IN THE HIGH COURT OF JUDICATURE AT BOMBAY
O.O.C.J.

INCOME TAX APPEAL NO. 237 OF 2017
WITH
INCOME TAX APPEAL NO 485 OF 2017

Pr. Commissioner of Income Tax -5 .. Appellant

Versus

Bajaj Finance Limited .. Respondent

.....

- Mr. Tejveer Singh for the Appellant
- Mr. Percy Pardiwalla, Sr. Counel a/w Ms. Vasanti Patel for the Respondent

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CORAM : AKIL KURESHI &
SARANG V. KOTWAL, JJ.

DATE : APRIL 2, 2019.

P.C.:

1. These appeals involve similar issues. We may record facts from Income Tax Appeal No. 237 of 2017.

2. The appeal is filed by the Revenue to challenge the judgment of the Income Tax Appellate Tribunal ("the Tribunal" for short) raising following questions for our consideration:-

> "(i) Whether on the facts and circumstances of the case and in law, the Tribunal was correct in disregarding the judgment of the Hon'ble Supreme Court given in the case of Southern Technologies Ltd Vs. JCIT 320 ITR 577 (SC)

which says that provisions of RBI Act cannot override the provision of Section 145 of the Income Tax Act, 1961, since both the Acts operate in different fields and therefore, assessee cannot recognize interest income on NPA and yet not offer it in Profit and Loss account?

(ii) Whether on the facts and in the circumstances of the case and in law, the Tribunal was correct in deleting the disallowance of Rs. 71,13,261/- made by AO u/S. 14A r/w Rule 8D after treating the disallowance of Rs. 57,600/- offered by assessee as insufficient on the ground that the AO has not recorded the error in the offer of the assessee before invoking Rule 8D, without any such explicit requirement of law?"

3. Question No. (i) arose in following background:-

3.1 Respondent assessee is a Non Banking Finance Company ("NBFC" for short). Respondent filed return of income for the assessment year 2009-10 in which the assessee had claimed deduction of interest on advances which had become non performing assets ("NPA" for short). The Assessing Officer disallowed the claim relying on such disallowance for the earlier assessment years which were on the ground that the assessee which was following the mercantile system of banking had to pay tax on interest on accrual basis.

3.2 The issue eventually reached the Tribunal. The Tribunal, by the impugned judgment, allowed the assessee's claim, upon which, the Revenue has filed this appeal.

4. Learned counsel for the Revenue submitted that the assessee had to offer the interest income to tax on accrual basis. The special provision for taxing interest income on NPAs on the basis of receipt has been made under Section 43D of the Income Tax Act, 1961 ("the Act" for short) which does not apply to NBFC. By necessary implication, therefore, the legislature desired that such benefit would be restricted only to such of the entities as are referred to in Section 43D of the Act.

5. On the other hand, learned counsel for the assessee brought to our notice several judgments of the different High Courts holding that on the principle of real income theory, interest on NPAs cannot be charged on accrual basis.

6. Gujarat High Court in case of **Principal CIT Vs. Mahila Sewa Sahakari Bank Ltd**[1] had held that in case of a co-

1 [2017] 395 ITR 324 (Guj)

operative bank, the interest on NPAs would not be chargeable to tax on mere accrual. The Court referred to and relied upon the decision of the Supreme Court in the case of **Southern Technologies Ltd Vs. Joint CIT[2] .** We may note that the decision concerns the assessment year 2010-11 when a co-operative bank was not included under Section 43D of the Act which was inserted by Finance Act, 2017 w.e.f 1.4.2018.

7. In case of **CIT Vs. Deogiri Nagari Sahakari Bank Ltd & Ors.[3],** this Court had expressed a similar view. We may further clarify that in the said case, the Court was concerned with a similar claim raised by the co-operative bank and the Court did record that the assessee was a co-operative bank and not NBFC. However, this distinction may not have much significance now in view of the fact that this Court in case of **CIT Vs. M/s. KEC Holdings Ltd** (Income Tax Appeal No. 221 of 2012 decided on 11.6.2014) held and observed as under:-

> "8. The assessee had credited only an amount of Rs.38,57,933/- as interest on loans. The Assessing Officer was of the view that the interest accrued on the entire loans should have been shown as income. The details as to how the interest income on accrual basis

2 [2010] 320 ITR 577 (SC)
3 [2015] 379 ITR 24 (Bom)

should have been disclosed are, therefore, referred to by the Tribunal. The Tribunal held that the said income was not realized. It held that the assessee follows the mercantile system of accounting. The Tribunal held that the loan advanced by the assessee which was in NBFC had become non-performing asset. That is how following judgments rendered by the Hon'ble Supreme Court and the Delhi High Court, the Tribunal has eventually held that once there is no dispute that the interest considered as accrued was a non-performing asset as per Reserve Bank of India guidelines, then, the income from this interest did not accrue to the assessee. It is in such circumstances, that this income in question was not and cannot be assessed on accrual basis.

9. We do not find that the Tribunal has either misdirected itself in law or its order can be termed as perverse warranting interference in our appellate jurisdiction. We find that the view taken by the Tribunal accords with the Reserve Bank of India guidelines and which are not in any way in conflict with the Income Tax Act, 1961, the Hon'ble Supreme Court has held in the case of UCO Bank that the interest income would have been brought to the Profit and Loss Account provided it was actually realized, that in case of Nationalized Bank it treated something which is doubtful, and therefore, kept it in a suspense account, was held to be a permissible exercise. In respect of the loans which are advanced, recovery of some of them if considered doubtful, then, even the interest on the loans advanced may not be realized. That is how the amount is not brought to the profit and loss account because they are not likely to be realized by the bank or a NBFC as well. It is permissible therefore to disclose or to show them as income in assessment year in which either the interest amount or part of it is recovered. The Tribunal in this case, namely, of the assessee before us, has precisely followed this course. We do not find that the course permitted and upheld by the Tribunal is in any way in conflict with any legal provisions or the settled principles. Rather as held by us, it is in accordance with the

same. Once the view taken by the Tribunal was possible and in the given facts and circumstances the income has not been realized by the assessee, the addition was rightly deleted. We, therefore, do not find that the appeal raises any substantial question of law. It is accordingly dismissed. No costs."

8. Delhi High Court in case of **CIT Vs. Vasisth Chay Vyapar Ltd**[4] held that interest on NPAs cannot be taxed on accrual basis. It was noted that NBFC would be governed by the directions issued by the Reserve Bank of India and RBI directives provided that under certain circumstances, a loan or advance would be treated as NPA. The Court on the real income theory held that such interest would not be taxable. We notice that the decision of the Delhi High Court in case of Vasisth Chay Vyapar Ltd (supra) was carried in the appeal by the Revenue before the Supreme Court. The Supreme Court in the judgment reported in [2018] 253 Taxman 401 (SC) approved the decision of the High Court and dismissed the appeal. Under these circumstances, this question is not entertained.

9. Question No. (ii) pertains to disallowance made by the Assessing Officer under Section 14A of the Act read with Rule

4 [2011] 330 ITR 440 (Delhi)

8D. The Tribunal, however, deleted the disallowance on the ground that the Assessing Officer had not recorded the necessary satisfaction for not accepting the disallowance offered by the assessee. As is well known, sub-section (2) of Section 14A provides that the Assessing Officer shall determine the amount of expenditure incurred in relation to income which is examined for tax if he is not satisfied with the correctness of the claim of the assessee in respect of such expenditure. The satisfaction of the Assessing Officer about the correctness of the expenditure offered for disallowance by the assessee therefore is a pre-condition. In the present case, we have perused the order of assessment in which the Assessing Officer had called upon the assessee to justify the limited disallowances voluntarily offered. The assessee made detailed representation inter alia pointed out that the assessee had not made any expenditure in the nature of administrative expenses. However, to avoid proceedings, a suo motu disallowance was made. The Assessing Officer did not in any manner reject this explanation of the assessee but merely proceeded to make disallowance by invoking Section 14A and applied Rule 8D

which the Tribunal correctly reversed.

10. No question of law arises. Income Tax Appeals are dismissed.

[SARANG V. KOTWAL, J.] **[AKIL KURESHI, J]**