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* **IN THE HIGH COURT OF DELHI AT NEW DELHI**
+ **INCOME TAX APPEAL Nos. 625/2017, 636/2017,**
642/2017, 667/2017, 672/2017, 673/2017

Date of decision: 28th August, 2018

PR.COMMISSIONER OF INCOME TAX-6 Appellant
Through: Mr. Zoheb Hossain, Sr. Standing
Counsel with Mr. Deepak Anand, Jr.
Standing Counsel for Revenue.

versus

NATIONAL HOUSING BANK Respondent
Through: Mr. Rohit Jain and Mr. Aniket D.
Agarwal, Advocates.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE CHANDER SHEKHAR

SANJIV KHANNA, J. (ORAL):

These appeals by the Revenue under Section 260A of the Income Tax Act, 1961 (Act, for short) assail the common order of the Income Tax Appellate Tribunal (Tribunal, for short) dated 20th February, 2017 in the case of National Housing Bank (respondent- assessee bank, for short) for the Assessment Years 2003-04, 2004-05, 2005-06, 2006-07, 2008-09 and 2009-10.

2. The respondent-assessee bank is wholly owned by the Reserve Bank of India.

3. The respondent-assessee bank has been accused by the Revenue of concealment or furnishing inaccurate particulars, by making a claim for deduction under Section 36(1)(viii) of the Act. The impugned order deletes penalty imposed on the respondent-assessee bank for concealment of income under Section 271(1)(c) of the Act.

4. The contention of the Revenue is that the Tribunal has erred in accepting the explanation given by the respondent-assessee bank as to why they had claimed deduction and benefit of Section 36(1) (viii) of the Act, though the respondent-assessee bank was not engaged in providing long-term finance for construction or purchase of houses in India for residential purpose. It is submitted that penalty under Section 271(1)(c) of the Act is to be imposed when an assessee conceals its income and furnishes inaccurate particulars of income. *Mens rea* or guilty mind is not required and necessary to impose penalty under the said Section.

5. We agree with the counsel for the Revenue that *mens rea* or guilty mind is not required to be established to impose penalty under Section 271(1)(c) of the Act. However, Explanation 1 to Section 271(1)(c) states that where in respect of any facts material to computation of total income of an assessee, the assessee offers no explanation or where an assessee offers an explanation, which he is

not able to substantiate and fails to prove that such explanation is *bona fide* and that all facts relating to the same and material to the computation of the said total income had been disclosed, the amount added or disallowed in computing the total income would be deemed to represent income in respect of which particulars has been concealed. As per mandate of clause (B) to Explanation 1, the assessee has to prove that the explanation offered was *bona fide* and that all facts relating to the same and material to the computation of the total income had been disclosed by him. When the twin conditions are satisfied, the amount added or disallowed while computing the total income is not deemed to be income in respect of which particulars have been concealed.

6. In the context of the present case, we would like to first reproduce clause (viii) of Section 36(1) of the Act as applicable in the Assessment Years 2003-2004 to 2009-2010, which reads:-

“**36.** (1) The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in section 28—

(viii) in respect of any special reserve created and maintained by a financial corporation which is engaged in providing long-term finance for industrial or agricultural development or development of infrastructure facility in India or by a public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase

of houses in India for residential purposes, an amount not exceeding forty per cent of the profits derived from such business of providing long-term finance (computed under the head “Profits and gain of business or profession” before making any deduction under this clause) carried to such reserve account:

[***]

Provided [***]that where the aggregate of the amounts carried to such reserve account from time to time exceeds twice the amount of the paid up share capital and of the general reserves of the corporation or, as the case may be, the company, no allowance under this clause shall be made in respect of such excess.

Explanation.—In this clause,—

- (a) "financial corporation" shall include a public company and a Government company;
- (b) “public company” shall have the meaning assigned to it in section 3 of the Companies Act, 1956 (1 of 1956);
- (c) “Government company” shall have the meaning assigned to it in Section 617 of the Companies Act, 1956 (1 of 1956);
- (d) “infrastructure facility” shall have the meaning assigned to it in clause (23G) of Section 10;
- (e) “long-term finance” means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years;”

A reading of the said clause would indicate that the said deduction was applicable in respect of any special reserve created or maintained by a financial corporation engaged in providing long-term finance for industrial or agricultural development or for development of infrastructure facility in India or public company formed and registered in India with the object of carrying on business or providing long-term finance for construction or purchase of houses in India for

residential purpose. Such deduction cannot exceed 40% of the profits derived from such business for providing long-term finance computed under the head “profits and gains from business or profession” which was carried to such reserve. Long- term finance has also been defined in the proviso to mean loan or advance where the terms under which money was loaned or advanced provide for repayment with interest for a period not less than five years.

7. By Finance (No. 2) Act, 2009, with effect from 1st April 2010 and accordingly applicable in respect of Assessment Year 2010-2011 and subsequent Assessment Years, clause (viii) to Section 36 (1) was amended to read as under:-

“**36.** (1) The deductions provided for in the following clauses shall be allowed in respect of the matters dealt with therein, in computing the income referred to in section 28—

(viii) in respect of any special reserve created and maintained by a specified entity, an amount not exceeding twenty per cent of the profits derived from eligible business computed under the head "Profits and gains of business or profession" (before making any deduction under this clause) carried to such reserve account:

Provided that where the aggregate of the amounts carried to such reserve account from time to time exceeds twice the amount of the paid up share capital and of the general reserves of the specified entity, no allowance under this clause shall be made in respect of such excess.

Explanation.—In this clause,—

(a) "specified entity" means,—

- (i) a financial corporation specified in section 4A of the Companies Act, 1956 (1 of 1956);
- (ii) a financial corporation which is a public sector company;

- (iii) a banking company;
- (iv) a co-operative bank other than a primary agricultural credit society or a primary co-operative agricultural and rural development bank;
- (v) a housing finance company; and
- (vi) any other financial corporation including a public company;
- (b) "eligible business" means,—
 - (i) in respect of the specified entity referred to in sub-clause (i) or sub-clause (ii) or sub-clause (iii) or sub-clause (iv) of clause (a), the business of providing long-term finance for —
 - (A) industrial or agricultural development;
 - (B) development of infrastructure facility in India; or
 - (C) development of housing in India;
 - (ii) in respect of the specified entity referred to in sub-clause (v) of clause (a), the business of providing long-term finance for the construction or purchase of houses in India for residential purposes; and
 - (iii) in respect of the specified entity referred to in sub-clause (vi) of clause (a), the business of providing long-term finance for development of infrastructure facility in India;
- (c) "banking company" means a company to which the Banking Regulation Act, 1949 (10 of 1949) applies and includes any bank or banking institution referred to in section 51 of that Act;
- (d) "co-operative bank", "primary agricultural credit society" and "primary co-operative agricultural and rural development bank" shall have the meanings respectively assigned to them in the *Explanation* to sub-section (4) of section 80P;
- (e) "housing finance company" means a public company formed or registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes;
- (f) "public company" shall have the meaning assigned to it in section 3 of the Companies Act, 1956 (1 of 1956);
- (g) "infrastructure facility" means—

- (i) an infrastructure facility as defined in the *Explanation* to clause (i) of sub-section (4) of section 80-IA, or any other public facility of a similar nature as may be notified by the Board in this behalf in the Official Gazette and which fulfils the conditions as may be prescribed;
- (ii) an undertaking referred to in clause (ii) or clause (iii) or clause (iv) or clause (vi) of sub-section (4) of section 80-IA; and
- (iii) an undertaking referred to in sub-section (10) of section 80-IB;
- (h) "long-term finance" means any loan or advance where the terms under which moneys are loaned or advanced provide for repayment along with interest thereof during a period of not less than five years;"

As per the amended provisions of clause (viii), the deduction was reduced to 20% of the profits derived from eligible business. The “eligible business” itself was defined to mean business for providing long-term finance for industrial or agricultural development, development of infrastructure facility in India or construction of purchase of houses in India for residential purposes. Respondent-assessee bank has been allowed deduction under Section 36(1)(viii), post the amendment with effect from Assessment Year 2010-2011.

8. It is an accepted and admitted case that the respondent-assessee bank is a certified corporation specified in Section 4A of the Companies Act, 1956.

9. The respondent-assessee bank, it is accepted and admitted by the Revenue, was engaged in promotion and regulation of housing finance institution in the country and had provided re-finance support to financial institutions, banks, etc. for development of housing in India. They had also undertaken business of financing some projects, rural housing projects, etc. They had not, however, directly granted housing loans or long-term finance for housing to individuals.

10. The respondent-assessee bank, before filing its return for the Assessment Year 2003-04, had written letter dated 22nd October, 2002 to the Director ITA-2, Central Board of Direct Taxes with a request for issue of notification certifying that the respondent-assessee bank was eligible for deduction under Section 36(1)(viii) on transfer of 40% of the profits derived from business for providing long-term finance for housing to the special reserve. Meetings were held with the officers of the Central Board of Direct Taxes on the question of deduction and benefit under Section 36(1)(viii) of the Act. Consequent to the said meetings, the respondent-assessee bank had written a letter dated 2nd December, 2002 referring to the discussions held and the view expressed that the respondent-assessee bank was eligible and entitled to deduction under Section 36(1)(viii) of the Act,

as it would satisfy the requirement and condition of providing long-term finance for housing.

11. The respondent-assessee bank had also taken legal opinion from a Chartered Accountant, who had opined that they were eligible and would be entitled to benefit of deduction under Section 36(1)(viii) of the Act being engaged in re-financing of long-term financing loans given by other financial institutions for purchase of residential houses in India. Thus, the respondent-assessee bank had bonafidely and genuinely believed that they were eligible and entitled to the said deduction.

12. Accordingly and in terms of the genuine belief predicated on the opinions expressed, the respondent-assessee bank had created a special reserve in the respective years to which the profits from the business of long-term finance were transferred to claim deduction under Section 36(1)(viii) of the Act.

13. To us there cannot be any doubt or debate, therefore, that the conduct of the respondent-assessee bank was *bona fide*. They were initially in doubt and debate whether the claim for deduction under Section 36(1)(viii) of the Act was admissible. Therefore, they had written to the Director ITA-2, Central Board of Direct Taxes.

Meetings were held and the opinion expressed then was that the respondent-assessee bank would be eligible for deduction. Legal opinion was also taken from a Chartered Accountant.

14. The respondent-assessee bank, in the return of income filed by them, had taken care and caution to make a specific disclosure in respect of deduction claimed under Section 36(1)(viii) of the Act. We would quote from the return of income for the Assessment Year 2003-04:-

“1. The assessee was established as a Bank by the National Housing Bank Act, 1987. Section 3 of the Act provides that the Bank is a body corporate having perpetual succession and a common seal with power, subject to the provisions of the Act, to acquire, hold and dispose of property and to contract and by that name, sue and be sued.

The object with which the National Housing Bank (herein after referred to as NHB/ Bank for short] was established is to provide long term finance for construction and/or purchase of residential housing or residential township-cum-housing development or slum clearance projects.

The entire capital of NHB is held by the Reserve Bank of India and the Bank is established as a SPV (Special Purpose Vehicle) for providing long term finance for residential housing in India.

It provides long term housing finance through the Housing Finance Institutions, Scheduled Banks, State Co-operative agricultural and Rural development Banks etc as well as directly.

The Bank was exempted from the payment of Income Tax by section 48 of the National Housing Bank Act, 1987. The section has been omitted with effect from 1st April, 2002.

Section 36(1)(viii) of the Income Tax Act, 1961 provides a Special deduction of forty percent of the income derived from the business of providing long term finance for housing in the computation of its taxable income to a Bank or financial corporation.

The special allowance is subject to fulfilling certain other conditions prescribed in that section more particularly creation of a special reserve to the extent of claim under the section.

The assessee fulfills the required conditions of section 36(1)(viii) of the IT Act, and had also created the necessary Special Reserve to the extent of Rs. 35.50 crores, in the accounts for the year ended on 31.3.2003.

Housing finance loans are to be extended for a period not less than 5 years each. Therefore some of the loans recovered can not be advanced again but retained to meet its obligations of repayment of borrowings.

The bank has obligations like repayment of borrowings at committed dates. Further banking prudence requires certain portion of the funds to be kept in liquid form or in Gilts to meet the financial commitments. The RBI which owns this bank, has prescribed the norms of such liquid funds by way of SLR and CRR ratios for the Commercial/ Scheduled Banks. This bank also follows such ratios of the purposes of financial prudence.

These funds are deployed by way of call money or short deposits, overnight deposits and other deposits with other banks for short periods as well as in Gilts. The income earned on it is nothing but recouping a part of interest paid on the funds and is incidental to the only main business of Housing finance.

Since the only object of the Bank is long term housing finance, the whole of the profits are eligible for the Special deduction of 40% of its profits.

2. Reserve for Doubtful/ Loss Assets-Claim u/s 36(1)(viii) [c]:

The Bank has provided a sum of Rs. 4.50 crores as Reserve for Doubtful assets/ loss assets covered by the provisions of Section 36(1) (viii) of the Income Tax Act, 1961. Keeping in view the privilege available to Banks, such provision has been reduced from the Gross receipt of Interest of the bank. It is being added back in the computation of taxable income for being claimed again as per the provisions of law in this regard.”

Similarly, disclosures were made in returns for other assessment years. It is not disputed and cannot be debated that the respondent- assessee had disclosed full and correct facts to claim deduction under Section 36(1) (viii) of the Act. Noting was concealed or withheld.

15. Despite the aforesaid factual background and clear explanation given by the respondent-assessee bank to establish and show their *bona fides*, the Assessing Officer had initiated and levied penalty under Section 271(1)(c) of the Act in respect of Assessment Years 2003-04 to 2009-10. The reason was that the Assessing Officer did not accept the claim of the respondent-assessee bank in the quantum or assessment proceedings for deduction under clause (viii) to Section 36(1) of the Act. In the meanwhile, the respondent-assessee bank had continued to raise the issue with the Central Board of Direct Taxes. Consequently, clause (viii) of Section 36(1) was amended by Finance (No.2) Act of 2009 with effect from 1st April, 2010 to specifically enact and give benefit to the respondent-assessee bank engaged in re-financing of long-term finance for construction and purchase of

houses in India. The said amendment obviously was enacted for the benefit of the respondent-assessee bank in view of different opinion expressed by the income tax authorities during the course of the assessment/quantum proceedings. Memorandum explaining the amendments made by Finance (No.2) Act, 2009 reads as under:-

“ A view has been expressed that NHB is not entitled to the benefits of section 36(1)(viii) on the ground that it is not engaged in the long-term financing for construction or purchase of houses in India for residential purpose. The proposed amendment seeks to provide that corporations engaged in providing long-term finance(including re-financing) for development of housing in India will be eligible for the benefit under section 36(1)(viii).”

16. Section 3 (22) of General Clauses Act, 1897 states that a thing shall be deemed to be done in good faith where it is in fact done honestly, whether it is done negligently or not. Section 52 of the Indian Penal Code, 1860 says that nothing is said to be done or believed in "good faith" which is done or believed without due care and attention. In ***Shiv Sarup Gupta Vs. Dr. Mahesh Chand Gupta*** AIR 1999 SC 2507, the Supreme Court interpreted the word ‘genuine’ to mean not spurious, natural, real, pure and sincere. It means absence of fraud or deceit. It should reflect the state of mind of the doer.

17. In the context of Explanation 1 to Section 271(1)(c), the word *bona fide*, i.e. good faith, would require due care and attention, which means reasonable care and attention. There should be an element of honesty attached to the defence and the explanation given by the assessee and there should be absence of any pretence, deceit or fraud (see paragraph 184 and onward in ***Subramanian Swamy Vs. Union of India*** (2016) 7 SCC 221)

18. Questioning the *bona fides* of the respondent-assessee bank, learned counsel for the Revenue had submitted and referred to the order passed by the Commissioner of Income Tax (Appeals) affirming the order of penalty. Commissioner of Income Tax (Appeals) had held that the respondent-assessee had paid advance tax for the Assessment Year 2003-04, without including and computing benefit of deduction under Section 36(1) (viii) of the Act, which would indicate and show that the respondent-assessee was not entitled to the benefit. We do not agree that payment of advance tax would show and establish lack of bona fides. It is not only the respondent-assessee bank who had verily believed their entitlement to deduction under clause (viii); even officers of the Central Board of Direct Taxes were of the same opinion. *Bona fides*, therefore, of the respondent-assessee cannot be doubted or debated as advance tax was paid. There is no

column of income tax returns whereby the assessee, in case of claim, can call upon Assessing Officer to decide and adjudicate claim for deduction. Provisions of Advance Ruling were not applicable. Therefore, to claim any benefit of any deduction, a claim is required to be made in the return with full particulars and details.

19. It is in this context that we have to examine the *bona fide* of the claim made in return for benefit under Section 36(1)(viii) of the Act. *Bona fides* are accordingly examined with reference to statutory provision, which is required to be interpreted, and whether interpretation placed by assessee was plausible and could have been accepted. Where the explanation is not make belief and sham but genuine, the assessee would satisfy the requirement of Explanation 1 to Section 271(1)(c) of the Act. This test and requirement is satisfied in the present case. Further, full and complete facts were clearly stated in the income tax returns. In our opinion, the respondent-assessee had acted bonafidely and were under a genuine belief that they were entitled to benefit of the said deduction. Appropriate for this case are the observations of the Delhi High Court in ***New Holland Tractors (India) Private Limited Vs. The Commissioner of Income -tax Delhi*** (2015) 275 CTR 291, wherein it was held as under:

“Test of bona fide has to be applied keeping in mind the position as it existed, when the return of income was filed. The Act, i.e. the Income Tax Act, is a complex legislation involving intricate and often debatable legal positions. The legal issue involved may relate to principles of accountancy. Invariably, on questions of interpretation, the assessee does adopt a legal position which they perceived as most beneficial or suitable. This would not be construed as lack of bona fides as long as the legal position so adopted is not per se contrary to the language of the statute or an undebatable legal position not capable of a different connotation and understanding. When two legal interpretations were plausible and there was a genuine or credible plea, penalty for concealment/furnishing of inaccurate particulars, should not and cannot be imposed. If the view taken by the assessee required consideration and was reasonably arguable, he should not be penalized for taking the position. The tax statutes are convoluted and complex and there can be manifold opinions on interpretation and understanding of a provision or the tax treatment. In such cases, even when the interpretation placed by the Revenue is accepted, penalty should not be imposed if the contention of the assessee was plausible and bona fide. Of course full facts should be disclosed. While applying the test of bonafide, we have to also keep in mind that even best of legal minds can have difference of opinion. It is not uncommon to have dissenting opinion on the question of law, in the courts.”

20. Recording the above, we dismiss the present appeals with no order as to costs.

SANJIV KHANNA, J.

CHANDER SHEKHAR, J.

AUGUST 28, 2018

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