

* **IN THE HIGH COURT OF DELHI AT NEW DELHI**
+ **INCOME TAX APPEAL NO. 127/2002**

Reserved on : 24th September, 2014
Date of decision: 11th November, 2014

THE COMMISSIONER OF INCOME TAX, DELHI-IV

..... Appellant

Through Mr. Kamal Sawhney, Sr. Standing
Counsel & Mr. Sanjay Kumar, Advocate.

versus

M/S INDUSTRIAL FINANCE CORPORATION OF INDIA
LIMITED

..... Respondent

Through Ms. Kavita Jha & Mr. Vivek Bansal,
Advocates.

CORAM:
HON'BLE MR. JUSTICE SANJIV KHANNA
HON'BLE MR. JUSTICE V. KAMESWAR RAO

SANJIV KHANNA, J.:

This appeal by the Revenue, which relates to Assessment Year 1986-87, stands admitted for adjudication on the following substantial questions of law:-

“1. Whether on the facts and circumstances of the case the ITAT was correct in law in allowing the deduction u/s 80M & 80K without reducing from the dividend income, the deduction as admissible u/s 36(1)(viii) of the Act?

2. Whether ITAT was correct in law in allowing the deduction u/s 36(1)(viii) of the Act to the extent of 40% of the income determined without restricting the amount transferred to the reserve created during the year?

3. Whether on the facts and circumstances of the case the Tribunal was correct in awarding the

allowance of Rs.72,574/- being the amortization expenses incurred for acquiring lease hold land by the assessee?”

2. Return filed by the respondent-assessee was made subject matter of regular assessment under Section 143(3) of the Income Tax Act, 1961 (“Act”, for short), vide assessment order dated 30th March, 1989. Total income was assessed at Rs.25,35,90,870/-. The assessee was allowed deduction under Section 36(1)(viii) of the Act and was also allowed deduction under Sections 80M and 80K of the Act on dividend income of Rs.2,26,12,593/-. The total quantum of deduction allowed under Section 36(1)(viii) was Rs.17,81,18,441/-. Similarly, the assessee was allowed amortisation of expenses of Rs.72,574/- in respect of the leasehold land.

3. The Commissioner of Income Tax, under Section 263 of the Act, by her order dated 7th March, 1991 issued directions to the Assessing Officer to pass a fresh or re-frame the assessment order on the aforementioned deductions, after giving due opportunity.

4. Thereupon, order dated 9th August, 1991 was passed by the Assessing Officer. The Assessing Officer after referring to Section 80AA and 80AB of the Act held that the deduction under Sections 80M and 80K should be allowed with reference to the ‘gross total income’ computed in accordance with the provisions of the Act before making any deduction under Chapter VI-A. The dividend income included in the ‘gross total income’ ought to be reduced by 40% as the deduction had been allowed under Section 36(1)(viii) of the Act. The reason given was that once deduction under Section 36(1)(viii) was allowed on income that included dividend income, the gross dividend should be reduced by 40% to compute the net dividend income. Accordingly, by order dated 9th August, 1991, the deduction under Sections 80K and 80M was recomputed as under:-

“A) <u>DEDUCTION U/S 80-K</u>	
Gross Dividend	46,976
Less: u/s 36(1)(viii)	<u>18,790</u>
	<u>28,186</u>
Exemption u/s 80-K @ 60%	Rs.16,911
B) <u>Deduction u/s 80-M</u>	
Other dividend	2,26,90,618
Less: Admn. Expenses	<u>25,000</u>
	2,26,65,618
Less: Dedn. U/s 36(1)(viii)40%	<u>90,26,247</u>
Dividend entitled to deduction	1,36,39,381
Before allowing deduction under Chapter-VIA	
Deduction u/s 80-M (60%)	81,23,622/-”

5. The Assessing Officer referred to the second proviso to Section 36(1)(viii) and observed that the “reserves” eligible for deduction cannot exceed twice the paid-up capital of the respondent of Rs.3500 crores. Thus, deduction allowable under Section 36(1)(viii) had to be restricted to Rs.17,75,72,000/- and need not be allowed upto 40% of the total income before making any deduction under the said sub-section or Chapter VI-A.

6. On the third question, the Assessing Officer disallowed revenue deduction of Rs.72,574/- treating the payment as capital in nature as it was incurred towards amortization of leasehold land at Calcutta, Patna and Kanpur. The lease period, it was observed, varied between 66 years to 99 years.

7. The Commissioner of Income Tax (Appeals) [C.I.T (A)], however, reversed the aforementioned findings holding that deduction under Section 80M should be calculated without deducting the “deduction” under Section 36(1)(viii) of the Act from the dividend income. Amortisation expenses were also directed to be allowed as revenue expense. Noticeably, the

assessee did not challenge re-computation of deduction under Section 80K made by the Assessing Officer possibly because the amount involved was only Rs.18,790/-. Similarly, the assessee did not challenge the re-computation of deduction under Section 36(1)(viii) with reference to the second proviso

8. Revenue preferred an appeal raising the following grounds:-

“On the facts and in the circumstances of the case, the Ld. CIT (A) has erred in:

- (i) directing A.O. to allow deduction u/s 80-M & 80-K without reducing from the dividend income the deduction admissible u/s 36(1)(viii) following its order in other asst. year which has not been accepted by department.
- (ii) directing the A.O. to allow the deduction u/s 36(1)(viii) to the extent of 40% of the income determined without restricting the amount transferred to the reserve created during the year u/s 36(1)(viii) by following appellate order for earlier year, which has not been accepted by the department.
- (iii) deleting the disallowance of Rs.72,574/- in respect of leasehold property by following the appellate order for earlier year, which not been accepted by the department.”

9. It is noticeable that the Revenue while framing the grounds of appeal did not notice that the assessee had not challenged reduction of deduction under Section 80K and the C.I.T(A) had not dealt with the said issue. Similarly, the assessee had not questioned application of the second proviso to Section 36(1)(viii) before the C.I.T(A) and this issue was neither raised nor decided. We accordingly hold that the Income Tax Appellate Tribunal (Tribunal, for short) fell in error in treating the deduction under Section 80K and disallowance made under Section 36(1)(viii) as a ground raised by the Revenue in appeal. Similar error has been made while framing the substantial questions of law. We hold and observe that while deciding question No. 1, we will examine the deduction under Section 80M

and not under Section 80K. Further, question No. 2 does not arise for consideration as the said issue never arose in the appellate proceedings after the findings recorded by the Assessing Officer. The findings of the assessing officer to this extent were accepted.

10. Now, we would like to reproduce Section 36(1)(viii) and Section 80M of the Act as they existed and applicable to the relevant assessment year:-

“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-

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(viii) in respect of any special reserve created by a financial corporation which is engaged in providing long-term finance for industrial or agricultural development 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 total income (computed before making any deduction under Chapter VI-A) carried to such reserve account:

Provided that the corporation or, as the case may be, the company is for the time being approved by the Central Government for the purposes of this clause:

Provided further 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 (excluding the amounts capitalised from 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, “public company” shall have the meaning assigned to it in Section 3 of the Companies Act, 1956 (1 of 1956)

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80M. (1) Where the gross total income of an assessee, being a domestic company, includes any income by way of dividends from a domestic company, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a

deduction from such income by way of dividends of an amount equal to-

- (a) in respect of such income by way of dividends from a company formed and registered under the Companies Act, 1956 (1 of 1956), after the 28th day of February, 1975, and engaged exclusively or almost exclusively in the manufacture or production of any one or more of the articles or things specified in items 2 and 3, item 4 (excluding alloy, malleable and S.G. iron castings), items 7 to 15 (both inclusive), items 17 and 18, item 23 (excluding refractories) and items 24, 26, 27, 28, 29, 30 and 33 in the list in the Ninth Schedule.

the whole of such income

- (b) in respect of such income by way of dividends other than the dividends referred to in clause (a) *sixty per cent of such income*

(2) Where a company to which this section applies is entitled also to the deduction under Section 80K, the deduction under sub-section (1) shall be allowed in respect of income by way of dividends referred to therein as reduced by the amount of the deduction under Section 80K.

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11. Before we proceed further, we would also like to reproduce Sections 80B(5) and 80AA of the Act, which are as under:-

“80B(5) ‘gross total income’ means the total income computed in accordance with the provisions of this Act, before making any deduction under this Chapter;

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80AA. Computation of deduction under Section 80M- Where any deduction is required to be allowed under Section 80M in respect of any income by way of dividends from a domestic company which is included in the gross total income of the assessee, then, notwithstanding anything contained in that section, the deduction under that section shall be computed with reference to the income by way of such dividends as computed in accordance with the provisions of this Act (before making any deduction under this Chapter) and now with reference to the gross amount of such dividends.”

12. Sub-section (1) to Section 36 states that the deduction provided in the clauses thereunder shall be allowed in respect of matters dealt with

therein while computing income referred to in Section 28 of the Act. Section 28 of the Act relates to income by way of “profits and gains of business or profession”. Clause (viii) of Section 36(1) states that the stipulated financial corporation shall be allowed deduction in respect of special reserve created by them of an amount not exceeding 40% of the total income computed before allowing any deduction under Chapter VI-A, carried to the reserve account. Thus, when special reserve was created and income earned during the year was carried or transferred to the reserve account, deduction under clause (viii) to Section 36(1) was to be allowed. The deduction could have exceeded 40% of the total income of the said year. The total income referred to in the said clause meant income computed before making any deduction under Chapter VI A. The second proviso to Section 36(1)(viii) dealt with second upper limit for claiming deduction under Section 36(1)(viii). On the application of the second proviso, the finding of the Assessing Officer has attained finality.

13. Chapter VI-A of the Act consists of fasciculus of Sections dealing with deductions permissible while computing total income. Section 80M in the opening words refers to the expression “gross total income of an assessee” and thereafter stipulates that where gross total income of the assessee includes income by way of dividends etc., the deductions would be allowed. The expression “gross total income” for the purpose of Chapter VI-A as defined in Section 80B(5) meant total income computed in accordance with the provisions of this Act but before making any deductions under Chapter VI-A. Accordingly, the Section postulated that the gross total income meant total income computed under Chapter III of the Act. Thus, the total income computed under Section 28 of the Act after allowing deductions under Section 36(1)(viii), plus other income of the assessee, as computed, would constitute the gross total income on which

deduction under Sections 80M could be allowed. The deduction allowed under Section 36(1)(viii) of the Act got excluded and did not partake income included in gross total income on which deduction under Sections 80M was to be allowed. The amounts deducted under Section 36(1)(viii) ceased to be part of the gross total income as stipulated in Section 80B(5). Thus, there is no question of double deduction or multiple deduction on the same income, if deduction under Section 36(1)(viii) stands excluded and is not part of the gross total income on which deduction under Section 80M was to be allowed.

14. Section 80M dealt with and allowed deduction on specific type/character of income by way of dividends. Deduction was to be allowed as per the computation made under the said Section. Section 80M did not make any reference to deduction under Section 36(1)(viii). There was no such stipulation expressed or implied. Reliance placed on Section 80AA of the Act (since omitted), which has been quoted above, is misconceived. Section 80AA dealt with computation of deduction under Section 80M and mandated that deduction under the said Section should be with reference to the income by way of dividends computed in accordance with the provisions of the Act, but before making any deduction under Chapter VI- A and not with reference to the gross amount of dividends. The said provision was incorporated by Finance (No. 2) Act, 1980 after the judgment of the Supreme Court in the case of ***Cloth Traders Private Limited versus Additional Commissioner of Income Tax***, (1979) 118 ITR 243 (SC). However, ***Cloth Traders Private Limited (supra)*** was overruled by the Supreme Court in ***Distributors (Baroda) Private Limited versus Union of India***, (1985) 155 ITR 120 (SC) and the counsel for the appellant-Revenue has relied upon the following paragraph of the latter judgment:-

“ We may, therefore, first examine the language of Section 80M for arriving at its true interpretation. But before we do so, let us consider what is the object behind grant of relief under Section 80M. It was common ground between the parties that the main object of the relief under Section 80M is to avoid taxation once again in the hands of the receiving company of the amount which has already borne full tax in the hands of the paying company. Vide the written submission under the heading “Object of relief on intercorporate dividends” filed by the learned Counsel on behalf of the assessee in the course of the arguments. Now when an amount by way of dividend is received by the assessee from the paying company, the full amount of such dividend would have suffered tax in the assessment of the paying company and it is obvious, that, in order to encourage inter-company investments, the Legislature intended that this amount should not bear tax once again in the hands of the assessee either its entirety or to a specified extent. But the amount by way of dividend which would other-wise suffer tax in the hands of the assessee would be the amount computed in accordance with the provisions of the Act and not the full amount received from the paying company. Therefore, it is reasonable to assume that in enacting Section 80M the Legislature intended to grant relief with reference to the amount of dividend computed in accordance with the provisions of the Act and not with reference to the full amount of dividend received from the paying company. It is difficult to imagine any reason why the Legislature should have intended to give relief with reference to the full amount of dividend received from the paying company when that is not the amount which is liable to suffer tax once again in the hands of the assessee. The Legislature could certainly be attributed with the intention to prevent double taxation but not to provide an additional benefit which would go beyond what is required for saving the amount of dividend from taxation once again in the hands of the assessee. Bearing in mind these prefatory observations in regard to the legislative object, we may now proceed to construe the language of Section 80M.”

15. The aforesaid paragraph shows that the Supreme Court was conscious and attentive to the fact that Section 80M stood enacted with the object to provide relief on inter-corporate dividends for the said income had already suffered incidence of tax in the hands of paying company and, therefore, should not be subjected to tax twice. Thus, where the dividend

would not have otherwise suffered tax, the said amount of dividend should not be allowed the said deduction.

16. We do not think the aforesaid ratio or provision under section 80AA would have any application to the facts of the present case. The assessee, as is apparent from the calculations made by the Assessing Officer, had received dividend of Rs.2,26,90,618/-. The total income of the assessee as per the original assessment order dated 30th March, 1989 was Rs.25.35 crores, which stood enhanced to Rs.26.96 crores. The income so computed was after deduction under Chapter VI A and after reducing administrative expenses of Rs. 26,26,65,618/-. The total income before deduction under VI-A, necessarily would be much higher. It therefore follows that the dividend income was a miniscule and a fraction of the total income. The aforesaid total (taxable) income was computed after allowing deduction under Section 36(1)(viii) of Rs.17.75 crores, an amount if not subtracted would have further increased the quantum the total income. Therefore, in the facts of the present case, it will not be appropriate and correct to treat dividend income of Rs.2,26,65,618/- as a part of Rs.17.75 crores, deposited and transferred to the special reserve. The aforesaid dividend income of Rs 2,26,65,618 could well be treated and regarded as a part of and included in the total income, subjected to tax of Rs.25.35 crores/ Rs.25.96 crores. There is therefore a basic fallacy and flaw in the argument raised by the Revenue.

17. Even otherwise we find that the issue in question, the effect of Section 36(1)(viii), viz. deduction claimed under Section 80M in view of Section 80AA stands examined by different High Courts with the question raised being decided in favour of the assessee and against the revenue. The first decision is that of Madhya Pradesh High Court in ***Commissioner of***

Income Tax versus Madhya Pradesh Audyogik Vikas Nigam Limited, (2005) 274 ITR 625 wherein reference was made to the decision of the High Court of Madras in ***CIT versus Chemical Holdings Limited***, (2001) 249 ITR 540 and the decision of the High Court of Bombay in ***CIT versus Maganlal Chhaganlal Private Limited***, (1999) 236 ITR 456, observing that Section 80AA only stipulated income by way of dividends included in the gross total income and it was inapposite to state that deductions under section 80M should take place after deducting the sum allowable under section 36(1)(viii). The deduction under Section 36(1)(viii) should be computed with reference to the income by way of dividends as computed in accordance with the provisions of the Act. The relevant words were “before making any deduction under this Chapter and not with reference to gross amount of such dividends”. Examining the aforesaid provisions, the courts had observed that the provisions did not support the submission of the Revenue. The ratio stands approved by the Karnataka High Court in ***CIT versus Canfin Homes Limited***, ITA No. 3159/2005 decided on 5th July, 2010, wherein it was held that Section 36(1)(viii) required creation of a special reserve by a finance corporation engaged in long-term finance for industrial or agricultural development in India. Deduction could not exceed 40% of the total income computed before making any deduction under the clauses of section 36(1) or Chapter VI A. An amount not exceeding 40% of the total income could be allowed as a deduction under the headings “profits and gains” of business or profession. Reference was thereafter made to the heading “income from other sources”, under Chapter III of the Act. On harmonious reading of the provisions, it was held that Sections 36(1)(viii) and 80M read with Section 80AA operated in altogether different fields and in the absence of any provision, prohibiting benefit, appellate authorities were justified in deciding the issue in favour of the assessee. Similar view stands expressed by the High Court of Gujarat in

Deputy Commissioner of Income Tax versus GIIC Limited, (2010) 325 ITR 597 (Guj.).

18. Question No. 1 accordingly has to be decided in favour of the respondent-assessee and against the Revenue. This answer will apply to the deduction claimed under section 80M and not in respect of deduction claimed under section 80K of the Act.

19. Question No. 3, counsel for the respondent-assessee concedes, has to be decided against the assessee in view of the pronouncement of this Court in ***Gail India Limited versus Joint Commissioner of Income Tax***, (2012) 211 Taxman 587 (Del.), wherein it has been held that amortisation of payments made towards long lease is not 'revenue expenditure' but 'capital expenditure'. Question No. 3 is accordingly answered in favour of the appellant-Revenue and against the respondent-assessee.

20. As far as second question is concerned, which arises from ground No.2 before the tribunal, the respondent-assessee never challenged the computation before C.I.T. (A), hence it need not have been raised before the Tribunal. The Tribunal's finding to this effect is null and void. The question is accordingly answered.

21. The appeal is accordingly disposed of. There will be no order as to costs.

(SANJIV KHANNA)
JUDGE

(V. KAMESWAR RAO)
JUDGE

November 11th, 2014
VKR/kkb