HIGH COURT OF JUDICATURE FOR RAJASTHAN
BENCH AT JAIPUR

D.B. Income Tax Appeal No. 52/2018

Chambal Fertilisers And Chemicals Ltd. , Having Its Registered Office At Gadepan, Dist. Kota, Rajasthan Through Its Assistant Vice President - Legal And Secretary Shri Rajveer Singh S/o Late Sh. Pabudan Singh, Aged About 49 Years.

----Petitioner

Versus

JCIT, Range-2 , Kota.

----Respondent

Connected With

D.B. Income Tax Appeal No. 68/2018

Pr. Commissioner Of Income Tax , Kota.

----Appellant

Versus

M/s. Chambal Fertilizers And Chemicals Ltd. , Gadepan, Distt. Kota.

----Respondent

For Appellant(s)	:	Mr. Sanjay Jhanwar in Appeal No.52/2018 and for respondent in Appeal No.68/2018
For Respondent(s)	:	Ms. Parinitoo Jain for respondent in Appeal No.52/2018 and for appellant in Appeal No. 68/2018

HON'BLE MR. JUSTICE KALPESH SATYENDRA JHAVERI
HON'BLE MR. JUSTICE ASHOK KUMAR GAUR

Judgment

31/07/2018

1. In both these appeals common question of law and facts are involved hence they are decided by this common judgment.

2. By way of these appeals, the assessee as well as the department have assailed the judgment and order of the tribunal whereby tribunal has disposed of the appeals deciding the issue raised before it.

3. This court while admitting the appeals framed following substantial questions of law:-

In D.B. ITA No.52/2018:-

1. Whether under the facts and circumstances of the case and in law the Ld. ITAT has not committed grave legal error in not appreciating that the investment made in the 100% subsidiary companies was out of commercial expediency warranting no interest disallowance?
2. Whether under the facts and circumstances of the case the Ld. ITAT has not legally erred in upholding disallowance on account of interest expenses holding the investments in subsidiary companies and mutual funds to be out of borrowed funds?
3. Whether under the facts and circumstances of the case the Ld. ITAT has not erred in holding that the education cess is a disallowable expenditure u/s 40(a)(ii) of the Act?
4. Whether under the facts and circumstances of the case the Ld. ITAT was justified in not allowing deduction on account of Capital expenses claimed against the sale of mining rights and not reducing the short-term capital gains as directed by Ld. ITAT in Appellant's own case for A.Y.2004-05?

In D.B. ITA No.68/2018:-

1. Whether the Tribunal was legally justified in allowing the deduction of Rs.86,08,460/- to the assessee against the sale proceeds of mining rights, without affording any opportunity of hearing to the Assessing Officer as per Rule 46?
2. Whether the Tribunal was legally justified in restricting the disallowance of interest paid on borrowed funds to Rs.37,65,316/- as against Rs.78,47,330/- made by the Assessing Officer specifically when there was no commercial expediency to make investment in subsidiary companies of the assessee company?
3. Whether the Tribunal was legally justified in deleting the addition of Rs.11,10,98,825/- out of disallowance of interest of Rs.12,90,03,457/- being the interest in relation to dividend income of Rs.4,89,31,413/- claimed as exempt u/s10(35) and further directing the Assessing Officer for computing the interest for the period of NCD borrowing?
4. Whether the Tribunal was legally justified in deleting the disallowance of Rs.25,00,816/- made on account of prior period expenses specifically when the assessee failed to substantiate its claim that the liability of account

of such expenses had been settled/crystallized during the year under consideration?

In D.B. ITA No.52/2018:-

4. Counsel for the appellant Mr. Jhanwar does not want to press question no.1 & 2 subject to liberty of raising the same in appropriate case, if the occasion arises for subsequent year. Thus, ground no.1 and 2 are decided as not pressed.

4.1 Regarding question no.3, Mr. Jhanwar has taken us to the order of CIT(A) and tribunal and strongly relied upon the circular dt.18.5.1967 which reads as under:-

CTR ENCYCLOPAEDIA ON INDIAN TAX LAWS
CIRCULAR F. NO. 91/58/66-ITJ(19) DT. 18TH MAY, 1967
Interpretation of provision of s.40(a)(ii) of IT Act, 1961-Clarification regarding 18/05/1967

BUSINESS EXPENDITURE
SECTION 40(a)(ii),
Recently a case has come to the notice of the Board where the ITO has disallowed the 'cess' paid by the assessee on the ground that there has been no material change in the provisions of s.10(4) of the old Act and s.40(a)(ii) of the new Act.
2. The view of the ITO is not correct. Clause 40(a)(ii) of the IT Bill, 1961 as introduced in the Parliament stood as under:
"(ii) any sum paid on account of any cess, rate or tax levied on the profits or gains of any business or profession or assessed at a proportion of, or otherwise on the basis of, any such profits or gains".
When the matter came up before the Select Committee, it was decided to omit the word 'cess' from the clause. The effect of the omission of the word 'cess' is that only taxes paid are to be disallowed in the assessments for the year 1962-63 and onwards.
3. The Board desire that the changed position may please be brought to the notice of all the ITOs so that further litigation on this account may be avoided.

4.2 He has relied on the following decisions:-

(i) In Municipal Corporation of City of Thane vs. Vidyut Metallics Ltd. & ors. (2007) 8 SCC 688, it has been held as under:-

> 14. So far as the proposition of law is concerned, it is well-settled and needs no further discussion. In taxation-matters, the strict rule of *res judicata* as envisaged by Section 11 of the Code of Civil Procedure, 1908 has no application. As a general rule, each year's assessment is final only for that year and does not govern later years, because it determines the tax for a particular period. It is, therefore, open to the Revenue/Taxing Authority to consider the position of the assessee every year for the purpose of determining and computing the liability to pay tax or octroi on that basis in subsequent years. A decision taken by the authorities in the previous year would not estop or operate as *res judicata* for subsequent year. [vide Maharana Mills (P) Ltd. v. ITO: [1959]36ITR350(SC) ; Visheshwar Singh v. CIT: [1961]41ITR685(SC) ; Installment Supp (P) Ltd. v. Union of India: [1962]2SCR644 ; New Jehangir Vakil Mills v. CIT : [1963]49ITR137(SC) ; Amalgamated Coalfields Ltd. v. Janapada Sabha 1963 Supp (1) SCR 172; Devilal v. STO : [1965]1SCR686 ; Udayan Chinubhai v. CIT: [1967]63ITR416(SC) ; M.M. Ipoh v. CIT : [1968]67ITR106(SC) ; Kapur Chand v. Tax Recovery Officer **(1969) 1 SCR 691**; CIT, W.B. v. Durga Prasad: [1971]82ITR540(SC) ; Radhasoami Satsang v. CIT: [1992]193ITR321(SC) ; Society of Medical Officers v. Hope **1960 AC 55**; Broken Hill Proprietary Co. Ltd. v. Municipal Council **1925 All ER 675**: **1926 AC 94** : **95 LJPC 33**; Turner on Res Judicata, 2ndEdn., para 219, p. 193].

(ii) In Jaipuria Samla Amalgamated Collieries Ltd. vs. Commissioner of Income Tax (1971) 82 ITR 580 (SC), it has been held as under:-

> 5. Now it is quite clear that the aforesaid cesses would be allowable deductions either under Clause (ix) or Clause (xv) of Sub-section (2) of Section 10 unless they fell within Section 10(4). We have already referred to the provisions of both Acts under which the cesses are levied which show that their assessment is not made at a proportion of the profits of the assessee's business. What has to be determined is whether the assessment of the cesses is made on the basis of any such profits. The words "profits

and gains of any business, profession or vocation" which are employed in Section 10(4) can, in the context, have reference only to profits or gains as determined under Section 10 and cannot cover the net profits or gains arrived at or determined in a manner other than that provided by Section 10. The whole purpose of enacting Sub-section (4) of Section 10 appears to be to exclude from the permissible deductions under Clauses (ix) and (xv) of Sub-section (2) such cess, rate or tax which is levied on the profits or gains of any business, profession or vocation or is assessed at a proportion of or on the basis of such profits or gains. In other words Sub-section (4) was meant to exclude a tax or a cess or rate the assessment of which would follow the determination or assessment of profits or gains of any business, profession "or vocation in accordance with the provisions of Section 10 of the Act.

6. The road cess and public works cess are to be assessed on the annual net profits under Sections 72 to 76 of the Cess Act 1880. The net annual profits have to be calculated on the average of the net profits for the last three years of the mine or the quarry and if the annual net profits of the property cannot be ascertained in the aforesaid manner then it is left to the Collector to determine the value of the property first in such manner as he considers expedient and determine 6 per cent on that value which would be deemed to be the annual net profits. The Cess Act of 1930 Mows the same pattern so far as the ascertainment of annual net profits is concerned. These profits arrived at according to the provisions of the two Cess Acts can by no stretch of reasoning be equated to the profits which are determined under Section 10 of the Act. It is not possible to see, therefore, how Section 10(4) could be applicable at all in the present case. Thus on the language of the provisions both of the Act and the two Cess Acts the applicability of Section 10(4) cannot be attracted. But even according to the decided cases such, cesses cannot fall within Section 10(4). The Privy Council in Commissioner of Income tax, Bengal v. Gurupada Dutta and Ors. 14 I.T.R. 100 had to consider whether the rate imposed under the provisions of the Bengal Village Self Government Act 1919 on a person occupying a building and using the same for the purpose of business was an allowable deduction in computing the profits of the business under Section 10 of the Act. Their Lordships laid down the law in the following words:

It will be noted that, in the absence of the necessary powers and machinery, which are not provided by the Act, the estimate of the annual income from business can only proceed on a rough guess, which is in no way comparable with the ascertainment of profits and gains under the Income-tax Act, and, in the opinion of their Lordships, the inclusion of this element of business income as part of the "circumstances" of the assessee with a view to the imposition of the union rate does not fall within Sub-section (4) of Section 10 of the Income tax Act. It is conceded that the union rate is not "levied on the profits or gains", which clearly implies an ascertainment of such profits and gains, and the words "assessed...on the basis of any such profits or gains" in the later part of the sub-section must also be so limited, No such ascertainment of the profits and gains of the business can be undertaken for the purposes of the union rate. The main argument for the Crown, therefore fails.

In our judgment this decision is quite apposite and fully covers the points under consideration. It has been followed by the Allahabad High Court in Simbholi Sugar Mills Ltd. v. Commissioner of Income tax, U.P. & V.P. MANU/UP/0222/1961 : [1962]45ITR125(All) in which the question related to the deducibility of tax payable under the U.P. District Boards Act 1922 which was imposed on persons assessed according to their circumstances and property. Similarly in Commissioner of Income tax, Delhi and Rajas than v. Banarsi Dass & Sons MANU/PH/0408/1965, the Punjab High Court held that a tax imposed under the U.P. District Boards Act on circumstances and property could be legitimately claimed is an allowance and the above decision of the Privy Council was followed. In the Income tax Act 1961, Section 28 relates to the income which shall be chargeable to income tax under the head "profits and gains of business or profession". Section 30(b)(ii) is equivalent to Clause (ix) of Section 10(2) of the Act. Section 40(a)(ii) corresponds to Section 10(4) of the Act. It is significant that in spite of the decision of the Privy Council in Gurupada Dutta's case(1) the Parliament did not make any change in the language of the provisions corresponding to Section 10(4). It can, therefore, legitimately be said that the view of the Privy Council with regard to the true scope and ambit of Section 10(4) of the Act was accepted. We are unable to concur in the reasoning or the conclusion of the Calcutta High Court in Commissioner of Income tax, West Bengal, v. West Bengal Mining Co. (2) in which it

was held that the two cesses being related to profits would attracts. 10(4) of the Act.

(iii) In Installment Supply (P) Ltd. & ors. vs. The Union of India (UOI) & ors. (1962) 2 SCR 644, it has been held as under:-

> 19. There is another answer to the point of res judicata raised on behalf of the petitioners, relying upon the decision of the Punjab High Court in Installment Supply Ltd., New Delhi v. State of Delhi MANU/PH/0068/1956. It is well settled that in matters of taxation there is no question of res judicata because each year's assessment is final only for that year and does not govern later years, because it determines only the tax for a particular period. (See the decision in the House of Lords in Society of Medical Officers of Health v. Hope (Valuation Officer) **[1960] A.C. 551** approving and following the decision of the Privy Council in Broken Hill Proprietary Company Limited v. Municipal Council of Broken Hill **[1925] A.C. 94**.

(iv) In Godrej & Boyce Manufacturing Company Ltd. vs. Dy. Commissioner of Income Tax & ors. (2017) 247 Taxman 361 (SC), it has been held as under:-

> 33. While answering the said question this Court considered the object of insertion of Section 14A in the Income Tax Act by Finance Act, 2001, details of which have already been noticed. Noticing the objects and reasons behind introduction of Section 14A of the Act this Court held that:
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> Expenses allowed can only be in respect of earning of taxable income.
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> In paragraph 17, this Court went on to observe that:
>
> Therefore, one needs to read the words "expenditure incurred" in Section 14A in the context of the scheme of the Act and, if so read, it is clear that it disallows certain expenditure incurred to earn exempt income from being deducted from other income which is includible in the "total income" for the purpose of chargeability to tax.
>
> The views expressed in Walfort Share and Stock Brokers P. Ltd. (supra), in our considered opinion,

> yet again militate against the plea urged on behalf of the Assessee.
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> 34. For the aforesaid reasons, the first question formulated in the appeal has to be answered against the Appellant-Assessee by holding that Section 14A of the Act would apply to dividend income on which tax is payable Under Section 115-O of the Act.

5. Therefore, he contended that the view taken by the tribunal is required to be reversed on issue no.3

6. Regarding issue no.4, he has taken us to the order of the tribunal and contended that for assessment year 2004-05 while considering the expenses the tribunal has observed as under:-

> Assessee received a sum of Rs.5,26,67,000/- from sale of mining rights and vide letter dated 10.10.2011 and 21.11.2011 [ITAT order was dated 28.7.2001] asked the AO to allow expenses of Rs.1,73,53,860/- against sale of mining rights. However there is no finding given by AO. As the order of ITAT was dated 28.07.2011 [after expiry of time for file revised Written] the Assessing Officer should have considered the issue, which he failed to do therefor the same is being considered by me.
> The Hon'ble ITAT has directed that in case the AO comes to conclusion that the capital expenses amounting to Rs.1,73,53,860/- included in the cost of mining rights i.e. non-tangible assets then such cost may be considered to be deducted against the sale of mining rights in the assessment year 2009-10.
> Therefore the assessee was asked to furnished details of these expenses which were included in the mining rights.
> The assessee submitted that amount of Rs.87,45,400/- were paid to M/s ANS construction for dismantling of existing structure, fencing of boundary, construction of temp. site office and security in plant area.
> Firstly from the above nothing could be concluded [no details were produced], secondly it's connection to mining was not proved.
> From the details already in the order of ITAT it can be concluded that of Rs.8608460/- related to deep excavation and road work were related to mining operation and treated as included in sale of mining rights.

> Whereas misc. Capital expenses of 87,45,400/- [in absence of details] cannot sale proceeds of mining rights.
> Therefore the AO is directed to allowed deduction of Rs.86,08,460/- from sale proceeds of mining rights.

7. He contended that once the details are given and payment is reflected in the books of accounts, the tribunal has committed serious committed an error in disallowing the expenses.

In appeal no. 68/2018

8. Counsel for the appellant has taken us to the paper book submitted by her wherein she has pointed out the following observation of the tribunal which reads as under:-

> 58. Ground No. 3 of the assessee's appeal is against not allowing the expenditure of education cess of Rs. 2,41,59,485/- from income claimed by the appellant and the Ld. CIT(Appeals) erred in confirming the same. The education cess was actually paid on income tax and is not a part of income tax as per the provisions of section 40(a)(ii) of the Act. The facts and the submissions of the assessee before the ld. CIT(A) is as under:-
>
> "That the assessee has debited the Profit and Loss Account for the year ended on 31.03.2008 by an amount of Rs. 9490.53 lac under the head "Income Tax", the break-up of which is as under:-

S.No.	Description	Income Tax	Surcharge	Education Cess	Secondary & Higher Education Cess	Total Education Cess	Grant Total (Tax surcharge & Cess)
(1)	(2)	(3)	(4)	(5)	(6)	7=(5)+(6)	(8)=(3)+(4)+(7)
1	Current tax	8331.61	833.16	183.29	91.65	274.94	9439.71
2	Tonnage tax	44.85	4.49	0.99	0.49	1.48	50.82
3	Total	8376.46	837.65	184.28	92.14	276.42	9490.53

> The assessee is of the considered opinion that the education cess and secondary & higher education cess (collectively called as education cess) are not a "tax" and hence not disallowable u/s 40(a)(ii) of the Act on the basis of following submission:-
> (1) That on a plain reading of the above provision of section 40(a)(ii), it is evident that a sum paid of any rate or tax is expressly disallowed by this sub-clause in two cases : (i) where the rate is

levied on the profit or gains of any business orprofession, and (ii) where the rate or tax is assessed at a proportion of or otherwise on the basis of any such profits or gains. It is evident that nowhere in the said section it has been mentioned that education cess is not allowable. Education cess is neither levied on the profits or gains of any business or profession nor assessed at a proportion of, or otherwise on the basis of, any such profits or gains.

(2) That in CBDT Circular No. 91/58/66 ITJ (19), dated May 18, 1967 it has been clarified that the effect of the omission of the word "cess" from section 40(a)(ii) is that only taxes paid are to be disallowed in the assessment for the years 1962-63 onwards. Thus, as per the said circular, Education cess cannot be disallowed; there cannot be a contradiction as the circulars bind the tax authorities.

(3) That education cess cannot be treated at par with any "rate" or "tax" within the meaning of section 40(a)(ii) especially when the same is only a "cess" as may also be seen from the speech of the hon'ble Finance Minister while placing before the Parliament the budget for the year 2004-05 ([2004] 268 ITR (ST.) 1,6).

"Education.

22. In my scheme of things, no issue enjoys a higher priority than providing basic education to all children. The NCMP mandates Government to levy an education cess. I propose to levy a cess of 2 per cent. The new cess will yield about Rs. 4000- 5000 crore in a full year. The whole of the amount collected as cess will be earmarked for education, which will naturally include providing a nutritious cooked midday meal. If primary education and the nutritious cooked meals scheme can work hand-in-hand, I believe there will be a new dawn for the poor children of India"

61. At the outset, the ld. CIT DR has submitted as under:-

"1. Regarding the assessee's ground that the amount of education cess is deductible, it is humbly stated that the background relating to introduction of the said cess needs to be examined. The said cess was introduced by Finance Bill, 2004-05, the relevant portion of which is as follows:

CHAPTER VI

EDUCATION CESS

"81.1 Without prejudice to the provisions of sub-section (11) of section!, there shall be levied and collected, in accordance with the provisions of this chapter as surcharge for purposes of the

Union, a cess to be called the Education Cess, to fulfill the commitment of the Government to provide and finance universalized quality basic education."

It is clear that the said cess is introduced as a SURCHARGE, which is admittedly not deductible. Copy of relevant portion of the Finance Bill is enclosed as Annexure-A.

2. The provisions of sec 40a(ii) are as under:

"any sum paid on account of any rate or tax levied on the profits or gains of any business profession or assessed at a proportion of, or otherwise on the basis of any such profits or gains."

The definition is wide enough to cover any sum paid on account of any rate or tax on the profits or assessed at a proportion of such profits. Education cess being calculated at a proportion (2% or 1%) to Income Tax, which in turn, is in proportion to profits of business, would certainly qualify as a sum assessed at a proportion to such profits. In short, if education cess is considered deductible, then by the same logic Income-Tax or any surcharge would also become deductible, which would be an absurd proportion.

3. Further, if Education cess were to be deductible, then it would not be possible to compute it, e.g. If profit is Rs. 100, Income Tax is Rs. 30 and Education Cess is Rs. 0.90 and if education cess were to be deductible from profit, such profit (after such deduction) would become Rs. 99.1 (100-0.9) which would again necessitate recomputation of Income-Tax which would now be 30% of Rs. 99.1 i.e. Rs. 29.73 and also recomputation of Education cess which would be Rs. 0.89. The vicious circle of such recomputation would continue, which is why legislature in its wisdom has not allowed deductibility of amounts calculated at a proportion of profits.

4. Mechanism of recovery of unpaid Education cess:

In case of unpaid education cess, Assessing Officer will raise demand of Income Tax and convey the same to 'assessee' vide notice of demand u/s 156. In case, the said demand is not paid during the notice period of 30 days of service of notice u/s 156, interest on such demand is chargeable u/s 220(2). In addition, the assessee is also liable for imposition of penalty u/ s 221. The wordings of sec 221(1) are as follows:

"When an assessee is in default or is deemed to be in default in making a payment of tax, he shall, in addition to the amount of the arrears and the amount of interest payable under

subsection (2) of section 220,be liable, by way of penalty, to pay such amount as the Assessing Officer may direct and in the case of a continuing default, such further amount or amounts as the Assessing Officer may, from time to time, direct, or, however, that the total amount of penalty does not exceed the amount of tax in arrears."

The above said provision makes it clear that penalty is leviable in case of default in payment of "tax". Such tax includes any demand relating to unpaid cess also, indicating that unpaid cess is treated as unpaid tax and is visited with all consequences of non-payment of demand. There is no separate machinery in the Act for recovery of unpaid cess and imposition of interest and penalty in case of default in payment of unpaid cess. This indicates that cess is a part of tax and all recovery mechanisms & consequences pertaining to recovery of tax apply to recovery of cess also without explicit mention of the word "cess" in the foregoing provisions. Hence, drawing a parallel, no explicit mention of "cess" is required in sec. 40a(ii) for making disallowance thereof.

5. In view of the above submissions, it is humbly requested not to allow the appellant's plea for deduction of the amount of Education cess."

9. She has also invited our attention to the following finding of AO which reads as under:-

6. <u>Investments in subsidiary companies:-</u>

The assessee has made investment of Rs.523.94 lakh and Rs.120.00 lakh in unquoted shares of its subsidiary companies M/s CFCL Overseas Ltd. and M/s Chambal Infrastructure Ventures Ltd. during the year. The assessee has furnished the following details in this regard vide para 3 of reply No.6 dated 10.10.2011:-

"As desired by your goodself, we wish to submit before your goodself that the assessee had further increased its investment in unquoted shares of CFCL Overseas Limited (a Foreign Company) and in the equity shares of Chambal Infrastructure Ventures Limited (an Indian Company); during the year under consideration as under:-

S.No.	Name of wholly owned subsidiary company	Amount (Rs. In lac)
1	CFCL Overseas Limited, Cayman Islands	523.94
2	Chambal Infrastructure Ventures	120.00

	Limited	

The CFCL Overseas Limited was incorporated as a Special Purpose Vehicle for consolidation of entire software business of assessee. It is a sholly owned subsidiary of the assessee. It would be pertinent to note here that the dividend from this company would not be exempt u/s 10(34).

The Chambal Infrastructure Ventures Limited as a Special Purpose Vehicle and wholly owned subsidiary of the assessee i.e. a 100% subsidiary. This subsidiary is engaged in development and setting up of power projects.

As desired by your goodself, please find enclosed herewith copy of relevant bank accounts reflecting above investment (Page no.3 to 12). Further, this is to submit that the investment have been made out of the internal of the Company."

Reliance is also placed on the judgment of the Hon'ble Supreme Court in the case of S.A. Builders Vs. CIT 288 ITR 1 (S.C.) observing that assessee is required to prove commercial expediency to make interest free advances investments in order to justify its claim for interest on borrowed funds. There is clear cut, direct and proximate nexus between interest bearing borrowed funds and nil income earning investments made by assessee. Further, the assessee has failed to prove that there was any commercial expediency to make investments in above said subsidiary companies. The assessee is paying interest @ 13.25%/12.75% per annum on the above said cash credit accounts. The interest payable on investments in above said subsidiaries is determined at Rs.78,47,330/- as per calculations below:-

(i) Interest @ 13.25% per annum on Rs. 5,23,94,115/- from 3.4.2008 to 31.3.2009	Rs.69,04,180/-
(ii) Interest @ 12.75% per annum on Rs.1.20 crore from 19.8.2008 to 31.3.2009	Rs.9,43,150/-
Total	Rs.78,47,330/-

Therefore, disallowance of Rs.78,47,330/- will be made out of interest paid by assessee on borrowed funds.

10. Thereafter, she has taken us to the finding of the CIT (A) which reads as under:-

4.8 Ground # 8

> "That the l'd Joint Commissioner erred in disallowing interest of Rs.78,47,330/- in respect of proportionate interest paid by assessee on borrowed funds on account of investment made in subsidiary companies without proving any nexus between investments and interest bearing loans. Hence the addition made on this account deserves to be deleted."

4.82 <u>Discussion and the Appellate Decisions</u>

I have gone through the details and it was see that the payment to it's wholly owned subsidiaries were made from cash credit account and same was therefore out of interest bearing funds. However it was seen that when payment of Rs.5.24 crores was made the assessee had credit balance in the account ad only Rs.2.13 crores were over draft. Thus out of Rs.5.24 crore only an amount of Rs.2.13 crore was related to interest bearing founds. The other payment of Rs.1.20 crore was directly related to over draft (interest bearing funds).

As the assessee diverted interest bearing fund to it's subsidiaries the disallowance was justified.

The quantum is computed below:

On Rs.2.13 crore	Rs.2822515/-
On Rs.1.20 crore	<u>Rs.942801/-</u>
	Rs.37,65,316/-

Therefore disallowance of Rs.37,65,316/- is confirmed the Assessing Officer is directed to delete the balance disallowance.

10.1 She contended that the view taken by the tribunal is contrary to law and relied on the judgment **in Godrej & Boyce Manufacturing Company Ltd. vs. Dy. Commissioner of Income Tax & ors. (2017) 247 Taxman 361 (SC)** wherein it has been held as under:-

> 24. The object behind the introduction of Section 14A of the Act by the Finance Act of 2001 is clear and unambiguous. The legislature intended to check the claim of allowance of expenditure incurred towards earning exempted income in a situation where an Assessee has both exempted and non-exempted income or includible or non-includible income. While there can be no scintilla of doubt that if the income in question is taxable and, therefore, includible in the total income, the deduction of expenses incurred in relation to such an income must be allowed, such deduction would not be permissible merely on the ground

that the tax on the dividend received by the Assessee has been paid by the dividend paying company and not by the recipient Assessee, when Under Section 10(33) of the Act such income by way of dividend is not a part of the total income of the recipient Assessee. A plain reading of Section 14A would go to show that the income must not be includible in the total income of the Assessee. Once the said condition is satisfied, the expenditure incurred in earning the said income cannot be allowed to be deducted. The Section does not contemplate a situation where even though the income is taxable in the hands of the dividend paying company the same to be treated as not includible in the total income of the recipient Assessee, yet, the expenditure incurred to earn that income must be allowed on the basis that no tax on such income has been paid by the Assessee. Such a meaning, if ascribed to Section 14A, would be plainly beyond what the language of Section 14A can be understood to reasonably convey."

10.2 For 25,00,816/-, she has relied upon the finding of CIT(A) which reads as under:-

4.12 **Assessee's submissions**

The assessee vide letter dated 21.08.2012, 17.09.2012 & 15.10.2012 submitted as under:-

"The details of major prior period expenses are as under:-

1. Rs. 9,43,693.00:- By oversight, the Income of Co-marketer arrangement was wrongly booked in excess vide document no. 100247242 dt. 31.03.2008 in the financial year 2007-08 and the error was noticed by us in next financial year, hence the same was corrected by us through document no.100105008 dt. 30.09.2008. This being a routine error is not actually an "expense" but a reversal of excess income booked in a previous year.

2. Rs. 11,50,279.00:- Due to some quality issue the appellant did not lift the material from the warehouse of NAITONAL AGRICULTURAL COOPERATIVE MARKETING FEDERATION OF INDIA LTD (NAFED) and sent a request to NAFED to waive the panal Godown rent for such period. But NAFED did not accept the request and the same was known to the appellant after closure of the financial year, hence the appellant booked the expenses in 2008-09 through document no.100107966 dt. 15.10.2008.

3. Rs.267,780.00:- During the financial year 2007-08 the appellant arranged a tour for its

business associates through M/s Lionel Holidays. Initially and gave an advance of Rs.8,71,600/- to M/s Lionel Holidays and the balance amount was to be settled after receipt of the final bill. However, the final bill was misplaced at the appellant's office and was finally traced in December 2008 and the same was processed by us through document no.100135535 dt. 31.12.2008.

As the above are routine revenue expenses being an exceptionally small portion of the total expenses of the appellant company, and some expenses crystallized only during the year hence the addition made on this account deserves to be deleted.

It is humbly submitted that an amount of Rs.4,89,31,413/- being dividend income was earned on mutual funds, which has been claimed as exempt income u/s 10(35) of the Act. The investments in the Mutual Funds were made out of the surplus short term funds available within the business during that period. There were no specific/direct borrowings for the investment. The copy of the bank statements reflecting entries relating to investment in the Mutual Funds were duly submitted during the course of assessment proceedings. A copy of the same is also annexed herewith at Annexure 5. As surplus fund were invested in the Mutual Funds, the appellant did not incur any interest expenditure relating thereto. The investment in Mutual Funds was based on the availability of surplus fund. The assessee would never borrow at prohibitive interest rates and invest to earn a meager 9% odd.

It is further submitted that the major investment in the Mutual Funds were made during December 2008 to March 2009 from the HDFC Bank Account and the bank has charged cash credit interest of only Rs.3,87,800/- during the period from December 2008 to March 2009. However, the L'd Assessing Officer calculated notional interest based on the period of holding of the security without considering the actual interest paid during the relevant peirod. When the total interest of only Rs.3,87,800 was paid in respect of HDFC, it is inconceivable that an interest of about Rs.12.77 crores has been calculated by the L'd Assessing Officer without any basis.

Further there is a mistake in the calculations of the L'd Assessing Officer are taken into consideration and there is a calculation mistake of Rs.9,598,087 as is evident from the statements given at Annexure 6 and 7.

> Considering the above, it is humbly submitted that the addition made on this account deserves to be deleted.

10.3 She has also relied on the observations of the tribunal which reads as under:-

> 18. We have heard the rival contentions and perused the material available on record. Firstly, regarding amount of Rs.9,43,693, it relates to income under the co-marketer arrangement which was booked in excess in the previous financial year and now been reversed during the current financial year. It is thus not an expense but a reversal of income excess booked earlier and now been rectified during the year under consideration. There is thus no question of disallowance of the same.

11. In support of her contentions, counsel for the appellant has relied on the following decisions:-

> **1. Travancore Titanium Products Ltd. vs. Commissioner of Income Tax, Kerala [1966]3SCR 321**
>
> 9. The position may therefore be summarised thus :
> the nature of the expenditure or outgoing must be adjudged in the light of accepted commercial practice and trading principles.
> The expenditure must be incidental to the business and must be necessitated or justified by commercial expediency. It must be directly and intimately connected with the business and be laid out by the taxpayer in his character as a trader. To be a permissible deduction, there must be a direct and intimate connection between the expenditure and the business i.e., between the expenditure and the character of the assessee as a trader, and not as a owner of assets, even if they are assets of the business.
>
> **2. M/s. Radhasoami Satsang Saomi Bagh, Agra vs. Commissioner of Income Tax [1992]193ITR 321 (SC)**
>
> 11. In that case Anand Marg was held to be a 'religious denomination' within the Hindu religion. It is not necessary for us to decide whether Radhasoami Satsang is a denomination of the Hindu religion or not as it is sufficient for our purposes that the institution has been held to be

religious and that aspect is no more in dispute in view of the frame of the question.

3. Smith Kline amp; French (India) Ltd. and Ors. vs. Commissioner of Income Tax [1996]219ITR 581 (SC)

7. We are unable to see as to how these observations help and assessee herein. Firstly, it may be mentioned, Section 10(4) of the 1922 Act or Section 40(a)(ii) of the present Act do not contain any words indicating that the profits and gains spoken of by them should be determined in accordance with the provisions of the Income Tax Act. All they say is that it must be a rate or tax levied in the profits and gains of business or profession. The observations relied upon must be read in the said context and not literally or as the provisions in a statute. But so far as the issue herein is concerned, even this literal reading of the said observations does not help the assessee. As we have pointed out hereinabove the surtax is essentially levied on the business profits of the company computed in accordance with the provisions of the Income-tax Act. Merely because certain further deductions (adjustments) are provided by the Surtax Act from the said profits, it cannot be said that the surtax is not levied upon the profits determined or computed in accordance with the provisions of the Income-tax Act. Section 4 of the Surtax Act read with the definition of "chargeable profits" and the First Schedule made the position abundantly clear.

8. We may mention that all the High Courts in the country except the Gauhati High Court have taken the view which we have taken herein. Only the Gauhati High Court has taken a contrary view in the decisions in Makum Tea Co. (India) Limited and Anr. v. Commissioner of Income Tax MANU/GH/0040/1989 and Doom Dooma Tea Co. Limited v. Commissioner of Income Tax MANU/GH/0033/1989. The decision of the Gauhati High Court in Makum Tea Co. (India) Limited, is under appeal before us in Civil Appeal Nos. 3976-77 of 1995. Similarly Civil Appeal No 3246 of 1995 is preferred against the decision of the Gauhati High Court following the decision in Doom Domma Tea Co. Limited. (On enquiry, the office has informed that no Special Leave Petition/Civil Appeal has been filed against the decision in Doom Dooma Tea Co. Limited.) For the aforesaid reasons, we can not agree with the view taken by the Gauhati High Court in the aforesaid decisions.

9. We agree with the view taken by the High Courts of (Calcutta) Molins (India) Limited v. Commissioner of Income Tax, West Bengal-III: [1983]144ITR317(Cal) and Brooke Bond (India) Limited v. Commissioner of Income Tax: [1992]193ITR390(Cal) , (Bombay) Lubrizol (India) Limited v. Commissioner of Income Tax: 187 I.T.R 25 followed in several other decisions of that Court, (Karnataka) Commissioner of Income Tax, Kamataka v. International Installments Private Limited: [1983]144ITR936(KAR) , (Madras) Sundaram Industries Limited v. Commissioner of Income Tax: [1986]159ITR646(Mad) , (Andhra Pradesh) Vazir Sultan Tobacco Co. Limited v. Commissioner of Income Tax: [1988]169ITR35(AP) , (Rajasthan) Association Stone Industries Co. Limited v. Commissioner of Income Tax (Gujarat) S.M. Maniklal Industries Limited v. Commissioner of Income Tax: [1988]172ITR176(Guj) followed in several cases thereafter (Allahabad) Himulyan Drug Co. Private Limited v. Commissioner of Income Tax: [1996]218ITR346(All) and (Punjab Haryana High Court) Highway Cycle Industries Limited v. Commissioner of Income Tax

4. SRD Nutrients Private Limited vs. Commissioner of Central Excise, Guwahati AIR 2017 SC 5299

21. Even otherwise, we are of the opinion that it is more rational to accept the aforesaid position as clarified by the Ministry of Finance in the aforesaid circulars. Education Cess is on excise duty. It means that those Assessees who are required to pay excise duty have to shell out Education Cess as well. This Education Cess is introduced by Sections 91 to 93 of the Finance (No. 2) Act, 2004. As per Section 91 thereof, Education Cess is the surcharge which the Assessee is to pay. Section 93 makes it clear that this Education Cess is payable on 'excisable goods' i.e. in respect of goods specified in the first Schedule to the Central Excise Tariff Act, 1985. Further, this Education Cess is to be levied @ 2% and calculated on the aggregate of all duties of excise which are levied and collected by the Central Government under the provisions of Central Excise Act, 1944 or under any other law for the time being in force. Sub-section (3) of Section 93 provides that the provisions of the Central Excise Act, 1944 and the Rules made thereunder, including those related to refunds and duties etc. shall as far as may be applied in

> relation to levy and collection of Education Cess on excisable goods. A conjoint reading of these provisions would amply demonstrate that Education Cess as a surcharge, is levied @ 2% on the duties of excise which are payable under the Act. It can, therefore, be clearly inferred that when there is no excise duty payable, as it is exempted, there would not be any Education Cess as well, inasmuch as Education Cess @ 2% is to be calculated on the aggregate of duties of excise. There cannot be any surcharge when basic duty itself is *Nil.*

12. We have heard counsel for the parties.

13. On the third issue in appeal no.52/2018, in view of the circular of CBDT where word "Cess" is deleted, in our considered opinion, the tribunal has committed an error in not accepting the contention of the assessee. Apart from the Supreme Court decision referred that assessment year is independent and word Cess has been rightly interpreted by the Supreme Court that the Cess is not tax in that view of the matter, we are of the considered opinion that the view taken by the tribunal on issue no.3 is required to be reversed and the said issue is answered in favour of the assessee.

13.1 Regarding question no.4 in Appeal No. 52/2018 for the assessment year 2004-05, it was stated that the same is not revenue expenses then for the relevant year, in our considered opinion, the CIT(A) has rightly accepted the details that payment has been made through cheque and the same has been reflected by the assessee in the balance sheet, merely on that ground the expenses cannot be disallowed since for earlier year it was accepted as capital expenses and capital gains, the issue ought to have been decided in favour of the assessee.

13.2 On first issue in Appeal No. 68/2018, in view of concurrent finding of both the authorities and in view of the fact that 86,08,460/- deduction which was allowed by the CIT (A) after following the detail reasoning and the matter was remitted to verify the accounts, in that view of the matter, the first question is answered in favour of assessee against the Department. Even on second question, in view of the concurrent finding though counsel for the appellant relied upon para-6, we are of the considered opinion that the funds borrowed to the extent which was from their own fund, interest is required to be deducted in view of the judgment of Supreme Court in **Godrej & Boyce Manufacturing Company Ltd. (supra)** relied on by Mr. Sanjay Jhanwar. Thus, issues No. 2 and 3 are required to be answered in favour of assessee against the Department. On the last issue, the finding of Tribunal being fact finding authority, the question No.4 is also required to be answered in favour of assessee against the Department.

14. Thus, the appeal of assessee being **No.52/2018** is partly allowed and issue No. 1 and 2 are answered as not pressed and issue No.3 and 4 are decided in favour of assessee.

15. In Appeal No. 68/2018, all the issues are answered in favour of assessee against the Department. Hence the appeal stands dismissed.

(ASHOK KUMAR GAUR),J (K.S.JHAVERI),J

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