‘’FREEBIES’’: PROPOSED AMENDMENT IN 37(1).A BRIDGE CROSSED TOO SOON? RULING IN APEX LABS BY SC ON 22ND FEBRUARY 2022

1.The Finance Bill 2022 proposes to add an Explanation to s 37(1).Yet another case of haste making waste beckons us.Attempting to do via legislating what was clearly in favour of revenue by multiple court decisions and ironically acknowledged in the Memorandum itself.When original legislation is laid down it defines law.But when it is used to negate adverse rulings, it sets in motion ,trends which diminish the majesty of law as law is seen as a reactive creation rather than a proactive measure.And when it piggybacks on a special bench reference ignoring the larger body of law ,a remedy is created which is in certain aspects,worse than the disease.It shows the earlier drafted legislation in poor light and strains the mischief rule unnecessarily.And it looks like a self goal when a ruling like Apex Labs comes by the Apex Court even while the amendment is in the form of a bill. We shall see this subsequently .

2.The proposed amendment:

*‘’ 12. **In section 37 of the Income-tax Act**, in sub-section (1),after Explanation 2, the following Explanation shall be inserted,namely:––*

‘Explanation 3.––For the removal of doubts, *it is hereby clarified that the expression “**expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law**” under Explanation 1, **shall include and shall be deemed to have always included** the expenditure incurred by an assessee,––*

(i)for any purpose which is an offence under, or which is prohibited by, any law for the time being in force, ***in India*** ***or outside India****; or*

(ii) ***to provide any benefit or perquisite****, in whatever form, to a person, whether or not carrying on a business or exercising a profession, and acceptance of such benefit or perquisite by such person* ***is in violation of any law or rule or regulation or guideline, as the case may be, for the time being in force, governing the conduct of such person****; or*

(iii) ***to compound an offence*** *under any law for the time being in force, in India* ***or outside India****.'.*

The terms "**rule**" ,"**regulation**" and "**guideline**" have not been defined in the I.T.Act..So we turn to some generic legal understanding thereof and are faced with interpretational challenges which we shall see subsequently.

3.MEMORANDUM EXPLAINING THE PROVISIONS IN THE FINANCE BILL, 2022

Clarifications on allowability of expenditure under section 37

Section 37 of the Act provides for allowability of revenue and non-personal expenditure (other than those failing under sections 30 to 36) laid out or expended wholly and exclusively for the purposes of business or profession. Explanation 1 of sub-section (1) of section 37 of the Act provides that if any expenditure incurred by an assessee ***for any purpose which is an offence or which is prohibited by law*** *shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure.*

2. However, it is seen that ***certain taxpayers are claiming deductions*** *on expenditure incurred in offering certain benefits or perquisite to a person* ***which are not intended to be allowed*** *under this section, like meeting his expenditure related to travel, hospitality, conference etc. In these cases acceptance of such benefit or perquisite by such person* ***is in violation of a law or rule or regulation or guidelines, as the case may be, governing the conduct of such person.***

3. CBDT, vide circular No. 5/2012 dated 1.8.2012, noted that the Indian Medical Council in exercise of its statutory powers amended the Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 (the regulations) on 10.12.2009 ***imposing a prohibition on the medical practitioner and their professional associations from taking any Gift, Travel facility, Hospitality, Cash or monetary grant from the pharmaceutical and allied health sector Industries****. Accordingly, CBDT clarified that the claim of any expense incurred in providing above mentioned or similar benefits in violation of the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 shall be inadmissible under section subsection (1) of section 37 of Act being an expense prohibited by the law.* ***This disallowance was directed to be made in the hands of such pharmaceutical or allied health sector Industries or other assessee*** *which has provided aforesaid benefits and claimed it as a deductible expense in its accounts against income.*

4. This circular was challenged in Himachal Pradesh High Court in the case of ***Confederation of Indian Pharmaceutical Industry Vs Central Board***

of Direct Taxes [(2013) 335 ITR 388 (HP)]*, in which the Hon'ble High Court rejected the petition and held that -*

"The regulation of the Medical Council prohibiting medical practitioners from availing of freebies is a very salutary regulation which is in the interest of the patients and the public. This Court is not oblivious to the increasing complaints that the medical practitioners do not prescribe generic medicines and prescribe branded medicines only in lieu of the gifts and other freebies granted to them by some particular pharmaceutical industries. Once this has been prohibited by the Medical Council under the powers vested in it, s. 37(1) comes into play. ***The Petitioner's contention that the circular goes beyond the section is not acceptable.*** *In case the assessing authorities are not properly understanding the circular then the remedy lies for each individual assessee to file an appeal but* ***the circular which is totally in line with s. 37(1) cannot be said to be illegal****. If the assessee satisfies the assessing authority that the expenditure is not in violation of the regulations framed by the medical council then it may legitimately claim a deduction, but it is for the assessee to satisfy the AO that the expense is not in violation of the Medical Council Regulations."*

5. After this there have been various judgments of Income-tax Appellate Tribunals.Some of these judgments have held that these expenses to be not allowable under sub-section (1) of section 37 the Act, while others holding it to be allowable. The latest judgment on this issue is from ITAT Mumbai in the case of ***Macleods Pharmaceuticals delivered on 14th October 2021*** *in ITA Nos. 5168 & 5169/Mum/2018. In this judgment ITAT held that the*

action of the assessing officer in disallowing the expenditure deserves to succeed and then explained as to why it is a fit case for the constitution of a special bench of three or more members. ITAT arrived at its recommendations based, inter-alia, on the followings:-

i. Honble Supreme Court, in the case of Keshavji Ravji& Co Vs CIT [(1990) 183 ITR 1 (SC)] has held that the burden that the Act itself through a correct interpretation of law envisages is equal to or higher than the burden envisaged by the CBDT circular, that burden of law cannot be negated because the circular also so states. Hence, the circular no 5 of 2012 is to be held as valid.

*ii. Once a judicial forum higher than this Tribunal, (i.e Himachal Pradesh High Court in the case of Confederation of Indian Pharmaceutical Industry) holds that the interpretation to the scope of Explanation to sub-section (1) of section 37, as given in the circular, is a correct legal interpretation, i**t cannot be open to us to discard the interpretation so approved** to be correct legal interpretation.*

*iii. In the case **Kap Scan and Diagnostic Centre (P) Ltd. [(2012) 344 ITR 476 (P&H)]**, the Hon'ble High Court of Punjab & Haryana held that **payments which are opposed to public policy** being in the nature of unlawful consideration cannot equally be recognized. It cannot be held that businessmen are entitled to conduct their business even contrary to law and claim deductions of payments as business expenditure, notwithstanding that such payments are illegal or opposed to public policy or have pernicious consequences to the society as a whole. The Court further held that if*

demanding of such commission was bad, paying it was equally bad. Both were privies to a wrong. Therefore, such commission paid to private doctors was opposed to the public policy and should be discouraged. The payment of commission by the assessee for referring patients to it cannot by any stretch of imagination be accepted to be legal or as per public policy. Undoubtedly, it is not fair practice and has to be termed as against the public policy.

iv. ITAT noted earlier coordinate bench judgment in the case of ***DCIT Vs PHL Pharma Pvt Ltd (2017) 163 ITD 10 (Mum),*** *where it was held that the disallowance could not be sustained as the MCI guidelines bind only the medical professionals and not the pharmaceutical companies. ITAT noted that this judgment was not in line with earlier co-ordinate bench judgment In the case of* ***Liva Healthcare Ltd, (2016) 161 ITD 63 (Mum)*** *where the Hon'ble Mumbai ITAT has held that the CBDT circular dated 01.08.2012 is merely a clarification in nature and creates a bar on such illegal payments being against public policy, the said bar always existed in the statute by virtue of the existence of Explanation of Section 37 of the Act which was inserted by Finance Act, 1998 w.e.f. 01-04-1962. It was also noted that in Hon'ble AP High Court's full bench decision in the case of CIT Vs B R Constructions (1993) 202 ITR 222 (AP- FC) their Lordships have observed that a "****precedent ceases to be a binding precedent ... (iii) when it is inconsistent with the earlier decisions of the same rank; and (iv) when it is rendered per incuriam".Clearly, therefore, the decisions which disregard earlier binding decisions on the same issue, "cease to be a binding judicial precedent".***

v. ITAT also noted that ***Hon'ble Delhi High Court in the case of Max Hospital Vs Medical Council of India (WP No. 1334 of 2013; judgment dated 10th January 2014)****, in which it was held that the provisions of Medical Council of India only bind the medical professionals and not others, such as hospitals and pharmaceutical companies. ITAT explained that it was a case in which Ethics Committee of the Medical Council of India, upon a complaint alleging death of a patient due to medical negligence, passed an order punishing the erring doctors but this order also had certain adverse remarks against the Max Hospital as well.Aggrieved by these observations, Max Hospital filed a writ petition contending that since the Medical Council of India (Professional Conduct, Etiquette and Ethics) Regulations, have been framed in exercise of the power conferred under Section 20-A read with Section 33 (m) of the Indian Medical Council Act, 1956, these regulations do not govern or have any concern with the facilities, infrastructure or running of the Hospitals and secondly, that the Ethics Committee of the MCI acting under the Regulations had no jurisdiction to pass any direction or judgment on the infrastructure of any hospital which power rests solely with the concerned State Govt. It was also contended that the Petitioner was not provided an opportunity of being heard and thus the principles of natural justice were violated. While dealing with these grievances,* ***Hon'ble Delhi High Court has held, in its operative portion of the judgment- which was reproduced by the ITAT in entirety, as follows:***

"8. It is clearly admitted by the Respondent that it has no jurisdiction to pass any order against the Petitioner hospital under the 2002 Regulations. In fact,

it is stated that it has not passed any order against the Petitioner hospital. Thus, I need not go into the question whether the adequate infrastructure facilities for appropriate post-operative care were in fact in existence or not in the Petitioner hospital and whether the principles of natural justice had been followed or not while passing the impugned order. Suffice it to say that the observations dated 27.10.2012 made by the Ethics Committee do reflect upon the infrastructure facilities available in the Petitioner hospital and since it had no jurisdiction to go into the same, the observations were uncalled for and cannot be sustained.

9. Since the MCI had no jurisdiction to go into the infrastructure facilities, I need not also go into the aspect that in the year 2011, the facilities available in the hospital were inspected and were found to be in order.

10. The petition therefore has to succeed. I hereby issue a writ of certiorari quashing the adverse observations passed by the MCI against the Petitioner hospital highlighted in Para 1 above."

ITAT thus held that in their humble understanding, the judgment of Delhi High Court does not negate, dilute, or even deal with, ratio decidendi of, or even casual observations in, Hon'ble HP High Court's judgment *in the case of Confederation of Indian Pharmaceutical Industry (discussed earlier). These judgments are in altogether in different field.*

vi. ITAT thus noted that while Hon'ble HP High Court dealt with the interpretation of Explanation to sub-section (1) of section 37, Hon'ble Delhi High Court dealt with the powers of the MCI to pass an order against a Hospital in Delhi on the question of adequacy regarding infrastructure

facilities by Hospitals in Delhi, and that too without affording an opportunity of hearing to the said hospital. Hon'ble Delhi High Court judgment in Max Hospitals case has no bearing on the question as to whether giving benefits to the medical professionals is in violation of law or not. ITAT further noted that it is also well settled in law, including by Hon'ble jurisdictional High Court in the case of CIT v. Sudhir Jayantilal Mulji (1995) 214 ITR 154 (Bom),that a judicial precedent is only "an authority for what it actually decides and not what may come to follow from some observations which find place therein".

vii. On the coordinate bench judgment in the case of DCIT Vs PHL Pharma Pvt Ltd (2017), ITAT noted the following:-

"The more we ponder about the rationale of PHL Pharma decision (supra), the more convinced we are that this decision calls for reconsideration by a larger bench. In our humble understanding, conclusions arrived in the said decision do not reflect the correct legal position, and the same is the position with respect to a large number of other coordinate bench decisions following the said decision or following the line of reasoning in the said decision- as discussed above. However, in all fairness, while we may or may not agree with a coordinate bench decision, it cannot be open to us to disregard the same, lest such judicial inconsistency should shake public confidence in the administration of justice and lest one of the fundamental legitimate expectations of the stakeholders, i.e. those exercising judicial functions will follow the reason or ground of the judicial decision in the earlier cases on identical matters, will stand declined. "It is, however, equally true", to borrow

the words of Hon'ble Supreme Courts as articulated in the case of Union of India Vs Paras Laminates Pvt Ltd [(1990) 186 ITR 722 (SC)], "that it is vital to the administration of justice that those exercising judicial power must have the necessary freedom to doubt the correctness of an earlier decision if and when subsequent proceedings being to light what is perceived by them as an erroneous decision in the earlier case" and that "in such circumstances, it is but natural and reasonable and indeed efficacious that the case is referred to a larger bench". Taking a cue from the path so guided by Hon'ble Supreme Court in the case of Paras Laminates (supra), ***we recommend constitution of a bench of three or more Members*** *to consider the question as to whether or not an item of expenditure on account of freebies to medical professionals, which is hit by rule 6.8.1 of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002- as amended from time to time, read with section 20A of the Indian Medical Council Act 1956, can be allowed as a deduction under section 37(1) of the Income Tax Act, 1961 read with Explanation thereto, in the hands of the pharmaceutical companies.*

6. Thus, the legal position is clear that the claim of any expense incurred in providing various benefits in violation of the provisions of Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002 shall be inadmissible under section sub-section (1) of section 37 of Act being an expense prohibited by the law. Delhi High Court decision which was relied upon by ITAT in some decisions was in completely different context as discussed by ITAT Mumbai in their judgment in the case of Macleods

Pharmaceuticals. These ITAT decisions allowing such expenditure are clearly not in line with the intention of the legislation.

7. ***Further, some taxpayers are seen to be claiming deduction on expenses incurred for a purpose which is an offence under foreign law or for compounding of an offence for violation of foreign law, claiming that provisions of Explanation 1 to subsection (1) of section 37 of the Act applies only to offences which are prohibited by the domestic law of the country****. In some case this view has also been accepted by the tribunal. These judgments are also against the intention of the legislation as the legislation does not say that the Explanation 1 applies only to the violation of domestic law.*

8. In order to make the intention of the legislation clear and to make it free from any misinterpretation, ***it is proposed to insert another Explanation*** *to sub-section (1) of section 37 to further clarify that the expression "expenditure incurred by an assesse for any purpose which is an offence or which is prohibited by law", under Explanation 1, shall include and shall be deemed to have always included the expenditure incurred by an assessee, —*

i. for any purpose which is an offence under, or which is prohibited by, any law for the time being in force, in India or outside India; or

ii. ***to provide any benefit or perquisite, in whatever form, to a person, whether or not carrying on a business or exercising a profession, and acceptance of such benefit or perquisite by such person is in violation of any law or rule or regulation or guidelines, as the case may be, for the time being in force, governing the conduct of such person****; or*

iii. ***to compound an offence under any law for the time being in force, in India or outside India.***

9. This amendment will take effect from 1st April, 2022.

[Clause 12]

4.THE ORIGINAL PROVISION AND ITS RATIONALE:

S 37

Explanation 1. **—For the removal of doubts, it is hereby declared that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure.]**

4.1 This explanation was Inserted by the Finance (No. 2) Act, 1998, w.r.e.f. 1-4-1962.

This is how the Finance Act 1998 explained it:

Amendment of section 37.

15. In section 37 of the Income-tax Act, after sub-section (1), **the following *Explanation* shall be inserted and shall be deemed to have been inserted with effect from the 1st day of April, 1962, namely :—**

"*Explanation.*—For the removal of doubts, it is hereby declared that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been

incurred for the purpose of business or profession and no deduction or allowance shall be made in respect of such expenditure.".

Terrific piece of drafting here. ***"shall be inserted and shall be deemed to have been inserted with effect from the 1st day of April, 1962,";*** this is how law is made.

4.2 The Memorandum to the Bill read as under:

Disallowance of illegal expenses

It is proposed to insert an explanation after sub-section (i) of section 37 to clarify that no allowance shall be made in respect of expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law. ***This proposed amendment will result in disallowance of the claim made by certain tax payers of payments on account of protection money, extortion, hafta, bribes, etc. as business expenditure.*** *This amendment will take effect from 1st April, 1962 and will accordingly apply in relation to the assessment year 1962-1963 and subsequent years. [Clause 17]*

4.2.1"ETC."is vital here.It is only an inclusive explanation ,not a exhaustive one.We shall expand on this later.

4.3 Notes on clauses read as under:

"Clause 17 seeks to amend section 37 of the Income-tax Act relating to general expenditure. It is proposed to insert an Explanation in sub-section (1) of section 37 of the Income-tax Act so as to clarify that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be allowed. ***This amendment will take effect retrospectively from 1st April, 1962 and will, accordingly, apply in relation to assessment year 1962-1963 and subsequent years."***

This is the manner and method in which Explanations are inserted.To me, an explanation normally only clarifies what is part of law and has to be retrospective by definition. The Explanation,in normal drafting terms is only **a declaratory legislation, for removal of doubts.**

4.4 Now Revenue defeats the very concept by making it applicable w.e.f 1.4.2022 but contradicting itself yet again in the opening lines of the new Explanation 3 by saying:

*''**"Explanation 3.––**For the removal of doubts, it is hereby clarified that the expression **"expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law"** under Explanation 1, **shall include and shall be deemed to have always included…….."***

4.4.1 This is astonishing.Two phrases in particular need pointing out:

***1."For the removal of doubts":* See the 1998 amendment.It uses the same phrase.But says the explanation is retrospective w.e.f.1-4-1962!!**And it has stood the judicial test and test of time.That has been diluted irreparably now by some astonishingly dim witted drafting by CBDT and puts in peril the Apex Labs decision because it virtually validates all such acts prior to AY 2022-23 and the superb interpretation by hon'ble SC is opened theoretically to a review petition by the assessee in Apex Labs stating that legislative intent has been clarified now and it applies w.e.f. AY 22-23.It also arguably shuts down all doors of 263/154/148 action for revenue in all unfavourable decisions prior to the amendment date,which was possible because interpretation of law by hon'ble SC means that this is what the provision meant from the very beginning and in any case after the date 14-12-2009[**sic.**The amendment is dated 10.12.2009] in case of medical freebies(ref para 4 of Apex Labs judgment) .But shockingly ,now the

revenue says ,there were doubts,we clarify the doubts and with this clearer vision we shall apply the renewed understanding **prospectively whereas the Apex Court is in their favour retrospectively**!This is numbing beyond words and as an ex-officer I deeply regret the ineptitude exhibited by the TPL division of CBDT in proposing this insertion in this manner even while quoting Liva decision in Memorandum[para iv which clearly upholds retrospectivity].Its a superb self goal yet again and that too in the last minute!

2. 'shall be deemed to have always included":CAN Revenue explain what ''**always**" means?If it is prospective ,it can't mean right from the beginning.Then why say it when intent in memorandum is prospective?

4.5 Same unmindful drafting daftness occurred in regard to **employee's contribution u/s 36(1)(va)** after insertion of Explanation 2 in the form of whether the amendment has **retrospectivity.**Litigation ensued on that as well.I had written an article on the same with specific reference to retrospectivity.Those interested can access it at **https://itatonline.org/digest/articles/retrospectivity-of-explanation-2-inserted-below-s-36-1va/**

Suffice it should to say here that accepted interpretation is that this phrase normally has an imbedded retrospectivity.

5.THE RETROSPECTIVITY SCARE:

The scare of retrospectivity has gotten into revenue ever since the ill defended and completely misunderstood Cairns matter where a refund was possible in view of international arbitration without disturbing a fine piece of legislation labelled as ''retro law and draconian and anti business" by people whose dim witted understanding of law is exceeded only by their

own dim witted understanding.So much so that now an amendment clearly shows retrospectivity and yet the explanatory memorandum contradicts the main provision!Rather, as I shall demonstrate later,even retrospectivity need not even be pleaded since this is merely clarificatory.To argue that there cannot be retrospective pecuniary penalization by an enacted fiscal law has no legal legs to stand upon.This amendment ,sadly to say drove entirely on the larger bench reference by ITAT Mumbai Macleods decision and went on to quote virtually the whole decision in its Memorandum, an unwelcome and undesirable trend by Revenue, that in my humble opinion diminishes the majesty of law in no small measure.It ,in the process, failed to not only not notice other healthy judicial precedents but also ,inspite of noting other contra decisions(shown plainly wrong in context of Apex Court judgment which we shall see)failed to ensure retrospective insertion in an unqualified manner to ensure that legally perverse decisions like PHL (supra), Aristo and others did not stand.

5.1 The following precedents,among others, went completely unnoticed in regard to retrospectivity:

1.*J.K. Jute Mills Co. Ltd.* v. *State of U.P.*, AIR 1961 SC 1534:competence of legislature to enact retrospectively upheld

2.*Sudhindra Thiratha Swamiar* v. *Commissioner, H.R. & C.E.*, AIR 1963 SC 966:levy of fee retrospectively upheld

3.*Entertainment Tax Officer* v. *Ambae Picture Palace*, [1994] 1 SCC 209:

*"13. **If the Parliament or the State Legislatures have competence to legislate, they can do so prospectively as well as retrospectively and taxation laws are no exception to this power.** (Reference in this connection may be made to the*

decision of this Court in Union of India v. Madan Gopal Kabra). Again in Krishnamurthi & Co. v. State of Madras this Court held that the legislative power conferred on the appropriate legislatures to enact laws in respect of topics covered by the several entries in the three lists can be exercised both prospectively and retrospectively."

4.*CIT* v. *Gold Coin Health Food (P.) Ltd.* [2008] 304 ITR 308/172 Taxman 386 (SC): retrospectivity of explanation to penal provisions upheld

5.2 It is now well settled that there is always a presumption of constitutionality whenever a legislation enacted by the Parliament or the State Legislature is questioned on the ground of unconstitutionality and the burden is on the petitioner bringing such a challenge. In the case of ***J & K* v. *T.N. Khosa*, AIR 1974 SC 1,** a Constitution Bench of the hon'ble Supreme Court, observed that **there is always a presumption in favour of the constitutionality of an enactment** and the burden is on him who attacks it to show that there has been a clear transgression of the constitutional principles.

This majesty of enacted law has clearly not been understood by revenue.

5.2.1 Hon'ble Supreme Court recognizes the considerable latitude in the Parliament in framing a taxing statute. ***In P.M. Ashwathanarayana Setty* v. *State of Karnataka*, AIR 1989 SC 100,** the Apex Court observed as under:

> "30. The problem is indeed, a complex one not free from its own peculiar difficulties. Though other legislative measures dealing with economic regulation are not outside Art. 14, **it is well recognised that the State enjoys the widest latitude where measures of economic regulation are concerned.** These measures for fiscal and economic regulation involve an evaluation of diverse and quite often conflicting economic criteria and

adjustment and balancing of various conflicting social and economic values and interests. **It is for the State to decide what economic and social policy it should pursue and what discriminations advance those special and economic policies. In view of the inherent complexity of these fiscal adjustments, Courts give a larger discretion to the Legislature** in the matter of its preferences of economic and social policies and effectuate the chosen system in all possible and reasonable ways. If two or more methods of adjustments of an economic measure are available, **the Legislative preference in favour of one of them cannot be questioned on the ground of lack of legislative wisdom** or that the method adopted is not the best or that there were better ways of adjusting the competing interests and claims. **The legislature possesses the greatest freedom in such areas. The analogy of principles of the burden of tax may not also be inapposite in dealing with the validity of the distribution of the burden of a 'fee' as well."**

5.3 What does an Explanation do;"For the removal of doubts" meaning:

Ordinarily, an explanation is introduced by the Legislature for clarifying some doubts or removing confusion which may be possible from the existing provisions. Normally, therefore, an explanation would not expand the scope of the main provision and the purpose of the explanation would be to fill a gap left in the statute, to suppress a mischief, to clear a doubt or as is often said to make explicit what was implicit.

In the case of ***S. Sundaram Pillai* v. *V.R. Pattabhiraman*, AIR 1985 SC 582,** the Apex Court observed that an explanation added to a statutory provision is not a substantive provision, but as the plain meaning of the word itself shows, it is merely meant to explain or clarify certain ambiguities which may have crept in the statutory provision. It was observed as under:

"52. Thus, from a conspectus of the authorities referred to above, it is manifest that ***the object of an Explanation to a statutory provision is -***

(a) to explain the meaning and intendment of the Act itself,

(b) where there is any obscurity or vagueness in the main enactment, to clarify the same so as to make it consistent with the dominant object which it seems to subserve,

(c) to provide an additional support to the dominant object of the Act in order to make it meaningful and purposeful,

(d) an Explanation cannot in any way interfere with or change the enactment or any part thereof but where some gap is left which is relevant for the purpose of the Explanation, in order to suppress the mischief and advance the object of the Act it can help or assist the Court in interpreting the true purport and intendment of the enactment, and

(e) it cannot, however, take away a statutory right with which any person under a statute has been clothed or set at naught the working of an Act by becoming an hindrance in the interpretation of the same."

5.4 The clincher: Parixit Industries Pvt. Ltd. [2013] 352 ITR 349 (Gujarat)

"25. It is now a settled law that **if an explanation is added to a section of a statute for the removal of doubts, the implication is that the law was the same from the very beginning** and the same is further explained by way of addition of the Explanation. **Thus, it is not a case of introduction of new provision of law by retrospective operation.** ……."

And this ruling was given in favour of the assessee in context of 147 action taken by the AO!

SLP filed by revenue in this case was dismissed. **[2012] 25 taxmann.com 301 (SC).**

Sometimes defeats hide in themselves seeds of hope.This was one such defeat.And yet the hope wasn't realized.!

5.5 A sterling illustration of judicially approved retrospectivity can be seen in Tube Investments of India Ltd. [1990] 33 ITD 444 (MAD.) wherein the legal issue was whether clause (c) to Explanation to section 263 was added by Finance Act 1989 with effect from 1-6-1988 had retrospective effect.

See the outstanding Memorandum drafted by Revenue there which is almost analogous to our situation here:

Memorandum explaining **provisions in Finance Bill, 1989 (176 ITR St. 127) which runs as follows:**

"Under the existing provisions of sec. 263 of the Act and corresponding provisions of the Wealth-tax and Gift-tax Act, the Commissioner of Income-tax is empowered to call for and examine the record of any proceeding and if he considers that the order passed by the Assessing Officer is erroneous insofar as it is prejudicial to the interests of Revenue, he may pass such order thereon as the circumstances of the case justify, including an order enhancing or modifying the assessment, or cancelling the same or directing a fresh assessment. ***By the Finance Act, 1988, an Explanation was substituted with effect from 1st June, 1988,*** *to the relevant Sections of the Act, to clarify that the term 'record' would include all records relating to any proceeding available at the time of examination by the Commissioner. Further, it was also clarified that the Commissioner is competent to revise an order of assessment passed by an Assessing Officer on all matters except those which have been considered and decided in an appeal.* ***The above Explanation was incorporated in the Finance Act, 1988, to clarify this***

legal position to have always been in existence. Some Appellate Authorities have, however, decided that the Explanation will apply only prospectively, i.e., only to those orders which are passed by the Commissioner after 1-6-1988. Such an interpretation is against the legislative intent and it is, therefore, proposed to amend sec. 263 of the Income-tax Act, so as to clarify that the provisions of Explanation shall be deemed to have always been in existence.

Amendments on the above lines have been proposed in sec. 25 of the Wealth-tax Act and sec. 24 of the Gift-tax Act also."

On this aspect of retrospectivity and the amendment ,an outstandingly brilliant ruling was given by the bench :

[quote]"4. We have heard the rival submissions. In our opinion, the contention of the assessee that the Commissioner has no jurisdiction to pass the order u/s 263 on the ground that entire order of the Income-tax Officer has merged with that of the CIT(A), cannot be accepted. It is not disputed that the CIT(A) had not been called upon to adjudicate on the issue whether the assessee is entitled to a higher rate of depreciation in respect of the written down value of the plant and machinery added to its block in the earlier years. What was subject matter of appeal before the CIT(A) was only whether the assessee is entitled to higher rate of depreciation in respect of the items of plant and machinery added during the course of the ear and not in respect of the w.d.v. of the machineries installed in the earlier years. **Clause (c) of the Explanation to sec. 263, introduced by Finance Act, 1988 and later amended by Finance Act. 1989 runs as follows:**

"Explanation: For the removal of doubts, it is hereby declared that, for the purposes of this sub-section, —

(c) where any order referred to in this sub-sec. and passed by the Assessing Officer had been the subject matter of any appeal filed on or before or after the 1st day of June, 1988, the powers of the Commissioner under this sub-section shall extend and shall be

deemed always to have been extended to such matters as had not been considered and decided in such appeal."

The Explanation clearly states that it was enacted for removal of doubts. It also declares the position of law that should be deemed to have existed at all times. When a statutory provision for removal of doubts declares that the powers of the CIT under section 263 shall be deemed always to have extended to such matters as are not considered and decided in an appeal, such legislation, in our opinion, will have retrospective effect and the Commissioner, when he has decided the issue in the present case shall be deemed to have had the powers to revise the order of the Income-tax Officer in respect of the matter which he had chosen to revise.

.....

''7. Thus it is clear from the above that the insertion of the Explanation and the amendment made thereto are to clarify the correct legal position and to clear the doubts created by some judgments of the appellate authorities, in which it was held that the Explanation would apply only prospectively. It is now well settled that an Explanation must be interpreted according to its own tenor. If the words used in the Explanation clearly indicate that the intention of the Legislature is to make it retrospective in its operation and their intention is clearly spelt out in it, such a provision should be taken as retrospective. **According to Maxwell (see the Interpretation of Statutes, Twelfth Edition, page 216) if the language or the dominant intention of the enactment so demands, the Act must be construed so as to have retrospective operation,** for the rule against the retrospective effect of statutes is not a rigid or inflexible rule but is one to be applied always in the light of the language of the statute and the subject-matter with which the statute is dealing. The mere fact that the footnote says that the Explanation has effect from 1-6-1988, does not take away the effect of the words used in the Explanation declaring the law that should be taken as having existed from the very beginning. It only means that any authority interpreting the provisions on or after 1-6-1988 has to take note of the Explanation also, while interpreting the section.

8. The Calcutta High Court had an occasion to consider a similar situation arising out of an amendment made to sec. 34 of the Income-tax Act 1922 with effect from 30th March, 1948. On a writ filed by the assessee, Bose J., the learned Single Judge of Calcutta High Court held that the amendment is expressly made retrospective from 30th March, 1948 and so it had no further retrospective operation. On an appeal filed by the Department, the Division Bench held that while the section itself came into operation on 30th March, '48, in deciding in what manner it would operate, it is pertinent to enquire from what the section itself says. The effect of sec. 8 of the Amending Act was that it placed the section on the Statute Book as on 8th March, 1948 and made it part of the I.T. Act from that date. But what was the effect of such introduction of the new sec. 34 to the I.T. Act itself has to be found out by examining the words of the section itself. Though the decision of the Division Bench was ultimately upset by the Supreme Court in Calcutta Discount Co. Ltd. v. ITO [1961] 41 ITR 191, on some other point, the above view expressed by the Division Bench of the Calcutta high Court was approved by the **Supreme Court in S.C. Prashar v. Vasantsen Dwarkadas [1963] 49 ITR 1 at page 16.** Thus, though the Explanation itself was brought into the Statute Book from 1-6-1988, to find out the effect of the Explanation, the express words used by the legislation have to be examined Looked at from that angle, in our opinion, the wording of the Explanation makes it very clear that its effect will be not only in respect of the orders passed by the Commissioner after 1-6-1988 but also in respect of orders passed before that date.

9. The Madhya Pradesh High Court in the case of Vithal Textiles (supra), [note**:CIT v. Vithal Textiles [1989] 175 ITR 629 (MP**)] while examining the retrospective effect of the Explanation held that **the declaratory Act may be defined as an Act to remove doubts existing as to the common law, or the meaning or effect of any statute. Such Acts are usually held to be retrospective.** In that case the Court was considering Cl. (a) of Explanation to sec. 263 which is also enacted for removal of doubts. Though the Explanation came into force from 1-10-1984, it was held that the amending Act, being declaratory, must be held to be retrospective.

10. From the above discussion, it will be clear that after the enactment of the Explanation and its subsequent amendment in 1989, it will not be possible to hold that the Commissioner had no powers to revise that portion of the order of the ITO

which had not been subject matter of appeal before the CIT(A) and on which he had not rendered any decision. In the result we reject the assessee's contention in this regard."[unquote]

There is hope for Revenue yet in this regard due to the clear interpretation of footnote about date of insertion of provision.Only if they were to realize it!

6.The Significance of "ETC.":

In para 4.2.1(supra) I had referred to the word" etc."in context of Memorandum to Finance Bill 1998 where the phrase " ***protection money, extortion, hafta, bribes, etc."*** **was used.**As we shall see ,the phrase was enough to cover a situation like freebies which majorly prompted the proposed amendment.The Apex Court decision has put it beyond pale of doubt ,but notwithstanding, **the informed inexactitude of "etc." has a defining and determining generic role to play**.Let's see whether,without the SC ruling of 22.2.22 the freebies issue was capable of being attacked or not.The meaning ,role and function of the term "etc." has been well explained in **CIT vs. MAULANA TEA CO. (2000) 244 ITR 0589(KER.)[** CONTEXT:S 271B; Circular No. 432, dt. 20th Sept., 1985]:

" Learned counsel for the Revenue, with reference to Circular No. 432, dt. 20th Sept., 1985 (supra), submitted that restriction on levy of penalty was relatable to filing of estimates, payment of advance tax, filing of returns in time and not to a case covered under s. 271B of the Act. ***This submission overlooks the use of expression "etc." after mentioning some of the specified categories of default.*** *"Etc." is an abbreviation of "et cetra", may mean and others and so forth; and the rest; other things; other things of the same character, or only those things ejusdem generis. Intention of the parties, the*

context and the manner and place in which the abbreviation is used may govern its meaning. ***Word 'etc' does not share the character of an inclusive definition. Usually, after reciting the initiatory words of a set formula, or a clause given in full, etc. is added as an abbreviation for the sake of convenience.*** *Circular No. 432, dt. 20th Sept., 1985 did not refer to any particular type or category of failure to carry out statutory obligation and use of the word 'etc.', cannot be given any restrictive meaning. In any event, subsequent circulars made it clear that intention was to give immunity from penal proceedings of all nature. Tribunal was, therefore, justified in directing deletion of the penalty under s. 271B."*

Again this defeat carried within it seeds of victory in another battlefield such as the one which presents itself before us now,but our backs were already turned on the potent weapon we had with us.As I wrote in my s.68 article a few weeks earlier[https://itatonline.org/digest/articles/section-68-source-of-source-a-layered-controversy/]some robust and informed arguing in ITAT and Higher Courts would have carried the day but we have ,as Revenue,not only queered the pitch by the memorandum faux pa of arguable prospectivity but have also arguably denied ourselves a shot at correcting **the earlier perverse decisions of Tribunals** and garnering revenue lost.

6.1 One such lost case was **Aristo Pharmaceuticals (P.) Ltd. [2019] 107 taxmann.com 119 (Mumbai - Trib.) which I happened to argue as CIT D.R. for revenue way back in 2019.** It was observed that MCI regulations relating to professional conduct of registered medical practitioners would only cover individual medical practitioners and not pharmaceutical companies or allied health sector industries - Whether therefore, assessee would be duly entitled for claim of sales promotion expenses incurred on distribution of articles to stockists, distributors, dealers, customers and doctors - Held, yes

The decision rode on allegedly its own case for AY 11-12 ,which in turn rode on PHL] and all decisions cited by me which were quoted approvingly in many decisions later and earlier were rendered hors de combat[Refer para 26 of said decision].

6.1.1 I am not aware of any attempt made by IT Department at Mumbai to highlight the perversity of decision in Aristo before the hon'ble HC to the best of my knowledge and in the process the superior wisdom of a HC[353 ITR 388] was ignored in the name of co ordinate bench when ironically other coordinate benches supported revenue as well.This ASPECT should have been taken up by the revenue before the higher court even if an appeal had been filed.

6.1.2 See how the ITAT brushed aside the cited H.C.citing earlier decision:

> **[QUOTE] ''26……(*iii*) *Confederation of Indian Pharmaceutical Industry (SSI)* v. *The Central Board of Direct Taxes* (CWP No. 10793 of 2012, dated 26.12.2012)(HP):**
>
> *We find that the aforesaid judgment of the Hon'ble High Court of Himachal Pradesh was considered by the ITAT, Mumbai Bench "C", Mumbai in the case of DCIT-8(2), Mumbai v. PHL Pharma (P.) Ltd.*
>
> *The Tribunal after considering the aforesaid judgment had observed that as held by the High Court, if the assessee was able to establish that the MCI regulation was not applicable to the assessee, then the same could not be blindly applied in its case……''*[UNQUOTE]

6.1.3 The lines ,most respectfully ,were taken and quoted partially and totally out of context both in Aristo and in PHL(PARA 4 AND 11 of the latter].Here is the actual full paragraph from the H.C. order:

*'' **3.** Shri Vishal Mohan, Advocate, on behalf of the legally unsustainable reasoning the CBDT appeals under the Income-tax Act **but the circular which is totally in line with Section 37(1) cannot be said to be illegal. In fact paragraph 4 of the circular quoted hereinabove itself clarifies that the value of the freebies enjoyed by the medical practitioner is also taxable as business income or income from other sources depending on the facts of each case.** Therefore, **if the assessee satisfies the assessing authority** that the expenditure is not in violation of the regulations framed by the medical council then it may legitimately claim a deduction, but it is for the assessee to satisfy the assessing officer that the expense is not in violation of the Medical Council Regulations referred to above.*

***4.** We, therefore, find no merit in the petition, which is accordingly rejected. No costs."*

This gives a totally different colour to the chosen lines.

6.1.4 This decision was followed and more damage was done to revenue in **Medley Pharmaceuticals Ltd.[2020] 118 taxmann.com 44 (Mumbai - Trib.)**

6.1.5If this part quoting is justice I would say a sterling job was done by the decision in Aristo.In **UNION OF INDIA & ORS. Vs DHANWANTI DEVI & ORS.(*1996*) *6 SCC 44*** the hon'ble SC deprecated this kind of quoting out of context by observing that "It would, therefore, be not profitable to extract a sentence here and there from the judgment and to build upon it because the essence of the decision is its ratio and not every observation found therein." In the case of ***CIT* v. *Sun Engg. Works (P.) Ltd.*** **[1992] 198 ITR 227(SC)** it was held that **"the courts must carefully try to ascertain the true principle laid down by the decision of this Court and not to pick out words and sentences from the judgment, divorced from the context of the questions under consideration by this Court, to support their reasonings**. . . ." (p. 320)

6.1.6 Further:

Lets see the basis of the conclusion in Aristo(13-14):

9. We have heard both the parties, perused the material available on record and gone through the orders of authorities below. The issue involved in the present appeal, *i.e.* whether freebies distributed to medical professionals by a pharmaceutical company is allowable u/s 37(1) of the Act or not in light of circular issued by MCI was **subject matter of deliberations by the co-ordinate bench of ITAT, Mumbai Bench "A" in assessee's own case for A.Y. 2011-12.** The co-ordinate bench, after considering various aspects including the circular issued by MCI and also circular of CBDT *vide* circular No.5 of 2012 held that the assessee was entitled for claim of sales promotion expenses incurred on distribution of articles to the stockists, distributors, dealers and doctors. **The relevant findings of the Tribunal are as under:—....**

10. In this view of the matter and consistent with view **taken by the co-ordinate bench in assessee's own case for A.Y. 2011-12,** we are of the considered view that there is no error in the findings recorded by the Ld.CIT(A) insofar as deletion of addition made by the AO towards sales promotion expenses and hence, we are inclined to uphold the findings of the Ld.CIT(A) and dismiss the appeal filed by the revenue."

It went on to quote extensively paras 21 to 25 of said decision of AY 11-12 which interalia also included extensive quoting from PHL and later cited(reason not seen) para 26-34 which pertained to AY 2012-13.I note with deepest shock the para 25 of said AY 2011-12 ORDER which is totally alien to the relief in AY 2013-14.Students of law must explicitly note the point as a huge aid in understanding perversity in application of alleged precedents which are not even precedents.

[cited from Aristo order for AY 2013-14 which is citing AY 11-12 ORDER]

QUOTE

''25. We thus, in the backdrop of the aforesaid settled position of law as regards the prospective applicability of an oppressive circular, are of the considered view that as the **CBDT as per its Circular No. 5/2012, dated 01.08.2012 had enlarged the scope of Indian Medical Council Regulation, 2002, and had made the same applicable to the pharmaceutical companies, thus the same cannot be reckoned to have a retrospective effect.** We find that a coordinate bench of the Tribunal viz. ITAT, Mumbai in the case of

Syncom Formulations (I) Ltd. v. *DCIT*-8(3), Mumbai (ITA No. 6428 & 6429/Mum/2012, dated 23.12.2015) for A.Ys 2010-11 and 2011-12 had concluded that the aforesaid CBDT Circular No. 5/2012, dated 01.08.2012 would not be applicable to the A.Ys 2010-11 and 2011-12, as the same was introduced w.e.f. 01.08.2012. **We thus, in terms of our aforesaid observations are of the considered view that the aforementioned CBDT Circular No. 5/2012, dated 01.08.2012 would not be applicable to the case of the assessee before us for A.Y. 2011-12."**

UNQUOTE

It is clear as day that mere retrospectivity was ruled upon as basis of decision.Please see again: ''CBDT as per its Circular No. 5/2012, dated 01.08.2012 had enlarged the scope of Indian Medical Council Regulation, 2002, and had made the same applicable to the pharmaceutical companies, thus the same cannot be reckoned to have a retrospective effect. .....We thus, in terms of our aforesaid observations are of the considered view that the aforementioned CBDT Circular No. 5/2012, dated 01.08.2012 **would not be applicable to the case of the assessee before us for A.Y. 2011-12.**"

''WOULD NOT BE APPLICABLE FOR AY 2011-12".Is this a precedent?Shocking.

Further it was said that reliance is placed on ITA 5553 AND 5167 decision for AY 2011-12.So the citing of ITA No. 5479 & 5747/Mum/2015 A.Y. 2012-13 later on in the order is of zero relevance.See the para 10 of the order (supra) wherein it is clearly mentioned that **AY 2011-12 IS BEING FOLLOWED.**

Did revenue take note of this?Or did it leave it for a retired IRS officer to indicate it?

6.1.7 And even in 2012-13 the astonishing finding is that though the circular is in operation,it can't be followed because it enlarges the scope of MCI guidelines without sanction of law/creates casus omissus!!

See the finding as cited by Aristo in 2013-14 order:

"**33.** That both the assessee and the revenue being aggrieved with the order of the CIT(A) has carried the matter by way of cross appeals before us. We find that the issue involved in the present case *viz*. disallowance of sales promotion expenditure remains the same, as was there before us in the assesses own case for the immediately preceding year *viz*. A.Y. 2011-12 as had been adjudicated by us hereinabove, except for the fact that in the present case the CBDT Circular No. 5/2012, dated 01.08.2012 **had came into force during the year** under consideration. **Be that as it may,** we are of the considered view that as deliberated by us at length hereinabove, the aforementioned **CBDT Circular No. 5/2012, dated 01.08.2012 had enlarged the scope of MCI regulations** and made the same applicable to the pharmaceutical companies, without any enabling provision either under the Income Tax Act or the Indian Medical Council Regulations. **We are of the considered view that as observed by us hereinabove, the CBDT by extending the scope and gamut of the MCI Regulation had by so doing traversed beyond the scope of its jurisdiction and provided casus omissus to the regulation issued by MCI, which though had not been expressly provided therein. We thus, being of the view that as the CBDT is divested of its power to create a new impairment adverse to an assessee or to a class of assessee without any sanction or authority of law, therefore, are unable to persuade ourselves to subscribe to the rigours contemplated as regards the pharmaceutical companies or the allied healthcare sector in the CBDT Circular No. 5/2012, dated 01.08.2012……..** "

So in 2011-12 it is not operational hence relief to assessee and in 2012-13 its operational but ultra vires ,hence relief to assessee.Fantastic!

6.1.8 And furthermore,in terms of HP HC order **the AO** had to be satisfied.Does that include ITAT?And if it does,pray how did it get satisfied? Truth is ,it perpetuated a legal perversity .It was not a case of discretionary interpretation.Because none existed.Did the Revenue see this?A travesty and a tragedy which shall go undocumented in recorded legal litigation history.

6.1.9 Not only this ,by a fantastic reasoning in AY 2012-13 in Aristo(as cited in AY 13-14 ORDER)it was held that the CBDT circular unduly enlarged the scope of MCI regulations and that it amounted to supplying a casus omissus!" ***"the CBDT cannot provide casus omissus to a statute or notification or any regulation which has not been expressly provided therein"***. It was held that "**CBDT had enlarged the scope and applicability of Indian Medical Council Regulation, 2002**"**!**

6.1.10 I must admit a deficiency in my legal instruction because casus omissus IS A JUDICIAL PRESERVE.It can't be applied either way to CBDT. **When a statute undertakes to foresee and to provide for certain contingencies, and a case remains to be provided for, it is said to be a casus omissus**.A guideline does not have a force of the statute.How could CBDT supply a casus omissus to a guideline as held in Aristo?

6.1.11 Further **the ruling is in direct contempt** of HP HC ruling(supra) which had upheld the legality of the circular.It is a popular misconception that non jurisdictional HCs only carry a persuasive force.If jurisdictional HC and SC are silent then it becomes binding.A non jurisdictional HC

prevails over a co ordinate bench of same jurisdiction.[The Tribunals like in Aristo in fact disregarded their own jurisdictional HC decision in **CIT *v.* Smt. Godavaridevi Saraf[1978] 113 ITR 589 (BOM.)which held** that" It should not be overlooked that the Income-tax Act is an All-India statute and if an Income-tax Tribunal in Madras, in view of the decision of the Madras High Court, has to proceed on the footing that section 140A(3) was non-existent, the order of penalty there under cannot be imposed by the authority under the Act. **Until a contrary decision is given by any other competent High Court, which is binding on a Tribunal in the State of Bombay, it has to proceed on the footing that the law declared by the High Court, though of another State, is the final law of the land.**"

6.1.12 This was reiterated in **TEJ INTERNATIONAL (P.) LTD.V. DCIT[2001] 118 TAXMAN 59 (DELHI) (MAG.)**which said that" In the hierarchical judicial system that we have, better wisdom of the Court below has to yield to higher wisdom of the Court above and, therefore, once a authority higher than this Tribunal has expressed an opinion on that issue, we are no longer at liberty to rely upon earlier decisions of this Tribunal even if we were a party to them. **Such a High Court being a non-jurisdictional High Court does not alter the position as laid down by Hon'ble Bombay High Court in the matter of *CIT* v. *Godavari Devi Saraf* [1978] 113 ITR 589 (Bom.). Therefore, we do not consider it permissible to rely upon the earlier decisions of this Tribunal even if one of them is by a Special Bench."**

6.1.13 This was reiterated further in **Kaybee (P.) Ltd. *v.ITO*[2020] 121 taxmann.com 277 (Mumbai - Trib.).However** there a request for forming special bench was refused stating that **non jurisdictional HC SHALL BIND EVEN SPECIAL BENCH** till we had jurisdictional HC view.(para 16

of it).**In Macleod ,in same Mumbai Tribunal** ,even in view of clear precedence of HP HC ,in virtually identical circumstances , referred the matter for forming a larger bench!!And it found justification for so doing by holding that *''while we may or may not agree with a coordinate bench decision, it cannot be open to us to disregard the same, lest such judicial inconsistency should shake public confidence in the administration of justice and lest one of the fundamental legitimate expectations of the stakeholders, i.e. those exercising judicial functions will follow the reason or ground of the judicial decision in the earlier cases on identical matters, will stand declined".*This is like running with the hare and hunting with the hound*!*Most respectfully ,public confidence is more shaken by perpetuating an error while clearly acknowledging the error and in not following its own earlier decision on selfsame subject matter rendered an year earlier. **In Distributors (Baroda) (P) Ltd. vs. Union of India (1985) 47 CTR (SC) 349 : (1985) 155 ITR 120 (SC), had observed thus :**"To perpetuate an error is no heroism. To rectify it is the compulsion of judicial conscience."

But even in referring the issue to a larger bench Mcleod perpetuated the error by not framing a categorical order as laudably done by Jabalpur bench,ignoring its own earlier order in **M/s J.P. Tobacco Products Pvt. Ltd.,Vs.A.C.I.T., ITA No.84/Jab/10 Assessment Year: 2007-08.An argument can be raised that HP decision was at least considered by these benches but arguably misread/misapplied .If there was a misreading of HP HC decision the ITAT had an opportunity of giving a contrary ruling as done in PLAZA INVESTMENTS (P) LTD. vs. ITO(2006)104 TTJ 98/108 ITD 239(MUM) which again was not done.**

So Macleod is not the unmixed blessing as the Memorandum makes it out to be as ,respectfully ,it ignored its own earlier decisions.

6.1.14 The contrary ITAT orders ,most respectfully are in contempt of the Bombay H.C. ruling(Godavari Devi,supra).Not only this ,in giving CBDT circular status of a statute ,assuming the elevation to be correct ,these decisions are also in contempt of hon'ble S.C.in questioning the vires of the very statute which created it: ***K.S. Venkataraman and Co. (P.) Ltd.* v. *State of Madras*** **[1966] 60 ITR 112; 17 STC 418: "an authority created by a statute cannot question the vires of that statute or any of the provisions thereof where under it functions."**

6.1.15 A Tribunal most respectfully does not have the status of a Court. **CIT *v.*1. ECOM GILL COFFEE TRADING P. LTD. 2. B. FOURESS P. LTD. [2014] 362 ITR 204 (Kar)held that** *"The Income-tax Appellate Tribunal is not an authority akin to a court but is a special Tribunal with limited jurisdiction as indicated in the statutory provisions."***In CIT VS Smt. Meera Devi* [2012] 26 taxmann.com 132 (Delhi)it was held that** *"The Court is also aware that the* ***Tribunal is a quasi-judicial authority, and is not a court of record.*** *There are* ***important exceptions to the doctrine of precedent, which reinforce the public interest in proper administration of justice.*** *The first is that a decision is an authority for what it says, in the context of the facts. The second is that if the previous decision is per incuriam, the Tribunal, or court is not bound to consider it as a binding precedent."*

6.1.16 The hon'ble SC IN Apex labs judgment discussed later held that *"This Court is of the opinion that such a narrow interpretation of Explanation 1 to Section 37(1) defeats the purpose for which it was inserted, i.e., to disallow an*

assessee from claiming a tax benefit for its participation in an illegal activity. Though the memorandum to the Finance Bill, 1998 elucidated the ambit of Explanation 1 to include "protection money, extortion, hafta, bribes, etc.", ***yet, ipso facto, by no means is the embargo envisaged restricted to those examples. It is but logical that when acceptance of freebies is punishable by the MCI*** *(the range of penalties and sanction extending to ban imposed on the medical practitioner),* ***pharmaceutical companies cannot be granted the tax benefit for providing such freebies,*** *and thereby (actively and with full knowledge) enabling the commission of the act which attracts such opprobrium.*

The illogicality and completely misconceived nature of such an interpretation *was dealt with in a similar interpretation of the provisions of PC Act, by a Constitution Bench of this Court…"*

It was a gross miscarriage of justice in decisions initated in PHL and taken to unprecedented heights by decisions like Aristo.

6.1.17 It is very well to say that the circular merely refers to the MCI guidelines and thereafter holds that the freebies given are covered as ''prohibited by law".The Board is not enlarging the scope of MCI but is defining what shall be included as ''prohibited by law".The charge of violating legislative mandate can arguably be made-but to say it is so on grounds of a casus omissus is astonishing.CBDT was not ruling on MCI guidelines .It was clarifying on scope of ''prohibited by law".It has no powers to legislate.

6.1.18 Not just this ,to cover further base WHY WAS RETROSPECTIVITY PARA CITED in 13-14 order? *''24. Alternatively, we are of the considered view*

that it is a trite law that a CBDT Circular which creates a burden or liability or imposes a new kind of imparity, cannot be reckoned retrospectively."

Now this circular is dated 1.8.2012.We are in AY 2013-14.How and where did the retrospectivity come into?[I tried to decipher why.It is because in PHL it was so said!!But there the AY was 2010-11.In own case again AY was 2011-12.How was this quoting and following relevant to Aristo in 2013-14?]

And which is this trite law?It is merely a arguable proposition for amendments and insertions in statutes.Is it applicable to s. 119 circulars?

6.1.19 What is this circular making power?It is enshrined in s **119** (1) which says that ‘*"The Board may, from time to time, issue such orders, instructions and directions to other income-tax authorities as it may deem fit for the proper administration of this Act, and such authorities and all other persons employed in the execution of this Act shall observe and follow such orders, instructions and directions of the Board :"*

Does this include power to legislate so as to bring charges of casus omissus and retrospectivity? In Apex Labs ,as we shall see,the hon'ble Court as early as in para 2 said that the circular merely clarifies.Also in that case the AY involved was AY 2010-11.!Here it was 2013-14.

Take your pick.

6.2 And now that the Apex Court decision has come all these legally perverse decisions should be a simple matter of a 254(2) for therein would lie the biggest victory for revenue and some just reward for the back breaking and spirit breaking unrecognized work of the DRs for revenue.

7.THE RULING IN APEX LABS: SLP (CIVIL) NO. 23207 OF 2019)

M/s Apex Laboratories Pvt. Ltd. Vs DCIT decided on 22.2.2022

Analysis and Conclusions part of the decision

a.Analysis of s 37:

'17……'Section 37 is a residuary provision. Any business or professional expenditure which does not ordinarily fall under Sections 30-36, and which are not in the nature of capital expenditure or personal expenses, can claim the benefit of this exemption. But the same is not absolute. Explanation 1, which was inserted in 1998 with retrospective effect from 01.04.1962, restricts the application of such exemption for "any purpose which is an offence or which is prohibited by law". The IT Act does not provide a definition for these terms. Section 2(38) of the General Clauses Act, 1897 defines 'offence' as "any act or omission made punishable by any law for the time being in force". Under the IPC, Section 40 defines it as "a thing punishable by this Code", read with Section 43 which defines 'illegal' as being applicable to "everything which is an offence or which is prohibited by law, or which furnishes ground for a civil action". It is therefore clear that Explanation 1 contains within its ambit all such activities which are illegal/prohibited by law and/or punishable."

b. Regulation 6.8. of the 2002 Regulations was stated.

c.The CBDT circular dated 01.08.2012 was set out.

It was then observed:

"The CBDT circular being clarificatory in nature, was in effect from the date of implementation of Regulation 6.8 of the 2002 Regulations, i.e., from 14.12.2009."(sic.The actual date is 10.12.2009).

d.The Court then referred PHL Pharma decision in detail.

THE FINAL RULING:KEY PARAS-

[QUOTE]''22. This Court is of the opinion that such a narrow interpretation of Explanation 1 to Section 37(1) defeats the purpose for which it was inserted, i.e., to disallow an assessee from claiming a tax benefit for its participation in an illegal activity. Though the memorandum to the Finance Bill, 1998 elucidated the ambit of Explanation 1 to include "*protection money, extortion, hafta, bribes, etc.*", **yet, *ipso facto*, by no means is the embargo envisaged restricted to those examples. It is but logical that when *acceptance* of freebies is punishable by the MCI (the range of penalties and sanction extending to ban imposed on the medical practitioner), pharmaceutical companies cannot be granted the tax benefit for providing such freebies, and thereby (actively and with full knowledge) *enabling* the commission of the act which attracts such opprobrium.**

23. **The illogicality and completely misconceived nature of such an interpretation** was dealt with in a similar interpretation of the provisions of PC Act, by a Constitution Bench of this Court in *P.V. Narasimha Rao v. State (CBI/SPE)*21.[(1998) 4 SCC 626.]……..

24. Even if Apex's contention were to be accepted - that it did not indulge in any illegal activity by committing an offence, as there was no corresponding penal provision in the 2002 Regulations applicable to it - **there is no doubt that its actions fell within the purview of "*prohibited by law*" in Explanation 1 to Section 37(1).**

25. Furthermore, if the statutory limitations imposed by the 2002 Regulations are kept in mind, Explanation (1) to Section 37(1) of the IT Act and the insertion of Section 20A of the Medical Council Act, 195623 (which serves as parent provision for the regulations), what is discernible is that **the statutory regime**

requiring that a thing be done in a certain manner, also implies (even in the absence of any express terms), that the other forms of doing it are impermissible……..

27. **It is also a settled principle of law that no court will lend its aid to a party that roots its cause of action in an immoral or illegal act *(ex dolo malo non oritur action)*** meaning that none should be allowed to profit from any wrongdoing coupled with the fact that statutory regimes should be coherent and not self-defeating. Doctors and pharmacists being complementary and supplementary to each other in the medical profession, a comprehensive view must be adopted to regulate their conduct in view of the contemporary statutory regimes and regulations. Therefore, denial of the tax benefit cannot be construed as penalizing the assessee pharmaceutical company. Only its participation in what is plainly an action prohibited by law, precludes the assessee from claiming it as a deductible expenditure.

28. **This Court also notices that medical practitioners have a quasi-fiduciary relationship with their patients. A doctor's prescription is considered the final word on the medication to be availed by the patient, even if the cost of such medication is unaffordable or barely within the economic reach of the patient – such is the level of trust reposed in doctors. Therefore, it is a matter of great public importance and concern, when it is demonstrated that a doctor's prescription can be manipulated, and driven by the motive to avail the freebies offered to them by pharmaceutical companies, ranging from gifts such as gold coins, fridges and LCD TVs to funding international trips for vacations or to attend medical conferences. These freebies are technically not 'free' – the cost of supplying such freebies is usually factored into the drug, driving prices up, thus creating a perpetual publicly injurious cycle. The threat of prescribing medication that is significantly marked up,**

over effective generic counterparts in lieu of such a *quid pro quo* exchange was taken cognizance of by the Parliamentary Standing Committee on Health and Family Welfare……[45th Report on Issues Relating to Availability of Generic, Generic-Branded and Branded Medicines, their Formulation and Therapeutic Efficacy and Effectiveness), dated 04.08.2010.]…….

29. **The impugned judgment, along with the judgments of Punjab & Haryana High Court (*Kap Scan*) and Himachal Pradesh High Court (*Confederation*) (supra) have correctly addressed the important public policy issue** on the subject of allowance of benefit for supply of freebies. The impugned judgment's reasoning is quoted as follows:

"A perusal of the decision of Co-ordinate Bench of this Tribunal in the assessee's own case as also the decision of the Hon'ble Himachal Pradesh High Court clearly shows that the basic intention of the decision was that the receiving of the gifts/freebies by Professionals is against public policy as also against the law in so far as the amendment by the Medical Council Act, 1956 to the Indian Medical Council (Professional Conduct, Etiquette and Ethics) Regulations, 2002, once receiving of such gifts have been held to be unethical obviously the corollary to this would also be unethical, being giving of such gifts or doing such acts to induce such Doctors and Medical Professionals to violate the Medical Council Act, 1956."

(emphasis supplied)

30. Thus, one arm of the law cannot be utilised to defeat the other arm of law – doing so would be opposed to public policy and bring the law into ridicule.29 In ***Maddi Venkataraman & Co. (P) Ltd. v. CIT*** ([1998) 2 SCC 95]. , a fine imposed on the assessee under the Foreign Exchange Regulation Act, 1947 was sought to be deducted as a business expenditure. This Court held:

*"Moreover**, it will be against public policy to allow the benefit of deduction under one statute, of any expenditure incurred in violation of the provisions of another statute or any penalty imposed under another statute.** In the instant case, if the deductions claimed are allowed, the penal provisions of FERA will become meaningless".*

(emphasis supplied)

31. It is crucial to note that **the agreement between the pharmaceutical companies and the medical practitioners in gifting freebies for boosting sales of prescription drugs** is also violative of Section 23 of the Contract Act, 1872 (as also noted by the Punjab and Haryana High Court in *Kap Scan* (supra))……..

33. Thus, pharmaceutical companies' gifting freebies to doctors, etc. is clearly "*prohibited by law*", and not allowed to be claimed as a deduction under Section 37(1). Doing so would wholly **undermine public policy.** ……

36. In the present case too, the incentives (or "freebies") given by Apex, to the doctors, had a direct result of exposing the recipients to the odium of sanctions, leading to a ban on their practice of medicine. Those sanctions are mandated by law, as they are embodied in the code of conduct and ethics, which are normative, and have legally binding effect. The conceded participation of the assessee- i.e., the provider or donor- was plainly prohibited, as far as their receipt by the medical practitioners was concerned. That medical practitioners were forbidden from accepting such gifts, or "freebies" was no less a prohibition on the part of their giver, or donor, i.e., Apex.

37. In view of the foregoing discussion, the impugned judgment cannot be faulted with. The appeal is dismissed without order on costs. Pending application(s), if any, also stand disposed of.

[UNQUOTE]

7.1 There we have it.Plain and clear interpretation of the Explanation ,prior to insertion of the unnecessary amendment clarifying what is part of the statute. *In* **Union of India v. Deoki Nandan Agarwal HON'BLE** *court observed that "The Court cannot rewrite, recast or reframe the legislation for the very good reason that it has no power to legislate. The power to legislate has not been conferred on the courts… Courts shall decide what the law is and not what it should be."*

This is the widely accepted Declaratory Theory of Jurisprudence.

All this undue complication created by an amazingly inept Revenue as witnessed by the Memorandum,the forgotten aspect of retrospectivity,ignoring sterling judicial precedents,ignoring even their own insertion of Memorandum to original Explanation could have been well avoided.The path to salvation still remains as indicated in paras above.Let's see if they are imaginative and courageous enough to get the earlier perverse rulings of Tribunals overturned armed with both,the amendment and the ruling.

8.DEFINITIONAL IRRITANTS REMAIN.WHAT ARE "RULES","REGULATIONS" AND "GUIDELINES"?

The hon'ble S.C. too in Apex Labs noted absence of certain definitions and took to G.C.Act to explain them.But still definitional imbroglios remain in regard to these three terms.Let us attempt an understanding.*We need to find interpretational aids and thus we look at General Clauses Act, 1897 first*

to understand "Rules"."Regulations","Guidelines". [The purpose of the General Clauses Act is to place in one single statute different provisions as regards interpretation of words and legal principles which would otherwise have to be specified separately in many different Acts and Regulations.It aims to provide, as far as possible, for uniformity of expression in Central Acts, by giving definitions of a series of terms in common use. The General Clauses Act functions as one of the statutory aids of interpretation.It stipulates in s 3 that" *In this Act, and in all Central Acts and regulations made after the commencement of this Act, unless there is anything repugnant in the subject or context-.....".*]

]

3(51) "rule" shall** mean a rule made in exercise of a power conferred by any **enactment,** and shall include a Regulation made as a rule under any **enactment

[(19) **"enactment"** shall include a regulation (as hereinafter defined) and any regulation of the Bengal, Madras or Bombay Code, and shall also include any provision contained in any Act or in any such regulation as aforesaid;]

(50) **"Regulation"** shall mean a Regulation made by the President 7[under article 240 of the Constitution and shall include a Regulation made by the President under article 243 thereof and] a regulation made by the Central Government under the Government of India Act, 1870, or the Government of India Act, 1915, or the Government of India Act, 1935;

Now this creates a big difficulty.Because the 1935 Act stands repealed by Article 395 of the Constitution.Earlier ones even more so.Where then,is the enabler?This may cause litigation issues.If we then look at other aids to interpretation ,Black's law dictionary helps us .There

REGULATION. *The act of regulating; a rule or order prescribed for management or government; a regulating principle; a precept. Curless v. Watson, 180 Ind. 86, 102 N.E. 497, 499. Rule of order prescribed by superior or competent authority relating to action of those under its control. State v. Miller, 33 N.M. 116, 263 P. 510, 513.*

For Rule also ,we can take help of Black's:

RULE, *n. An established standard, guide, or regulation; a principle or regulation set up by authority, prescribing or directing action or forbearance; as, the rules of a legislative body, of a company, court, public office, of the law, of ethics. A regulation made by a court of justice or public office with reference to the conduct of business therein.*
An order made by a court, at the instance of one of the parties to a suit, commanding a ministerial officer, or the opposite party, to do some act, or to show cause why some act should not be_ done. It is usually upon some interlocutory matter, and has not the force or solemnity of a decree or judgment.

Guideline is not defined in either of these two."**Law insider"provides valuable insight.**

Guideline *means a set of statements by which to determine a course of action. It* ***means a*** ***document issued by a regulatory agency with respect to a matter within its authority, which sets out recommended procedures, standards or forms reflecting that regulatory agency's advice as to what constitutes best practice on a matter.*** *By definition, following a guideline is never mandatory.It* ***is a*** *set of optional directions that provide guidance, advice or explanation to support the implementation of a policy or procedure.*

EU recognizes a guideline as a Soft law instrument and referred as *"rules of conduct which, in principle, have no legally binding force but which nevertheless may have practical effects".*

These concepts shall bring their unique litigational potential on the table in time to come.

9.The best course for Revenue is either to withdraw the amendment,else to ensure that all past legally perverse orders of Tribunals are rendered inoperative by virtue of Apex labs and embedded retrospectivity of the amendment ,their own self goal notwithstanding.An interesting scenario lies ahead of us.

Anadi Varma