Direct Tax Vista

Your weekly Direct Tax recap

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By Vivek Jalan, Partner, Tax Connect Advisory Services LLP

1. MAT Credit to be allowed on the basis of Form 29B

Simple matters should be kept simple. Sometimes it is made complicated when argued incorrectly or understood with a presumption. The claim of assessee in respect of MAT credit pertaining to a prior year can simply be proved with a Form 29B of a Chartered Accountant wherein there is a space for disclosure of "Income Tax payable as per normal provisions" and "tax payable as per MAT provisions", as follows –

6.	Total income of the company under the Act.	
7.	Income-tax payable on total income.	
8.	...	
9.	...	
10.	...	
11.	...	
12.	...	
13.	...	
14.	...	
15.	...	
16.	...	
17.	...	
18.	Book profit as computed according to *Explanation 1* given in sub-section (2) read with sub-sections (2A), (2B) and (2C) (total of Sl. No. 11 to 17).	
19.	18.5 per cent of "book-profit" as computed in Sl. No. 18.	

The difference is MAT Credit entitlement. If this form is filed and even if the correct disclosures are not made in the Income Tax return, then the officers should merely

rely on the submissions, the Form 29B and Form 26AS of the relevant AY, so as to not deny MAT Credit entitlement. The very fact that this matter travelled to the ITAT is reflective of the legal tangle in which it got engulfed in.

Notwithstanding, the Hon'ble ITAT Kolkata ('A' Bench) in an elaborate judgement in the case of The Jute Corporation of India Ltd. Vs Deputy Commissioner of Income Tax, Circle-1(2), Kolkata on 28th November 2023, found it proper to remit the matter on this issue back to the file of AO to verify the records in respect of claim of MAT credit and allow the same in accordance with the provisions of law with a direction that the assessee be given reasonable opportunity of being heard and to furnish all the relevant documentary evidence in support of its claim.

2. Penalty is allowed if it is compensatory and teaches the assessee how to run its business in future... It is disallowed if it is a punishment for intentional violation of a law

The question asked many times is whether all penalties are disallowed under the Income tax Law as being expenses made for violations of a law. Prior to Explanation 1 of Sec 37 of The Income Tax Act, there were a catena of decisions dealing with the allowability of expenditure u/s 37, whether illegal or not, treated on a case by case basis. One principle to note which seems to be present right from pre-amendment days is that if the amounts paid were compensatory in nature, they were allowable. If they were penal in nature, it wasn't to be allowed.

The Department wanted to enshrine in law that illegal expenditure cannot be a deduction under the ambit of Income Tax. Thus Explanation 1 was inserted by the amendment by Finance Act, 1998 and was given retrospective effect from April 1 1962. The legislative intent behind the insertion of this explanation as given in memorandum of Finance Bill 1998 being as follows:

"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

payment on account of protection money, extortion, hafta, bribes, etc. as business expenditure."

Further, the CBDT clarified this position vide Circular 722 dated 23/12/1998 whose extract reads as follows: Section 37 of the Income-tax Act is amended to provide 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 purposes of business or profession and no deduction or allowance shall be made in respect of such expenditure. This amendment will result in disallowance of the claims made by certain assessees in respect of payments on account of protection money, extortion, hafta, bribes etc. as business expenditure. It is well decided that unlawful expenditure is not an allowable deduction in computation of income.

In this backdrop, the issue in the case of AMALSAD VIBHAG KELVANI MANDAL Vs I.T.O [2023-VIL-1600-ITAT-SRT] was whether the penalty paid for violation of provision of Foreign Contribution (Regulation) Act, 2010 is allowable as a deduction under Income Tax Act.

The assessee's contention was that the penalty was levied on acceptance of foreign donation. Such donation was received in earlier years for building fund. Such penalty was paid as the assessee was not having permission of Ministry of Home Affairs to receive such funds. Further, the penalty was not paid for any offence rather it was paid for regularization of fund received from foreign remittance. Hence such incurring such expenses provided an understanding to the assessee as to how to deal with such compliances in future. Hence the expenses were claimed as educational expenses i.e. capital in nature and were compensatory in nature.

The argument was accepted and hence the point re-asserted is that penalty is allowed if it is compensatory in nature and disallowed if it is a punishment for intentional violation of a law.

3. CSR expenditure is allowable u/s 80G of The Income Tax Act – On the maxim of 'Expressio Unius Esl Exclusio Alterius'

Allowability of CSR expenditure has been sealed after Explanation 2 to Section 37(1) was inserted in the Income tax Act 1961 w.e.f. 1.4.2015. It reads as -

> "Explanation 2- For the removal of doubts, it is hereby declared that for the purposes of sub-section (1), any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 (18 of 2013) shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession."

Explanation-2 to section 37(1) of the Act thus denies deduction for CSR expenses by way of business expenditure and is applicable only to the extent of computing business income under Chapter IV-D and it could not be extended or imported to CSR contribution which was otherwise eligible for deduction under Chapter VI. Various ITAT and High Court decisions are available in this respect. The ITAT Mumbai in the case of SAVITA OIL TECHNOLOGIES LTD Vs ACIT, CENTRAL CIRCLE [2023-VIL-1595-ITAT-MUM] has again held in this regard on the following grounds –

A. The embargo created by this Explanation 2 inserted in Section 37 of the Act by the Finance (No.2) Act, 2014 was to deny deduction for CSR expenses incurred by companies, as and by way of regular business expenditure while computing "Income under the head Business. So, it can be clearly seen that this Explanation 2 to Section 37(1) of the Act which denies deduction for CSR expenses by way of business expenditure is applicable only to the extent of computing 'Business Income' under Chapter IV-D of the Act.

B. The Court relied on the interpretation maxim "**Expressio Unius Esl Exclusio Alterius**" which is a Latin phrase that means "express mention of one thing excludes all others. The phrase indicates that items not on the list are assumed not to be covered by the Statute. When something is mentioned expressly in a Statute, it leads to the presumption that the things not mentioned are excluded. Even if the assessee has included the expenditure as CSR Expenditure because there is no prohibition or restriction placed by

the Parliament on such a donation even if shown as CSR expenditure. The reason for saying so is that in section 80G of the Act certain restrictions in respect of deduction in respect of two donations are expressly seen in this Section. So the Parliament has expressed its intention clearly by bringing in restriction in respect of expenditure classified by an assessee company while claiming deduction u/s. 80G of the Act i.e. CSR expenditure related to Swachh Bharat Kosh and Clean Ganga Fund. So if an assessee makes some donation to these projects and include/classify it as CSR expenditure while claiming deduction u/s. 80G of the Act then it will be allowed only the amount that is other than the sums spent by the assessee in pursuance of CSR u/s. 135 of the Companies Act.

In other words, if an assessee company spends only the mandatory expenditure of 2% of net profit for CSR activity, which includes the amount of donation to Swach Bharat Kosh & Clean Ganga Fund (iiihk) and (iiihi) of clause (a) of subsection (2) of section 80G of the Act, then deduction u/s. 80G of the Act is not allowable. However, in a case scenario, wherein the assessee expends the mandatory expenditure and gives donation to these two projects i.e. over and above the mandatory CSR expenditure u/s. 135 of Companies Act, that sum donated to Swach Bharat Kosh & Clean Ganga Fund will be eligible for 100% deduction u/s. 80G of the Act [refer section 80G (1)(i) and subject to section 80G (4)]. However, such a restriction in respect of expenditure made by an assessee to any other fund or institution as referred to in sub clause (iv) of clause (a) of sub-section 2 of section 80G of the Act had not been placed by the Legislature. If the Parliament desired, it could have been made such kind of restriction or any restriction like in the case of donation to Swach Bharat Kosh & Clean Ganga Fund.

4. If exempt income is offered to tax, no disallowance can be made for the corresponding expenditure

From a combined reading of Section 14A and Rule 8D of The Income Tax Law, the inescapable conclusion is that Rule 8D provides for allocation of expenditure relatable to exempt income and that such expenditure is to be disallowed even when there is actually no exempt income during the previous year as the Rule speaks of

"income from which does not or shall not form part of the total income", and the phrase 'shall not' here refers to the future income. This interpretation is further amplified by the use of the word "or between the phrase "does not' and 'shall not'. Hence where despite having dividend income, which is exempt from tax, the assessee does not claim exemption in respect of such income and offers the said income to taxation, the assessee cannot be subjected to disallowance in respect of the expenses relating to such income. That would amount to double taxation and impinge on the fundamental right of the appellant. In this view of the matter, no disallowance can be made u/s 14A was held in the case of DCIT, CENTRAL CIRCLE-6, NEW DELHI Vs SAHARA PRIME CITY LTD [2023-VIL-1594-ITAT-DEL]

5. CBDT Extends Time Limit to Process Refund Claimed ITRs for AYs 2018-19 to 2020-21 to January 31, 2024

In October the CBDT has granted a deadline extension until January 31, 2024, for processing electronically filed income returns with refund claims up to Assessment Year 2017-18. Now It has also noted technical issues or other non-attributable reasons causing the non-processing of validly filed income tax returns for AYs 2018-19 to 2020-21. As a result, taxpayers are experiencing delays in receiving legitimate refunds despite the delay not being their fault. Hence it has issued Order vide *F. No.225/132/2023/ITA-II dated December 01, 2023* regarding the processing of returns of income validly filed electronically with refund claims under section 143(1) of the Income-tax Act, 1961 ("the IT Act") beyond the prescribed time limits in non-scrutiny cases. However, this relaxation shall not be available to the following returns:

a) Returns selected in scrutiny,

b) Returns remain unprocessed, where either demand is shown as payable in the return or is likely to arise after processing it, and

c) Returns remain unprocessed for any reason attributable to the assessee.

6. Better accounting can help in better tax compliance

It is always advisable for Individuals to make their balance sheet and cash flow statements for better reflection on the computation of income and not make basic

accounting mistakes. Further the vouchers and invoices for business income should be present. Consider the following case –

A. An assessee is married and has two children
B. All household expenses are met by his father
C. The assessee has not debited any amount towards drawings for personal expenses in capital account
D. The assessee has claimed to have agricultural income with the following particulars-

i. He does not own any agricultural land.
ii. He could not produce any evidence to prove sale of agricultural produce and also proof of expenditure incurred for earning agricultural income

The above are issues which could be avoided by better accounting, in the absence of which the order was confirmed in the case of V. ARUMUGAPANDI Vs THE ASST. COMMISSIONER OF INCOME TAX [2023-VIL-1566-ITAT-CHE]

7. Sec 263 cannot be invoked without any analysis by the PCIT himself

It was held in the case of VOLKSWAGEN INDIA PRIVATE LIMITED Vs PCIT-4, PUNE [2023-VIL-1565-ITAT-PNE] that Sec 263 cannot be invoked merely on the request of AO and without any analysis by the PCIT satisfying himself that the revision/re-opening is required. In this case, AO wrote a letter to PCIT that assessment order passed for year under consideration did not properly deal with issue of taxability of subsidy from Government. On sole strength of this letter of AO, PCIT made up his mind and issued show cause notice seeking to revise assessment order without calling for and examining any record of proceeding for year under consideration and independently satisfying himself that assessment order required revision. Such satisfaction of PCIT is crucial and sine qua non and hence such revision cannot take-off.

8. Business Expenditures - to be allowed... but dis-allowed

Many a times certain expenses are disallowed by AOs in assessments wherein the jurisprudence is very clear. We list down some of them in our articles. Here are a few more –

Revenue expenditure consumed over a period of time – Held in the case of HINDUSTAN EPC COMPANY LTD Vs ACIT, CIRCLE-11(2), NEW DELHI [2023-VIL-1562-ITAT-DEL] that Facilitation/upfront fee on loan facilities taken from banks. For purpose of income tax, entire payment being incurred and paid during the year would become allowable, as long as loan borrowed is utilized for purpose of business.

Depreciation under Sections 32(1)(ii) on Payment of non-compete fees – Non-compete fee paid by assessee as a part of initial outlay on acquisition of business by assessee and is very much part of entire part of purchase of business by assessee to acquire right to carry on business unfettered by any competition which results in protection for business as a whole and will help appreciate the whole of capital assets. Such expenditure incurred towards payment of non-compete fees was held in the case of EATON POWER QUALITY PRIVATE LIMITED Vs THE DEPUTY COMMISSIONER OF INCOME TAX [2023-VIL-1560-ITAT-CHE], to be capital in nature and the assessee was entitled for depreciation under Section 32(1)(ii) of the Act. The same is not allowed u/s 37 as a general deduction.

Provision towards litigation and tax matters – Without any scientific working to estimate of provision for such expenditure, with complete details and explanation, the same may be disallowed.

Sponsorship expenses – Held in the case of DCIT CENTRAL CIRCLE-2(1) CHENNAI Vs M/s AGNI ESTATES & FOUNDATIONS PVT LTD [2023-VIL-1558-ITAT-CHE] that requirement of Section 37(1) of the Act is that expenditure is incurred wholly and exclusively for purposes of business. Where assessee pays sponsorship fees to carry out business promotional activities, Payment is backed by agreement and invoices and revenue has no material to doubt the same, sponsoree uses logo of assessee in

its promotional campaigns or advertisements and other such evidences are produced, such expenditure should be allowed.

9. Error Trade loss allowed for share brokers

The nature of business of share broking agencies are such that there are certain losses arising out of the purchase and sale of shares with an obligation of payments and delivery. Certain times the client does not accept the loss and therefore, brokers has to bear it by reversal of the trade. The issue raised is that the provisions of Section 73 of the Act hits it and loss is speculative. The decision of the Hon'ble Bombay High Court in 379 ITR 146 can be relied upon wherein such loss was considered non-speculative. The same was also upheld in the case of CITIGROUP GLOBAL MARKETS (INDIA) PRIVATE LIMITED Vs THE DCIT [2023-VIL-1579-ITAT-MUM].

(*The author is a CA, LL.M & LL.B and Partner at Tax Connect Advisory Services LLP. The views expressed are personal. The author is The Lead - Indirect Tax Core Group of CII-ER and The Chairman of The Fiscal Affairs Committee of The Bengal Chamber of Commerce. He has Authored more than 15 books on varied aspects of Direct and Indirect Taxation. E-mail - vivek.jalan@taxconnect.co.in*)