IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION

INCOME TAX APPEAL NO.718 OF 2017

Pr.Commissioner of Income-Tax-2 … Appellant
V/s.
M/s State Bank of India … Respondent

Mr.Suresh Kumar for Appellant.
Mr.P.Pardiwala, Senior Advocate with Mr.N.Joshi i/by Mr.Atul Karsandas Jasani for the Respondent.

CORAM : AKIL KURESHI AND
S.J.KATHAWALLA, JJ.
DATE : JUNE 18, 2019.

P.C.:-

1. This appeal is filed by the revenue to challenge the judgment of the Income Tax Appellate Tribunal ("Tribunal" for short).

2. Following questions are presented for our consideration :-

> "i. Whether on the facts of the case and in law, ITAT was right in directing the A.O. to carry out verification and allow the claim of interest credited to "Interest Suspense Account" taxed in earlier years now written off

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during the year if found correct without clearly holding as to whether the interest is taxable in the year of credit of the suspense account or in the year of recovery?

ii. Whether on the facts and in the circumstances of the case and in law, the tribunal was justified in allowing deduction of expenditure of Rs.50 lakhs incurred by the assessee towards contribution to retired employees benefit scheme ignoring the provision of section 40A(9) of the Act which provide for deduction only for payment to approved/recognized funds as referred to section 36(1)(iv) & (v) of the Income Tax Act, 1961?"

iii. Whether on facts and in the circumstances of the case, the Tribunal was right in law in allowing a loss of Rs.16,84,481/- on account of loss on revaluation of permanent category investments, even though the same is a notional loss and inadmissible in law?

iv. Whether on the facts and in the circumstances of the case and in law, ITAT was right in deleting the disallowance without appreciating the fact that the disallowance determined by the Ld. CIT(A) on the basis of the decision of ITAT in the assessee's own case in earlier years and giving scientific method of disallowance of the interest expenses in respect of share purchase during the year?"

3. Question No.i arises out of the judgment of the Income Tax Appellate Tribunal in remanding the issue before the Assessing Officer for proper verification of

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facts. The record would suggest that the assessee, in view of its success before the Tribunal on the issue of disallowance of interest credited to Interest Suspense Account, had not pressed the ground of appeal in the earlier year, however, clarifying that if at all such decision of the Tribunal is reversed by the High Court the assessee would be at liberty to revise the claim. This offer of the assessee was accepted by the Tribunal. On the same ground in the present year the Tribunal followed the formula of the earlier year and for such limited purpose placed the matter before the Assessing Officer. We do not find any error. No question of law therefore arises.

4. Question No.ii relates to the revenue's objection to the assessee's claim of deduction of expenditure of Rs.50 lakhs towards contribution to a fund created for the health care of the retired employees. The revenue argues that such fund not being one recognized under Section 36(1)(iv) or (v), claim of expenditure was hit by the provisions of Section 40A(9) of the Income Tax Act,

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1961 (“the Act” for short).

5. The Tribunal while accepting such claim of the assessee observed that the assessee had made such contribution to the medical benefit scheme specially envisaged for the retired employees of the bank. Sub-section (9) of Section 40A of the Act, in the opinion of the Tribunal was inserted to discourage the practice of creation of bogus funds and not to hit genuine expenditure for welfare of the employees. The Tribunal also noted that the Assessing Officer had not doubted the bonafides of the assessee in creation of fund and that such fund was not controlled by the assessee-bank. The Tribunal proceeded on the basis that the Assessing Officer and the CIT (Appeals) had not doubted the bonafides in creation of the Trust or that the expenditure was not incurred wholly must exclusively for the employees. The Tribunal thus allowed the assessee’s appeal on this ground and deleted the disallowance.

6. Sub-section (9) was inserted to Section 40A of the

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Act by Finance Act, 1984 with the retrospective effect from 1st April, 1985 and reads as under:-

> "(9) No deduction shall be allowed in respect of any sum paid by the assessee as an employer towards the setting up or formation of, or as contribution to, any fund, trust, company, association of persons, body of individuals, society registered under the Societies Registration Act, 1860 (21 of 1860), or other institution for any purpose, except where such sum is so paid, for the purposes and to the extent provided by or under clause (iv) (or clause (iva) or clause (v) of sub-section (1) of section 36, or as required by or under any other law for the time being in force."

7. In plain terms, sub-section (9) of section 40A disallows deduction of any sum paid by an assessee as an employer towards setting up of or formation of or contribution to any fund, trust, company etc. except where such sum is paid for the purposes and to the extent provided under clauses (iv) or (iva) or (v) of sub-section (1) of Section 36 or as required by or under any other law for the time being in force. It is undoubted that the instance of the assessee does not fall in any of the above mentioned clauses of sub-section (1) of Section 36. However, the question remains whether the purpose of

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inserting sub-section (9) of section 40A of the Act was to discourage genuine expenditure by an employer for the welfare activities of the employees. This issue has been examined by this Court on multiple occasions. Before taking note of such decisions, we may notice that the explanatory notes on the provisions contained in the Finance Act, 1984, in the context of insertion of sub-section (9) to Section 40A of the Act records as under:-

> "(ix) Imposition of restrictions on contributions by employers to non-statutory funds.
> 16.1 Sums contributed by an employer to a recognised provident fund, an approved superannuation fund and an approved gratuity fund are deducted in computing his taxable profits. Expenditure actually incurred on the welfare of employees is also allowed as deduction. Instances have come to notice where certain employers have created irrevocable trusts, obstensibly for the welfare of employees, and transferred to such trusts substantial amounts by way of contribution. Some of these trusts have been set up as discretionary trusts with absolute discretion to the trustees to utilize the trust property in such manner as they may think fit for the benefit of the employees without any scheme or safeguards for the proper disbursement of these funds. Investment of trust funds has also been left to the complete discretion of the trustees. Such trusts are, therefore, intended to be used as a vehicle for tax avoidance by claiming deduction in respect of such contributions, which may even flow back to the

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employer in the form of deposits or investment in shares, etc.

16.2 With a view to discouraging creation of such trusts, funds, companies, association of persons, societies, etc. the Finance Act has provided that no deduction shall be allowed in the computation of taxable profits in respect of any sums paid by the assessee as an employer towards the setting up or formation of or as contribution to any fund, trust, company, association of persons, body of individuals, or society or any other institution for any purpose, except where such sum is paid or contributed (within the limits laid down under the relevant provisions) to a recognized provident fund or an approved gratuity fund or an approved superannuation fund or for the purposes of and to the extent required by or under any other law.

16.3 With a view to avoiding litigation regarding the allowability of claims for deduction in respect of contributions made in recent years to such trusts, etc., the amendment has been made retrospectively from 1st April, 1980. However, in order to avoid hardship in cases where such trusts, funds, etc. had before , 1st March 1984, bonafide incurred expenditure (not being in the nature of capital expenditure) wholly and exclusively for the welfare of the employees of the assessee out of the sums contributed by him, such expenditure will be allowed as deduction in computing the taxable profits of the assessee in respect of the relevant accounting year in which such expenditure has been so incurred, as if such expenditure had been incurred by the assessee. The effect of the under-lined words will be that the deduction under this provision would be subject to the other provisions of the Act, as for instance, section 40A(5), which would

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> operate to the same extent as they would have operated had such expenditure been incurred by the assessee directly. Deduction under this provision will be allowed only if no deduction has been allowed to the assessee in an earlier year in respect of the sum contributed by him to such trust, fund, etc."

8. The very purpose of insertion of sub-section (9) of section 40A thus was to restrict the claim of expenditure by the employers towards contribution to funds, trust, association of persons etc. which was wholly discretionary and did not impose any restriction or condition for expanding such funds which had possibility of misdirecting or misuse of such funds after the employer claimed benefit of deduction thereof. In plain terms, this provision was not meant to hit genuine expenditure by an employer for the welfare and the benefit of the employees.

9. In case of **Commissioner of Income Tax Vs. Bharat Petroleum Corporation Limited**[1], Division Bench of this Court considered a similar issue when the

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assessee had claim deduction of contribution towards staff sports and welfare expenses. The revenue opposed the claim on the ground that the same was hit by section 40A(9) of the Act. The High Court allowed the assessee’s appeal making following observations :-

> “For the aforestated assessment year 1985-86, the Assessing Officer disallowed Rs.2,60,283 under section 40A(9) paid by the assessee for staff welfare activities. The assessee claimed that the entire amount was for staff welfare activity. That, the said amount was a grant for staff welfare activity and that the entire amount was for the benefit of the employees and, therefore, the assessee claimed deduction as business expenditure under section 28. However, the Department rejected the assessee’s claim on the ground that a club known as Trombay Club was incorporated by the assessee for social, cultural and recreational activities of its members who were required to pay subscription fees. Hence, the Assessing Officer as also the Commissioner of Income-tax (Appeals) came to the conclusion that the said amount constituted contribution to the club and, therefore, under section 40A(9), the claim for deduction was disallowed. Being aggrieved, the assessee went in appeal to the Tribunal which took the view that the aforestated amount represented reimbursement of expenses incurred by a society and, therefore, it did not constitute contribution under section 40A(9). Being aggrieved by the decision of the Tribunal, the Department has come in appeal.
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> Findings on question No. 2:

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Bharat Petroleum Corporation is a Central Government undertaking. It has incorporated a club, essentially to carry on staff welfare activities. Under clause 28, Bharat Petroleum Corporation Limited had a right to issue directives to the club which were binding on the club. At times, the members of the club, who were the employees of Bharat Petroleum Corporation, took part in tournaments held outside the club premises like Times shield in cricket. On such occasions, the assessee-Corporation used to reimburse expenses incurred by the club. This is the finding of fact recorded by the Tribunal. In the circumstances, section 40A(9) is not applicable. No substantial question of law arises. Hence, our answer to the aforestated question No.2 is in the negative, i.e. in favour of the assessee and against the Department."

10. In case of **Commissioner of Income-tax-LTU Vs. Indian Petrochemicals Corporation Limited[1],** Division Bench of Bombay High Court considered the case where the assessee-employer had contributed to various clubs meant for staff and family members and claimed such expenditure as deduction. Once again the revenue had resisted in the expenditure by citing section 40A(9) of the Act. This Court confirmed the view of the Tribunal and dismissed the revenue's appeal, in which the Tribunal had

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allowed the expenditure claimed by the assessee.

11. Once again in case of **The Principal Commissioner of Income-Tax-14 Vs. Indian Oil Corporation reported in Income Tax Appeal No. 1765 of 2016,** revenue had raised such an issue when the assessee had spent certain amounts in either setting up or providing grant-in-aid made to Kendriya Vidyalaya Schools where the students of the assessee-Indian Oil Corporation would receive education. This Court referred to a judgment of Kerala High Court in case of **P. Balakrishnan, Commissioner of Income-Tax Vs. Travancore Cochin Chemicals Ltd.**[1] and of the decision of this Court in case of **Bharat Petroleum Corporation Limited (supra)** held that the Tribunal had correctly allowed the assessee's claim of expenditure. In view of this discussion, this question is not entertained.

12. With respect to question No.c, it is an agreed

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position that such an issue in case of this very assessee had traveled the High Court in Income Tax Appeal No.254 of 2014. In respect of this question, the Court observed as under:-

> "(i) It is agreed position between parties that the issue raised herein stands concluded against revenue and in favour of the respondent assessee by the order of this Court in CIT vs. Union Bank of India (Income Tax Appeal 1977 of 2013) rendered on 8th February, 2016.
> (ii) In the above view question (d) does not give rise to any substantial question of law. Thus not entertained."

13. In view of such discussion, this question is not entertained.

14. The sole surviving question (iv) arises out of the revenue's contention that the claim of the assessee under Section 80M of the Act should be on the net of the income and not gross. This issue is squarely covered in favour of the assessee by virtue of decision of this Court in case of **Commissioner of Income-tax-6 Vs. Modern Terry**

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Towers Ltd.[1]**.** This Court held that the principles applicable for computing deduction under Section 80HHC of the Act cannot be imported into Section 80M of the Act. The Court observed as under :-

> "The provisions of section 80HHC are entirely different from those of sections 80M and 80AA. There is no basis for importing the provisions of section 80HHC with section 80M. The same does not lead to a satisfactory computation of the net dividend under section 80M."

15. In the result, Income Tax Appeal is dismissed.

(S.J.KATHAWALLA, J.) **(AKIL KURESHI, J.)**

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1 (2014) 43 taxmann.com 466 (Bombay)

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