from such investment is offered by the assessee under the head business and profession then assessee is eligible for deduction u/s 36(1)(iii) otherwise if income is offered under the head 'capital gain' or 'income from other sources' then said interest expenses will also go under respective head subject to provisions of law. He submitted that investment made by the assessee in so called 'capital asset' is not contributing to the business income of the assessee. He

submitted that if overall provisions of the Income-tax Act are properly appreciated then basic principle is that expenditure could be allowed under respective head under which the income from said source is offered. Certainly, the assessee has not declared any income from those investment under the head 'profit and gains business or profession' and therefore, assessee was not entitled u/s 36(1)(iii) of the Act.

8.23 Regarding the alternate request for allowing the said interest u/s 57(1) of the Act, the Ld. DR submitted that in view of decision of the Hon'ble Bombay High Court in the case of Amritaben Shah (supra) when investment is made for obtaining, controlling interest and then in such circumstances deduction u/s 57(iii) is not allowable against the dividend income.

8.24He further submitted that when investment in shares of foreign subsidiaries can yield or is capable of yielding- 'Income from other sources' only; deduction of such interest expenditure can only be examined under the head 'Income from Other Sources'. Therefore, allowability of interest expenditure of Rs.146.73 crores has to be examined only under the provisions of Section 57(iii) of the Act. As per Section 57(iii) of the Act only such interest expenditure can be allowed as a deduction which has been laid out or expended wholly and exclusively for the purpose of making or earning dividend income. In this case, the purpose of incurring interest expenditure was not wholly and exclusively for earning

dividend income because as per the assessee's own admission such an investment was made to acquire and manage the controlling stake in foreign subsidiary. The ld DR relied on the decision of the Hon'ble Bombay High Court in the case of Amritaben Shah (supra) where in it is held as under:

> *"Section 57(iii) provides that in order to get deduction the expenditure should be incurred wholly and exclusively for the purpose 'of making or earning income from other sources' and that it should not be in the nature of capital expenditure. Section 58(1)(a) further provides that no deduction shall be allowed in case the expenditure is in the nature of personal expenses of the assessee. In the instant case, there was no dispute that shares in question were purchased by the assesssee for the purpose of acquiring controlling interest in the company and not for earning dividend. That being so, the expenditure incurred by way of interest on loan taken by the assessee for the said purpose could not be held to be an expenditure incurred wholly and exclusively for the purpose of earning income by way of dividends. From the nature of transaction, it was clear that the expenditure was not for the purpose of earning income by way of dividends but for the purpose of acquiring controlling interest in the company and, therefore, it would not be allowable as a deduction under Section 57(iii)."*

8.25 The ld DR further submitted that even otherwise, as per the provisions of **Section 115BBD**, no deduction can be granted in computing income by way of dividend from a foreign subsidiary, where the assessee holds more than 26% of the equity share capital. In the case of this assessee, it hold more than 26% of the equity share capital of the foreign subsidiary. For invoking the provisions of Section 115BBD, it is not necessary that the shares of the foreign subsidiary have actually yielded dividend income or not; what is material is that the shares of the foreign subsidiary are capable of yielding dividend income only and therefore, the provisions of Section 115BBD(2) are clearly applicable. Provisions of Section 115BBD(2) clearly states that no deduction of any expenditure under any provision of the Act is allowable against dividend income from foreign subsidiary. Therefore, no deduction of interest is allowable to the assessee in view of Sec 115BBD of the Act.

8.26 The DR accordingly submitted that in view of the above submissions, interest expenditure of Rs.146.73 cores cannot be allowed as a deduction either u/s.57(iii) or u/s 115BBD(2) or u/s 36(1)(iii) of the Income-tax Act.

8.27 We have carefully considered the rival submissions advanced by the parties and have perused the material available on record. It is an admitted position that the assessee had borrowed funds for the purpose of making investments in its subsidiary

companies with a view to acquiring and retaining controlling interest therein. The principal contention of the assessee is that such investments were made for the purposes of its business and, therefore, the interest paid on the borrowed funds utilised for such investments is allowable as a deduction under section 36(1)(iii) of the Act.

8.28 The Ld. counsel for the assessee submitted that in assessee's own case for assessment year 2017-18, the Co-ordinate Bench of the Tribunal, while setting aside the order passed u/s 263 by the ld PCIT held that the interest paid on fund borrowed for the purpose of acquiring companies is allowable expenditure u/s 36(1)(iii) of the Act. But, it is noted that the Coordinate Bench setaside the order u/s 263 for the reason that PCIT had not controverted the factual and legal submission filed by the assessee.

8.29 Though the assessee in its written submission has filed a long list of cases in support of its contention, but we have considered the cases which were cited during the course of hearing .There can be no quarrel with the legal proposition, as laid down in the decisions relied upon by the assessee, that interest on capital borrowed for the purposes of business is allowable under section 36(1)(iii), irrespective of whether the borrowing is for acquisition of a capital asset or a revenue asset. However, the crucial issue which requires examination is whether the capital so invested forms part of an asset which is directly and integrally employed in the business

operations of the assessee so as to generate business income assessable under the head "Profits and gains of business or profession".

8.30 By way of illustration, where an assessee acquires plant and machinery out of borrowed funds, such acquisition, though capital in nature, results in the creation of a tangible business asset which is put to use in the course of the assessee's business and directly contributes to the generation of business income. In such a situation, the interest paid on the borrowed capital is allowable as a revenue deduction, once the asset is put to use, since the borrowing is undeniably for the purposes of the business. Similarly, where borrowed funds are utilised for acquisition of a building, which is also a capital asset, the allowability of interest depends upon the head under which the income arising therefrom is assessed. If the rental income from such building is assessed under the head "Profits and gains of business or profession", the interest paid on the borrowed funds may be allowable under section 36(1)(iii) of the Act. However, where the rental income is assessed under the head "Income from house property", the deduction of interest is governed by the specific provisions applicable to that head, and the interest cannot be allowed under section 36(1)(iii) of the Act.

8.31 In the present case, however, the borrowed funds have been deployed by the assessee towards investment in the share capital of its subsidiary companies. The income arising from such

investments accrues to the assessee either by way of dividend or upon transfer of the shares. It is of considerable significance that the assessee itself has accepted that such income is not offered to tax under the head "Profits and gains of business or profession". The disallowance under section 36(1)(iii) of the Act, on the other hand, operates strictly within the framework of computation of income under the head "Profits and gains of business or profession". The scheme of the Act envisages a compartmentalised method of computation of income under distinct heads. Sections 15 to 17 govern computation of income from salaries; sections 22 to 27 deal with income from house property; sections 28 to 44DB provide for computation of income under the head "Profits and gains of business or profession"; sections 45 to 55A relate to computation of capital gains; and sections 56 to 59 prescribe the manner of computation of income from other sources. Each head constitutes a separate and self-contained code, permitting only such deductions as are expressly provided for within the respective computational provisions. The deduction under section 36(1)(iii) is embedded in the statutory scheme governing computation of business income and, therefore, can be allowed only against income assessable under the head "Profits and gains of business or profession". It cannot be extended to income which is assessable under other heads. The statute itself clarifies that interest on capital borrowed for acquisition of a capital asset is to be capitalised up to the point when the asset is first put to use, and only thereafter does it

assume the character of revenue expenditure allowable in accordance with the provisions applicable to business income.

8.32 In our considered view, permitting deduction of interest expenditure against business income, when the corresponding investment yields income assessable under entirely different heads, would be contrary to the fundamental scheme and principles governing computation of income under the Act.

8.33 The borrowed capital in the present case has not resulted in the acquisition of any business asset employed in the assessee's business operations, but has merely facilitated acquisition of controlling interest in subsidiary companies. Consequently, the nexus required for allowance of deduction under section 36(1)(iii) is absent.

8.34 Accordingly, we hold that the interest expenditure claimed by the assessee under section 36(1)(iii) of the Act is not allowable on the facts of the present case. The judicial precedents relied upon by the assessee are distinguishable and do not advance its case.

8.35 Coming to the alternative plea of the assessee for allowance of the interest expenditure against dividend income under section 57(iii) of the Act, we find that the issue stands squarely covered by the judgment of the Hon'ble Bombay High Court in *CIT v. R. Amritaben Shah (supra)*, wherein it has been categorically held that interest incurred on borrowed funds utilised for acquiring

controlling interest in a company is not allowable as a deduction under section 57(iii), as such expenditure is not incurred wholly and exclusively for the purpose of earning dividend income. Respectfully following the said binding precedent, we decline to accept the alternative claim of the assessee.

8.36 The, Ground No. 4 of the assessee's appeal is dismissed.

8.37 The ground No. 5 of the appeal was not pressed therefore, same is dismissed as infructuous.

Ground No. 6 – Disallowance of Provision for Post-Retirement Medical Benefits

9. Ground No. 6 of the appeal relates to the disallowance of ₹6,37,00,000/- being provision for post-retirement medical benefits made by the assessee and disallowed by the Assessing Officer.

9.1 The assessee has been extending post-retirement medical benefits to its retired employees and their dependent family members in terms of a long-standing policy. Under the said scheme, retired employees are entitled to free medical check-ups, medicines, and treatment at hospitals affiliated with the assessee. During the year under consideration, the assessee debited an amount of ₹6.37 crores to its Profit and Loss Account towards incremental liability for post-retirement medical benefits, treating the same as a non-

current liability and claiming deduction thereof in the computation of income.

9.2 The assessee submitted that the liability was contractual in nature and was required to be accrued annually in accordance with the mercantile system of accounting. It was explained that the provision was created on the basis of an independent actuarial valuation, which took into account relevant parameters such as number of beneficiaries, benefit utilisation pattern, salary escalation, and appropriate actuarial discounting factors. The amount debited, according to the assessee, represented an ascertained liability accrued during the year.

9.3 The Assessing Officer, however, did not accept the above explanation and disallowed the claim on the ground that employee benefit expenditure is allowable only on payment basis in terms of section 43B of the Income-tax Act, 1961.

9.4 The objections raised by the assessee before the Dispute Resolution Panel were rejected, following the DRP's own orders for earlier assessment years 2012-13 and 2013-14.

9.5 Before us, the learned counsel for the assessee reiterated that the assessee as a matter of policy, has been allowing post retirement medical benefit to its retired employees and their family members and consistently followed the mercantile system of accounting and that a reasonable estimate of post-retirement

medical benefit expenditure was made on actuarial basis. It was contended that section 43B has no application to the present case. The relevant clauses therein as dealing with payments for the benefits of the employees concerns clause (b) which refers to sum payable by the assessee as an employer by way of contribution to any provident fund or superannuation fund or gratuity fund or any other fund for the welfare of the employees. Since, in the present case, no contribution is made to any fund created for the benefit of the employees, the said clause will have no application. Further, clause (f) refers to any sum payable by the assessee as an employer in lieu of any leave at the credit of his employee. This clause is also not applicable to the present case.

9.6 It was further submitted that an identical issue had arisen in the assessee's own case for assessment years 2007-08 and 2008-09. By a consolidated order dated 31.03.2023, the Tribunal had held that provisions for post-retirement medical benefits do not fall within the ambit of section 43B and cannot be disallowed on that ground alone. The Tribunal had, however, remanded the matter to the Assessing Officer for verification of the actuarial valuation report, as the same had not been produced during the assessment proceedings.

9.7 The assessee submitted that pursuant to the said directions, the actuarial valuation report was examined by the Assessing Officer while giving effect to the Tribunal's order, and the deduction

was ultimately allowed by order dated 09.01.2024. It was further stated that a similar position obtained for assessment year 2008-09.

9.8 We have heard arrival submission of the parties on the issue in dispute and perused the relevant material on record. The Assessing Officer has disallowed the provision for post-retirement medical benefits solely on the premise that such expenditure is allowable only on payment basis under section 43B of the Act. This approach, in our considered view, is contrary to the settled legal position. As already held by the Tribunal in the assessee's own case for earlier assessment years, a provision for post-retirement medical benefits does not fall within any of the clauses of section 43B, particularly when no contribution is made to any fund and the liability is otherwise contractual. However, it is equally well settled that for a provision to be allowable under the mercantile system of accounting, the liability must be an **ascertained liability** and not a mere contingent one. The existence of a scientific and reliable actuarial valuation is therefore a critical requirement.

9.9 Before us the learned counsel for the assessee submitted that identical issue in assessment year 2007-08 and 2008-09, was restored to the file of the Assessing Officer for examination and verification of the actuarial valuation report. The relevant finding of the Tribunal is reproduced as under

> *"The ld. AO however, strangely applied the provisions of section 43B of the Act and held that since the said provision made for post retirement medical benefits had not been actually paid by the assessee, the same would become disallowable in terms of Section 43B of the Act. We are unable to comprehend ourselves to understand this contention of the Revenue. On perusal of the provisions of Section 43B of the Act, this expenditure provision made for post retirement medical benefits would not fall under any of the clauses provided in Section 43B of the Act. It is an admitted fact that no fund is created by the assessee in respect of this post retirement medical benefits."* (emphasis supplied).

9.10 In said case actuarial valuation report was not submitted before the ld AO during assessment proceedings and as per the directions of the Tribunal the assessee had submitted the actuarial valuation report. Since the said report was placed before the Tribunal for the first time to justify that the said provision was made on a scientific basis, the matter was remanded back to the AO for *de-novo* adjudication in accordance with law.

9.11 In the present assessment year, it is an admitted position that the actuarial valuation report was not furnished before the Assessing Officer during the course of assessment proceedings. The same has been produced for the first time before us and is placed at pages 601 to 618 of Paper Book-9.

9.12 Since in the year under consideration, the actuarial valuation report was not filed before the Assessing Officer, therefore following

the finding of the Tribunal (supra) in the case of the assessee for assessment year 2007-08 and 2008-09, we restore the matter back to the file of the Assessing Officer. The Assessing Officer shall examine the actuarial valuation report and determine, in accordance with law, whether the provision for post-retirement medical benefits represents an ascertained liability allowable as deduction.

9.13 The assessee shall be afforded a reasonable opportunity of being heard and of producing all relevant material in support of its claim.

9.14 The ground no. 6 of the appeal of the assessee is accordingly allowed for statistical purposes.

Ground No. 7 – Disallowance of In-house Scientific Research and Development Expenditure under Section 35(2AB)

10. Ground No. 7 of the appeal relates to the disallowance of ₹4,24,13,526/- in respect of expenditure claimed by the assessee towards in-house scientific research and development, for which weighted deduction under section 35(2AB) of the Income-tax Act, 1961 was denied.

10.1 Briefly stated facts of the case are that the assessee claimed to have incurred expenditure of ₹48,07,56,635/- on in-house scientific research and development and accordingly claimed weighted

deduction at 200% under section 35(2AB), amounting to ₹96,15,13,270/-. During the course of assessment proceedings, the Assessing Officer called upon the assessee to justify the claim.

10.2 The assessee submitted that it had three in-house research and development units, namely, (i) Innovation Centre at Pune, Maharashtra, (ii) Centre for Agri Solutions and Technology at Aligarh, Uttar Pradesh, and (iii) Mithapur, Gujarat. It was stated that all the units were duly recognised by the Department of Scientific and Industrial Research (DSIR), New Delhi, and approval in Form No. 3CM was granted vide letter dated 30.05.2013, subsequently revised on 10.07.2018, valid up to 31.03.2018. The assessee contended that once the facility was approved by the prescribed authority, it was entitled to weighted deduction under section 35(2AB) on the entire expenditure incurred for in-house scientific research, as certified by its auditors.

10.3 It was submitted that having complied with the requirement and satisfied the prescribed authority, the assessee company obtained the relevant certificates from the prescribed authority, which was sufficient compliance of the provisions in the weighted action should be allowed without further enquiry by the Assessing Officer. It was further contended that the role of the secretary, Department of scientific and industrial research, Government of India (DSIR) is confined to approval of the in-house research facility and that neither the statute nor the rules empower the

prescribed authority to determine or restrict individual items of expenditure, except to the extent expressly excluded by the provision itself.

10.4 The Assessing Officer observed that the statutory auditors, while certifying expenditure eligible for weighted deduction, had excluded certain expenses aggregating to ₹4,24,13,526/-. According to the Assessing Officer, since these expenses were not quantified or certified by the auditors as eligible expenditure under section 35(2AB), weighted deduction could not be allowed in respect thereof. but the assessee submitted that the expenses stated by the auditors was beyond the guidelines but incurred for the purpose of scientific research and development and therefore should be considered for the weighted deduction.

10.5 The Assessing Officer after considering the submission of the assessee and verification of the documents, however denied the weighted deduction u/s 35(2AB) in respect of the amount of rupees 4,24,13,526/-as same was not quantified by the auditor as expenditure incurred for claim under section 35(2AB).

10.6 The Dispute Resolution Panel upheld the action of the Assessing Officer by following its own orders for assessment years 2012-13 and 2013-14. Reliance was placed on the guidelines issued by the DSIR, under which auditors were required to certify that the expenditure claimed does not fall under the excluded heads. The

learned DRP has reproduced a table of the expenses claimed by the assessee in the expenses denied by the Assessing Officer, which for ready reference are reproduced as under:

> *3. In respect of the abovementioned research unit, the Company has incurred certain expenses which are eligible for weighted deduction of 200% under section 35(2AB) of the Act. (For details on expenses incurred in this respect, refer page 112 of the annual report for year 2013-14). A summary of the break-up of revenue and capital expenditure eligible for claiming deduction is as under:-*
> *4.*

Units	*Capital Exp.*	*Revenue. Exp.*	*Total*		*Weighted Deduction (Rs.)*
CAT Aligarh	*1,431,711*	*16,431,963*	*17,863,674*	*200%*	*35,727,348*
IC- Pune	*176,466,216*	*209,370,798*	*385,837,014*	*200%*	*771,674,028*
SoP- Mithapur	*71,785,504*	*5,270,443*	*77,055,947*	*200%*	*154,111,894*
	249,683,431	***231,073,204***	***480,756,635***		***961,513,270***

> *5. The expenditure claimed by the Company, the amount certified by Auditors (as certain expenses were beyond the DSIR guidelines) is given as follows :-*

	(A)		***(B)***	
	TCL'S claim		***Auditor's Report***	
	Capital Exp.	***Revenue Exp.***	***Capital Exp.***	***Revenue Exp.***
CAT Aligarh	*1,431,711*	*16,431,963*	*1,431,711*	*15,132,089*
IC- Pune	*176,466,216*	*209,370,798*	*176,211,907*	*171,171,391*
Sop- Mithapur	*71,785,504*	*5,270,443*	*71,785,504*	*2,610,507*
R&D Exp.	***249,683,431***	***231,073,204***	***249,429,122***	***188,913,987***
Total		***480,756,635***		***438,343,109***
Variation (A-B)				***42,413,526***

10.7 The learned DRP, thereafter relied on the earlier orders for AY 2012-13 and 2013-14. For ready reference, relevant finding of the ld. DRP is reproduced as under:

> *29.1 This issue has come up before DRP in A.Y.2012-13 and 2013-14. DRP directions for A.Y.2013-14 are as under:*
>
> *"42.1 We have gone through the Auditors' Report and it was seen that the in respect of Aligarh Unit, the Auditors have observed as under :-*

"7. On the basis of our verification of such books of account and other relevant records and documents referred to above, subject to our comments in paragraphs 3 and 6 above and according to the information and explanations given to us, we certify that:

a) It is The Company has maintained separate account for the R&D centre. clarified that the Company maintains its books of account in an Electronic Enterprise Resource Planning System in which the company has identified and accumulated income and expenditure under unique cost centre which forms the basis for preparation of the separate account for the R&D Centre.

b) The Account has been satisfactorily maintained. The expenditure certified is also in consonance with DSIR guidelines.

c) The Company has extended full co-operation to us in carrying out the audit of the Account of the R&D Centre.

d) The expenditure of Rs.223.48 lakhs reported for the year ended as at 31st March, 2013 relevant to the assessment year 2013-14 as detailed in Appendix II to Annexure IV of DSIR guidelines al para 4 is correct, except as mentioned below, to the best of our knowledge and belief as per the result of the audit of the separate cost centre account of the R&D centre carried out by us. Also the R&D capital expenditure and revenue expenditure excluding revenue expenditure of Rs.112.90 lakhs is reflected on page 90. Note 27(c) in the audited financial statements / annual report as referred to in note 4 of schedule H.

Attention is invited to the fact that, included therein is expenditure of Rs.41.62 lakhs, as mentioned in the table below, which are not allowable as per the DSIR guidelines. However, management represents that there are court decisions in favour of allowability of such expenses.

Particulars	*Amount (Rs. in lakhs)*
Building maintenance, Municipal taxes and rental charges being paid	*0.78*
Others as being not directly related to R&D expenses	*40.84*
Total	*41.62*

In respect of Pune Unit, Auditors have observed as under :-

d) The expenditure of Rs.1,596.12 lakhs reported for the year ended as at 31^{st} March, 2013 relevant to the assessment year 2013-14 as detailed in Appendix II to Annexure IV of DSIR guidelines at para 4 is correct, except as mentioned below, to the best of our knowledge and belief as per the result of the audit of the separate cost centre account of the R&D centre carried out by us. Also the R&D capital

expenditure and revenue expenditure excluding revenue expenditure of Rs.112.90 lakhs is reflected on page 90. Note 27(c) in the audited financial statements / annual report as referred to in note 5 of schedule M.

However, attention is invited to the fact that, included therein are expenditure of Rs.141.83 lakhs, as mentioned in the table below, which are not allowable as per the DSIR guidelines. However, management represents that there are court decisions in favour of allowability of such expenses.

Particulars	*Amount (Rs. in lakhs)*
Building maintenance, Municipal taxes and rental charges being paid	*35.48*
Others as being not directly related to R&D expenses	*106.35*
Total	*141.83*

42.2 Similar issue also came up before DRP in A.Y. 2012-13 wherein the DRP as observed as under :

22.1 On this issue, the DRP has noted that the auditors in Para 7(d) of its audit report specifically qualified that expenditure worth Rs. 24.34 lakhs for the Aligarh Unit and worth Rs. 113.65 lakhs for Pune Unit is not allowable, as per the DSIR guidelines. The DRP has noted that these expenses have been incurred for building maintenance, municipal taxes, rental charges, market research, sales promotion, quality control etc.. The details furnished before the DRP reveals that these expenses are not directly related to R&D expenses.

22.2 The guidelines issued by the DSIR for issuance of Audit Report by the Auditors has to certify that the expenditure claimed does not include the following: -

i. Expenditure on outsourced R&D activities.

ii. Expenditure purely related to market research, sales promotion, quality control, testing, commercial production, style changes, routine data collection or activities of a like nature.

iii. Lease rent paid for research farms or research labs.

iv. Expenditure on foundation seeds multiplication, demonstration crops and grow out test etc. beyond breeder seed development.

v. Foreign patent filing expenditure.

vi. Foreign consultancy expenditure.

vii. Building maintenance, Municipal taxes and rental charges being paid.

viii. Any interest component on loans for R&D.

ix. Clinical trial activities carried out outside the approved facilities.

x. Contract research expenses duly certified by chartered accountant.

xi. Expenditure on any payments made to members of the board of Directors or any other part time employees working for R&D.

22.3 It is clear from the above guidelines of DSIR that the following items of expenditure are not allowable:-

Expense Head	*IC Pune (In Rs.)*	*CAT Aligarh (In Rs.)*
Foreign Tour Expenses	*2,233,466*	*4,621*
Corporate Overheads Allocation	*1,861,259*	-
Bus Hire Charges - Staff	*1,277,013*	*164,134*
Telephone, Telex & Fax Charges	*1,041,529*	*175,010*
Canteen Expenses	*595,477*	-
Stationery & Printing	*350,378*	*39,009*
Forex	*220,534*	-
Loss on Assets Discarded	*155,737*	-
Courier Charges	*133,753*	*28,860*
Recoveries	*(540,021)*	-
Travelling Expenses	-	*1,097,501*
Security and Person	-	*457,617*
Office Car Expenses	-	*171,544*
House Keeping Expenses	-	*69,000*
General Expenses	-	*40,710*
Seminar Expenses	-	33,000
Others	*104,106*	*81,396*
Building Maintenance, Municipal Taxes, Rental Charges etc.	*39,27,000*	*72,000*
Expenditure purely related to market research, sales promotion, quality control etc.	*5000*	-
Total	***1,13,65,000***	***24,34,000***

22.4 In view of the above discussion, the AO has rightly disallowed the deduction u/s 35(2AB) of the I.T. Act 1961. Accordingly, this ground of objection of the assessee company is rejected."

42.3 Before us no specific details of the expenses were furnished, however, the AO has relied on the Auditors' Report for disallowance

of expenses. (Para 29.1.5.) The approach of AO appears to be reasonable.

42.4 In view of the auditors finding and following the decision of DRP in earlier year, the action of AO does not require any interference, this objection is therefore rejected."

10.8 Before us, the learned counsel for the assessee explained, item-wise, the nature of the expenses excluded by the auditors and sought to justify their eligibility as expenditure incurred wholly and exclusively for in-house scientific research and development. These included, inter alia, capital items used in the R&D canteen, consultancy and retainership fees paid to technical and support personnel, lease rent and repairs of R&D premises, clinical trial expenditure incurred outside approved premises, foreign patent filing expenses, and other general expenses incurred at the R&D units. Relevant explanation filed by the assessee is reproduced as under:

1. The head of expenses involved in the present ground and the brief description thereof, are as stated hereafter:

a. *Capital expenditure at the Pune unit being Rs.2,54,309 represents assets being water dispenser, refrigerator, microwave oven, vacuum cleaner etc. put up in the canteen facility which is a part of the research and development unit. The said canteen is used only by the personnel at the said unit.*

b. *Consultation fees, retainership fees, contract manpower and labour of Rs._2,91,14,660 at the Pune unit, Rs.4,63,435 at the Aligarh unit and Rs.26,59,936 at the Mithapur unit (aggregating to Rs. 3,22,38,031).*

Travelling expenses of Rs. 17,810 relating to non R& D staff will also bear the same character. These includes hiring of technical and support personnel as and when required. Based on the requirement of manpower which includes the technical personnel who actually assist in carrying out the research and development work and administrative and support staff, consultants or personnel are hired by the Appellant. The senior technical people are paid consultation fees or retainership fees, whereas, the assistant/s or the junior staff whether technical or forming part of the administrative, house-keeping and support staff are paid through contract manpower hiring agencies. In respect of such employees who are on the pay-roll of the Appellant's research and development Department, there is no dispute. Merely, because a part of the personnel has been hired on need basis cannot lead to the conclusion that the said expenditure is not with respect to scientific research. Further, expenditure on scientific research cannot be restricted to only the technically qualified team directly working on the research. However, they also need support from the administration, house-keeping and other such staff forming part of the research and development unit.

c. *Lease rent paid for research laboratory at Pune being Rs.7,82,024 and repairs and maintenance on the building at Pune of Rs.11,98,988 and Rs.7,65,295 at Aligarh. A part of the facility forming an integral part of the research and development unit has been taken on lease on which rent has been paid. Repairs and maintenance expenditure represents such expenses incurred with respect to the building where the research and development activity is being carried out. In such circumstances, such rent and repairs and maintenance expenditure should also qualify as a part of any expenditure on scientific research.*

d. *Clinical trial activities carried out outside the approved premises as relatable to Aligarh unit of Rs.53,334 - Any research carried out by a research unit has to be validated by clinical trial being carried out. At times, the facility to carry out the clinical trial is not available in house. In such circumstances, assistance of outside agencies needs to be taken. In the present case, such expenditure had to be incurred for validation of research carried out at the Aligarh unit.*

e. *Foreign patent filing expenditure incurred at Pune Rs.28,51,410. This expenditure represents expenses incurred for registration of the patent with respect to the research carried out by the research unit. This is necessary to protect it from someone else exploiting it without authority.*

f. *Expenditure of general nature at Pune, Rs.42,51,925 (it majorly includes conference charges, recruitment charges, staff training expenses, legal & registration expenses, transport charges, stationery & printing charges, etc.**)** - This expenditure also represents expenses incurred at the research and development Unit and, hence, forms part of any expenditure on scientific research.*

10.9 It was further contended that the requirement for quantification and certification of eligible expenditure by the prescribed authority was introduced only with effect from 01.07.2016 and that denial of weighted deduction for periods prior thereto was not legally sustainable.

10.10 We have heard rival submission of the parties and perused the relevant metal record. The controversy before us arises primarily on account of the difference between the expenditure claimed by the assessee as eligible for weighted deduction under section 35(2AB) and the amount certified by the auditors for such purpose.

10.11 In order to examine the correctness of the claim and the objections raised by the Assessing Officer, it is necessary to advert to the auditor's certificates furnished in respect of the various units, wherein certain categories of expenditure were identified as being at variance with the approved parameters.

10.12 The relevant extract of the auditor's report relating to the Pune unit is placed at pages 223 to 225 of Paper Book–II. From the said report, it emerges that expenditure aggregating to ₹3,84,53,716/- was identified as not qualifying, on account of differences in classification or treatment. The break-up of such expenditure, as reported by the auditor, is as under:

Particulars	**Amount in Rs.**
Capital Expenditure not used for Research and Development	2,54,309
Consultancy expenditure, retainership, contract manpower/labour	1,38,51,445
Foreign patent filing expenditure	28,51,410

Expenditure on Building repairs and maintenance	11,98,988
lease rent paid for research laboratories	7,82,024
Expenditure of general nature	42,51,925
Expenditure on manpower not regarded as R&D manpower	1,52,63,615
Total	**3,84,53,716**

10.13 Similarly, the auditor's certificate in respect of the Aligarh unit, placed at pages 246 to 257 of the Paper Book, records certain limited areas of divergence, which have been specifically noted at page 247 thereof. The expenditure in dispute in respect of this unit aggregates to ₹12,99,874/-, the details of which are as under:

Particulars	**Amount in Rs.**
Building - repairs and maintenance expenditure	4,63,435
Consultancy expenditure, retainership, contract manpower/labour	7,65,295
Clinical trial activities carried outside the approved premises	53,334
Travelling expenses for non R&D staff	17,810
Total	**12,99,874**

10.14 Lastly, the auditor's certificate pertaining to the Mithapur unit, available at pages 258 to 270 of the Paper Book, indicates a difference of opinion confined to a single item. As noted at page 259, the variance relates to expenditure on manpower in respect of which allocation details were not maintained on a regular basis, aggregating to ₹26,59,936/-.

Particulars	**Amount in Rs.**
Expenditure on manpower for which allocation details are not maintained on a regular basis	26,59,936
Total	**26,59,936**

10.15 The above auditor-identified variations form the sole basis of the adjustments proposed by the Assessing Officer and constitute the factual foundation upon which the impugned disallowance rests. The allowability or otherwise of these expenditures, therefore, falls to be examined in the light of the statutory provisions, the nature of the activities carried on by the respective units, and the evidence placed on record, which we proceed to consider hereinafter.

10.16 It is undisputed that the research facilities of the assessee were duly approved by the DSIR during the relevant period. However, approval of the facility, by itself, does not dispense with the requirement that the expenditure claimed must be shown

to have been incurred on in-house scientific research and development.

10.17 It is well settled that approval of an in-house research facility by the prescribed authority constitutes a threshold condition for availing weighted deduction, but the allowability of individual items of expenditure must still be examined by the Assessing Officer on the touchstone of their direct and proximate nexus with scientific research, based on facts and contemporaneous evidence.

10.18 During the relevant assessment year, the statutory framework did not provide for quantification of eligible expenditure by the prescribed authority. In such a situation, the onus squarely lay on the assessee to demonstrate, with reference to contemporaneous records, that each item of expenditure claimed was incurred wholly and exclusively for in-house scientific research. The Assessing Officer, in turn, was required to examine the nature of such expenditure on the basis of material placed before him

10.19 In the present case, the detailed item-wise justification for the disputed expenditure has been furnished by the assessee for the first time before the Tribunal. Verification of such claims would necessarily require examination of underlying bills, vouchers, agreements, and the nexus of each item of expenditure with in-house scientific research activities. Such an exercise is essentially

factual in nature and cannot be undertaken for the first time at the appellate stage.

10.20 In view of the above, and in the interest of justice, we consider it appropriate to restore the matter to the file of the Assessing Officer. The Assessing Officer shall examine, de novo, the eligibility of the disputed expenditure of ₹4,24,13,526/- for weighted deduction under section 35(2AB), after verifying the supporting evidence and affording the assessee a reasonable opportunity of being heard. The Assessing Officer shall decide the issue in accordance with law, uninfluenced by any observations made herein.

10.21 The ground No. eight of the appeal of the assessee accordingly allowed for statistical purposes.

Ground No. 9 – Claim of Foreign Tax Credit

11. Ground No. 9 of the appeal relates to the grant of foreign tax credit in respect of tax withheld in a foreign jurisdiction.

11.1 The assessee earned income of ₹15,25,40,506/- by way of fees for extending corporate guarantees to its associated enterprises located in various countries. In respect of such income, tax was withheld in Kenya by Tata Chemicals Magadi Limited, amounting to an INR equivalent of ₹15,71,220/-.

11.2 In the return of income originally filed, the assessee did not claim credit for the foreign tax so withheld. The claim for foreign tax credit was raised for the first time by way of a letter dated 24.12.2018 during the course of assessment proceedings.

11.3 The Assessing Officer rejected the claim on the ground that it was not made in the return of income, placing reliance on the decision of the Hon'ble Supreme Court in *Goetze (India) Ltd. v. CIT* (284 ITR 323).

11.4 In proceedings before the Dispute Resolution Panel, the DRP directed the Assessing Officer to verify the claim and to allow foreign tax credit in accordance with the applicable Double Taxation Avoidance Agreement, if it was found that the corresponding income had been offered to tax in India. However, in the final assessment order passed thereafter, no such credit was granted.

11.5 The learned counsel for the assessee submitted that the income in question had admittedly been offered to tax in India and, therefore, in terms of the specific directions issued by the DRP, the Assessing Officer was duty-bound to allow the foreign tax credit. It was further pointed out that an identical claim for foreign tax credit had been allowed by the Tribunal in the assessee's own case for assessment year 2006–07, vide order dated 31.03.2023 passed in ITA No. 9057/Mum/2010.

11.6 Based thereon, and the specific directions of the DRP for the current year which has not been implemented by the AO, it is urged that the Tribunal may be pleased to allow foreign tax credit in respect of the aforesaid amount of Rs. 15,71,220.

11.7 We had heard rival submission of the parties and perused the relevant material on record. The restriction enunciated by the Hon'ble Supreme Court in Goetze (India) Ltd.(supra) operates only at the stage of assessment and does not impinge upon the powers of appellate authorities or the obligation of the Assessing Officer to faithfully implement directions issued by the Dispute Resolution Panel. It is evident that the Dispute Resolution Panel had already issued a clear and specific direction to the Assessing Officer to verify the claim of foreign tax credit and to allow the same in accordance with law, subject to verification that the corresponding income was offered to tax in India. The grievance of the assessee arises from the non-implementation of the said direction in the final assessment order. Thus the issue in dispute is of non-implementation of a DRP direction, not denial on merits.

11.8 In our considered view, once a direction has been issued by the DRP and the Assessing Officer has failed to give effect thereto, the appropriate statutory remedy available to the assessee is to seek rectification of the assessment order under the relevant provisions of the Act. The assessee has not availed of such remedy thus far.

11.9 Having regard to the above, and without entering into the merits of the claim at this stage, we consider it appropriate to direct the Assessing Officer to examine and dispose of any rectification application that may be filed by the assessee for grant of foreign tax credit, strictly in accordance with law and in conformity with the directions already issued by the DRP.

11.10 The ground of the appeal of assessee accordingly allowed for statistical purposes.

12. In the result, appeal of the assessee is allowed partly for statistical purposes.

Order pronounced in the open Court on 04/02/2026.

Sd/-	**Sd/-**
(RAHUL CHAUDHARY)	**(OM PRAKASH KANT)**
JUDICIAL MEMBER	**ACCOUNTANT MEMBER**

Mumbai;
Dated: 04/02/2026
Rahul Sharma, Sr. P.S.

Copy of the Order forwarded to :

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

BY ORDER,

//True Copy//

(Assistant Registrar)
ITAT, Mumbai