$-J-5, 6 & 7

* **IN THE HIGH COURT OF DELHI AT NEW DELHI**

Judgement reserved on: **09.04.2021**
Judgement pronounced on: **05.07.2021**

\+ **ITA 213/2020**

\+ **ITA 214/2020**

\+ **ITA 215/2020**

COFORGE LIMITED (FORMERLY KNOWN AS NIIT TECHNOLOGIES LTD) .....Appellant

Through: Mr. Rohit Jain and Mr. Aniket D. Agarwal, Advocates.

versus

ACIT .....Respondent

Through: Mr. Shailender Singh, Senior Standing Counsel.

CORAM:

HON'BLE MR. JUSTICE RAJIV SHAKDHER
HON'BLE MR. JUSTICE TALWANT SINGH

RAJIV SHAKDHER, J:

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Preface: -

1. The above-captioned appeals are directed against a common order dated 28.01.2020, passed by the Income Tax Appellate Tribunal [in short "Tribunal"] Pertinently, ITA 213/2020 and ITA 215/2020 concern assessment year [AY] 2007-2008 while ITA 214/2020 concerns AY 2008-2009.

1.1. On 13.01.2021, all three appeals were admitted and the following questions of law were framed.

Questions of law framed in ITA 213/2020 and 214/2020

> "(i) Whether, on the facts and in the circumstances of the case, the Tribunal erred in law in upholding the disallowance of Rs.44,00,739/- claimed under section 35DD of the Act, being l/5th of expenses incurred in [the] assessment year 2004-05 on [the] demerger of certain units of NIIT and vesting of the same in the Appellant, on the incorrect premise that such deduction is allowable only in the hands of the demerged company (NIIT) and not the resulting company (Appellant)?
>
> (ii) Whether on the facts and in the circumstances of the case, the Tribunal erred in law in sustaining and not deleting the disallowance under Section 14A of the Act, to the extent of 0.5% of [the] average value of investments which yielded exempt income during the year?"

Questions of law framed in ITA 215/2020

> "(i) Whether on the facts and in the circumstances of the case, the Tribunal erred in law in not deleting in-toto the disallowance of one-time commuted/discounted lease rent amounting to Rs. 77,98,042/- (equivalent to 11 times annual rent) made by the assessing officer?
>
> (ii) Whether the Tribunal erred in law in travelling beyond the scope of the appeal and the case set-up by the assessing officer/CIT(A) and argued by the Revenue, contrary to the mandate of Section 254 of the Act, and that too, without confronting the said reasoning/basis to the Appellant (through its counsel) at the time of hearing?"

Background facts: -

2. Before we proceed further to adjudicate upon the questions of law framed in the captioned appeals, the following broad facts are required to be noticed in each of the appeals.

3. The appellant/assessee had filed its return for AY 2007-2008, on 30.10.2007, declaring its taxable income as Rs.1,03,47,200/-. Via this return, deduction of Rs. 1,06,43,88,624/- was claimed under Section 10B of the Income Tax Act, 1961 [in short "Act"].

3.1. The assessment concerning the appellant/assessee was framed under Section 143(3) of the Act. An order to that effect was passed on 30.12.2010, wherein the appellant/assessee's taxable income was assessed at Rs. 36,28,88,570/-. The assessing officer [in short "AO"] while passing the assessment order, inter alia, made the following disallowances.

i. The amortised legal and professional expenses amounting to Rs.44,00,739/-; being 1/5th of the total amount incurred under this head i.e. Rs.2,20,03,694/- in the AY 2004-05, in connection with demerger. The deduction was claimed by the appellant/assessee under Section 35DD of the Act.

ii. Disallowance of Rs. 1,79,17,211/-; this disallowance was ordered by the AO based on the provisions of Section 14A of the Act and Rule 8D of the Income Tax Rules, 1962 [in short "Rules"]. Although, the appellant/assessee suo motu disallowed an amount of Rs. 5,62,842/-, no findings were returned by the AO qua the same in the assessment order. The break-up of the said figure is detailed out hereafter.

S. No.	Particulars	Amount (Rs.)
1.	Direct expenditure concerning exempt income [(refer Rule 8D(2)(i)]	Nil
2.	Interest expenditure not directly attributable to any particular income [(refer Rule 8D (2)(ii)]	1,02,88,677
3.	½% of average investments [(refer Rule 8D(2)(iii)]	76,28,534

	TOTAL	1,79,17,211

3.2. The appellant/assessee carried the order, passed by the AO, in appeal to the Commissioner of Income Tax (Appeals) [in short "CIT(A)"]. The CIT(A), vide order dated 30.07.2013, partly allowed the appeal preferred by the appellant/assessee. The net result was that, while CIT(A) sustained the disallowance ordered by the AO under Section 35DD of the Act, the disallowance directed by the AO under Section 14A of the Act read with Rule 8D of the Rules was scaled down from the figure of Rs. 1,79,17,211/- to Rs. 82,05,031/-. Also, the CIT(A) rejected the aforementioned suo motu disallowance, as being ad-hoc in nature and without any basis. The break-up of the disallowance under Section 14A of the Act, as ordered by the CIT(A) is as follows.

S. No.	Particulars	Amount (Rs.)
1.	Direct expenditure concerning exempt income	Nil
2.	Interest expenditure not directly attributable to any particular income	44,71,541
3.	½% of average investments	37,33,490
	TOTAL	82,05,031

3.3. This propelled the appellant/assessee to carry the matter further, and accordingly, an appeal was preferred with the Tribunal. The Tribunal, via its order dated 28.01.2020, also allowed the appeal, albeit, partially. Resultantly, while the Tribunal sustained the findings of the AO and CIT(A) concerning disallowance under Section 35DD of the Act, it deleted the entire disallowance of Rs. 44,71,541/- ordered by the authorities below, in respect of interest expenditure [inadvertently the figure has been noted in the order as Rs. 37,33,490/-] under Section 14A of the Act read with Rule 8D of the Rules and ordered that the disallowance under Section 14A of the Act be restricted only to administrative expenditure, which, according to it, ought to be quantified at

0.5% of the value of investments, that yielded income exempt from tax in the period under consideration.

3.4. Since the appellant/assessee was not satisfied, it has preferred the instant appeal with this Court.

ITA 214/2020

4. The appellant/assessee had filed its return for AY 2008-2009, on 30.09.2008, declaring its taxable income as Rs.13,91,86,140/- and book profits under Section 115JB of the Act as Rs.1,09,27,33,369/-. Via this return, deduction of Rs. 1,04,94,23,584/- was claimed under Section 10B of the Act.

4.1. The assessment concerning the appellant/assessee was framed under Section 143(3) of the Act. An order to that effect was passed on 12.12.2011, wherein the appellant/assessee's taxable income was assessed at Rs. 34,95,45,730/-, and the book profits under Section 115JB of the Act were enhanced to Rs. 1,10,83,41,631/-. The AO, while passing the assessment order, inter alia, made the following disallowances.

i. The amortised legal and professional expenses amounting to Rs.44,00,739/-; being 1/5th of the total amount incurred under this head i.e. Rs.2,20,03,694/- in the AY 2004-05, in connection with demerger. The deduction was claimed by the appellant/assessee under Section 35DD of the Act.

ii. Disallowance of Rs. 1,56,08,262/-, after deducting suo motu disallowance of Rs.7,79,063/-; this disallowance was made by the AO by invoking provisions of Section 14A of the Act and Rule 8D of the Rules. The break-up of the said figure is detailed out hereafter.

S. No.	Particulars	Amount (Rs.)
1.	Direct expenditure concerning exempt	Nil

	income [(refer Rule 8D(2)(i)]	
2.	Interest expenditure not directly attributable to any particular income [(refer Rule 8D (2)(ii)]	66,48,325
3.	½% of average investments [(refer Rule 8D(2)(iii)]	97,39,000
	Total	1,63,87,325
	Less: Suo motu disallowance by appellant/assessee	7,79,063
	DISALLOWANCE	1,56,08,262

4.2. The appellant/assessee carried the order, passed by the AO, in appeal to the CIT(A). The CIT(A), vide order dated 30.07.2013, partly allowed the appeal preferred by the appellant/assessee. The net result was that, while CIT(A) sustained the disallowance ordered by the AO under Section 35DD of the Act, the disallowance directed by the AO under Section 14A of the Act read with Rule 8D of the Rules was scaled down from the figure of Rs. 1,56,08,262/- to Rs. 91,18,132/-. The break-up of the disallowance under Section 14A of the Act, as ordered by the CIT(A) is as follows.

S. No.	Particulars	Amount (Rs.)
1.	Direct expenditure concerning exempt income	Nil
2.	Interest expenditure not directly attributable to any particular income	36,85,740
3.	½% of average investments	62,11,454
	Total	98,97,195
	Less: Suo motu disallowance by appellant/assessee	7,79,063
	DISALLOWANCE	91,18,132

4.3. This propelled the appellant/assessee to carry the matter further, and accordingly, an appeal was preferred with the Tribunal. The Tribunal, via its order dated 28.01.2020, also allowed the appeal partially. Resultantly, the Tribunal sustained the findings of the CIT(A) concerning disallowance of

deduction claimed under Section 35DD of the Act, in line with its decision for AY 2007-08. Likewise, it ordered that the disallowance under Section 14A of the Act be restricted only to administrative expenditure. According to the Tribunal, as held by it qua AY 2007-2008, administrative expenditure ought to be quantified at 0.5% of the value of investments, that yielded income exempt from tax in the period under consideration.

4.4. Since the appellant/assessee was not satisfied, it has preferred the instant appeal with this Court.

ITA 215/2020

5. The appellant/assessee, on 12.01.2007, executed an agreement/ lease deed with the Greater Noida Industrial Development Authority [in short "GNIDA"] concerning a parcel of land situated at Plot No. 2A, Sector Techzone (IT Park), GNIDA District, Gautam Budh Nagar, admeasuring about 20622.92 square metres. Under the said lease deed, the appellant/assessee was obliged to complete the construction of the superstructure within seven years of its execution, as per the layout and building plan approved by GNIDA. The tenure of the lease was fixed at 90 years; commencing from 12.01.2007; with the rights and interest in land reverting to GNIDA at the end of the tenure. [See: page 109 of the paper book]

5.1. Pertinently, in terms of the said lease deed, the appellant/assessee had the option, to either pay the annual rent of Rs. 7,08,913/- during the tenure of the lease, or in the alternative, a commuted and discounted one-time lease rent amounting to Rs. 77,98,042/-. The commuted and discounted lease rent was 11 times the annual lease rent.

5.2. The appellant/assessee opted for the second option for payment of lease rent, and accordingly, paid Rs. 77,98,042/- to GNIDA in the financial year [FY] 2006-2007, which is relevant for AY in issue i.e. 2007-2008.

5.3. Consequently, in the return filed by the appellant/assessee, on 30.10.2007, for AY 2007-2008 wherein it had declared its total taxable income as Rs. 1,03,47,200/-, it claimed a deduction of the aforementioned lease rent i.e. Rs. 77,98,042/-, as revenue expenditure.

5.4. The AO, vide order dated 30.12.2010, passed under Section 143(3) of the Act, assessed the appellant/assessee's taxable income at Rs. 36,28,88,570/-, and while doing so, he disallowed the deduction claimed towards lease rent. The AO was of the view that "one-time lease rent charges" paid by the appellant/assessee gave it the benefits of enduring nature, and hence, had to be classified as capital expenditure and not revenue expenditure.

5.5. In the appeal preferred by the appellant/assessee, the CIT(A), vide order dated 30.07.2013, deleted the disallowance ordered by the AO in respect of the aforesaid one-time lease rent charges, and held that the expenditure was incurred wholly and exclusively for the purpose of business.

5.6. The revenue, being dissatisfied with the order of the CIT(A), instituted an appeal with the Tribunal. The Tribunal, vide order dated 28.01.2020 while accepting the principle contention on behalf of the appellant/assessee that commuted and discounted lease rent amounting to Rs. 77,98,042/- had to be classified as revenue expenditure, directed that the said amount should be spread through the entire tenure of the lease i.e. 90 years by applying the matching principle of accounting.

Submissions on behalf of the appellant/assessee: -

6. Mr. Rohit Jain advanced submissions on behalf of the appellant/assessee. He, broadly, made the following submissions concerning the issues that arose before us.

i. Insofar as the disallowance of expenditure for the AYs in issue, i.e., AY 2007-08 and 2008-09 is concerned, it was contended that the Tribunal

had erred in upholding the disallowance even while the same had been allowed for 3 AYs i.e. AY 2004-2005, 2005-2006 and 2006-2007. In other words, the submission was that the principle of consistency should have been kept in mind by the revenue. [See: ***CIT vs. Rajasthan Breweries Limited*** [ITA 889/2009] (Del); the SLP filed vis-à-vis this judgement i.e. SLP (Civil) 1379/2014 was dismissed on 07.02.2014; and ***Shasun Chemicals & Drugs Ltd. vs. CIT***, (2016) 289 CTR 97 (SC)]

ii. The Tribunal's view that the expression "assessee" in Section 35DD of the Act only refers to the demerged company, and upon demerger, the resultant company, which is the appellant/assessee, in this case, is non-existent and comes into existence only after the demerger takes place, is both on law and on facts flawed.

iii. The Tribunal lost sight of the fact that the demerger took place between two existing companies, and that the appellant/assessee was in existence on the date of the demerger. The Tribunal, thus, sustained the disallowance based on a case that was not even set up by the revenue.

iv. As regards disallowance under Section 14A of the Act read with Rule 8D of the Rules being partly allowed by the Tribunal was concerned, the same was assailed, on the following grounds.

a) The disallowance was based on the presumption that expenditure had been incurred in earning income which was exempt from tax.

b) The Tribunal failed to note that, the AO had to arrive at a satisfaction that expenditure was indeed incurred in earning income, which was exempt from tax. This is the *sine qua non* for application of the provisions of Section 14A of the Act. The AO failed to record any such satisfaction.

c) Since Rule 8D(iii) of the Rules came into force only from AY 2008-2009 onwards, the said rule could not have been applied in any case for affirming, *albeit* partly, disallowance for AY 2007-2008.

v. As far as the Tribunal's direction was concerned for the AY 2007-2008 that the one-time commuted/discounted lease rent aggregating to Rs. 77,98,042/- should be spread in equal proportion over the tenure of the lease i.e. 90 years, it was assailed on the following grounds.

a) The Tribunal failed to appreciate the ratio of the judgement of the Supreme Court in the case of ***Taparia Tools Ltd. vs. JCIT***, (2015) 372 ITR 605 (SC), which categorically held that, the Act did not recognise the concept of deferred revenue expenditure.

b) The Tribunal erred in travelling beyond the scope of the appeal before it and the case set up by the revenue, and thus, acted contrary to the mandate of Section 254 of the Act. The reasoning adopted by the Tribunal was not put to the appellant/assessee at the time of the hearing.

Submissions advanced on behalf of the revenue: -

7. On the other hand, Mr. Shailendra Singh relied upon the orders passed by the Tribunal. It was argued that the Tribunal had taken the correct view about the deduction claimed by the appellant/assessee under Section 35DD of the Act, the extent to which the disallowance was sustained, under Section 14A, as also the direction issued that the one-time lease rent paid by the appellant/assessee should be spread over the tenure of the lease, in equal proportion.

Analysis and reasons: -

8. Having heard counsel for the parties, although four substantial questions of law have been admitted, the issues which arise for consideration concern

three aspects. Therefore, we would be adjudicating the same, having in mind, the three issues that have arisen in the matter.

Deduction claimed under Section 35DD: -

9. The facts which have emerged vis-à-vis this issue and qua which there is no dispute are as follows.

i. An undertaking of NIIT Ltd. was spun off under the scheme of demerger approved by this Court. The demerger came into effect from 01.04.2003. The demerged entity vested in an existing company i.e. the appellant/assessee herein, formerly known as, NIIT Technologies Ltd.

ii. The appellant/assessee had incurred Rs. 2,20,03,694/- on legal and professional expenses in AY 2004-2005 for pursuing the scheme of demerger.

iii. The appellant/assessee had claimed deduction, in consonance with provisions of Section 35DD of the Act, of 1/5th of Rs. 2,20,03,694/-, i.e., Rs. 44,00,739/- for the first time in AY 2004-2005. Likewise, the said amount i.e. 1/5th of Rs. 2,20,03,694/- was claimed by the appellant/assessee in the subsequent years i.e. AYs 2005-2006 to 2008-2009. The claim was allowed only in AYs 2004-2005, 2005-2006 and 2006-2007.

iv. The AO disallowed the claim in the AYs in issue i.e. AYs 2007-2008 and 2008-2009 on the ground that, it could be claimed only in the hands of the demerged company i.e. NIIT Ltd. and not in the hands of the appellant/assessee i.e. NIIT Technologies Ltd. This view has been sustained both by CIT(A) as well as the Tribunal. The argument of the revenue is, that the provision in Section 35DD of the Act uses the expression "assessee" and not "assessees", and therefore, the deduction is available only in the hands of the demerged company in this case, i.e.

NIIT Ltd., and hence, cannot be claimed by the resulting company i.e. NIIT Technologies Ltd. i.e. the appellant/assessee.

v. Insofar as the submission made on behalf of the appellant/assessee, as regards revenue failing to adhere to the rule of consistency is concerned, the stand of the revenue is that, if an error has been committed, the same should not be perpetuated.

10. The Tribunal's view, as contained in paragraph 4.6 and 4.7, of the impugned order, is extracted hereafter.

> "4.5 We have heard the rival submission of the parties and perused the relevant material on record. As a result of demerger of units of parent company M/s NIIT Ltd , few units were merged with the assessee company. It is the claim of the assessee that legal and professional expenses towards the demerger of the units of parent company M/s NIIT Ltd has been incurred by the assessee in assessment year 2004-05 and 1/5th of said expenses has been claimed deduction under section 35DD of the Act since assessment year 2004-05 for consecutive five assessment years. According to the Revenue, the said deduction under section 35DD of the Act is allowable only to the parent demerged company and not to the resultant company i.e. the assessee company. For ready reference, the said provisions of section 35DD of the Act are reproduced as under:
>
> > "Amortisation of expenditure in case of amalgamation or demerger.
> >
> > 35DD. (1) Where an assessee, being an Indian company, incurs any expenditure, on or after the 1st day of April, 1999, wholly and exclusively for the purposes of amalgamation or demerger of an undertaking, the assessee shall be allowed a deduction of an amount equal to one-fifth of such expenditure for each of the five successive previous years beginning with the previous year in which the amalgamation or demerger takes place.
> >
> > (2) No deduction shall be allowed in respect of the expenditure mentioned in sub-section (1) under any other provision of this Act."
>
> 4.6 In the above section the deduction has been allowed to the "assessee" for expenditure incurred wholly and exclusively for demerger of an undertaking. Since demerger of the undertaking(s) in the instant case has taken place from the parent company M/s NIIT Ltd, the word "assessee" here refers to M/s NIIT Ltd. and not the target company M/s NIIT Technologies Ltd. i.e. the Assessee, with whom the undertakings of M/s NIIT Ltd. got merged. In our opinion the language of the section is clear and there is no ambiguity, as who is entitled to claim the said deduction. In case of demerger, where the undertaking(s) which get demerged, may result in new entity and in said

circumstances, the resultant company cannot incur expenditure before its birth. It is the parent entity, who initiates demerger of the undertaking(s) and incur expenditure for legal and professional expenses in relation to such demerger. The resultant company, come into existence as a result of demerger only, the word “assessee” in section 35DD of the Act cannot mean to include the resultant company. The decision relied upon by the assessee in the case of CIT Vs Bombay dyeing and manufacturing company limited (supra) relates to period prior to insertion of section 35DD of the Act, wherein the expenses related to amalgamation were allowed to the assessee as incurred wholly and exclusively for the purpose of the business of the assessee.. In the said case the issue was of whether the legal and professional expenses incurred in relation to the amalgamation were revenue or capital in nature. The ratio of the said decision cannot be applicable over the facts of the instant case in view of the specific provision of section 35DD of the Act introduced.

4.7 As far plea of rule of consistency is concerned, we may like to refer to the decision of the Hon’ble Supreme Court in the case of **Distributors (Baroda) P. Ltd. Vs. Union Of India & Ors. reported in 155 ITR 120**, where it is observed if any wrong has been committed, same should not be perpetuated. The relevant observations of the Hon’ble Supreme Court are reproduced as under:

> “28. But, even if, in our view, the decision in Cloth Traders' case (supra) is erroneous, the question still remains whether we should overturn it. Ordinarily, we would be reluctant to overturn a decision given by a Bench of this Court, because it is essential that there should be continuity and consistency in judicial decisions and law should be certain and definite. It is almost as important that the law should be settled permanently as that it should be settled correctly. But there may be circumstances where public interest demands that the previous decision be reviewed and reconsidered. The doctrine of stare decisis should not deter the Court from overruling an earlier decision, if it is satisfied that such decision is manifestly wrong or proceeds upon a mistaken assumption in regard to the existence or continuance of a statutory provision or is contrary to another decision of the Court. It was Jackson, J., who said in his dissenting opinion in Massachusetts vs. United States (333 US 611) : "I see no reason why I should be consciously wrong today because I was unconsciously wrong yesterday". Lord Denning also said to the same effect when he observed in Ostime vs. Australian Mutual Provident Society (1960) AC 459, 480 :
>
> "The doctrine of precedent does not compel your Lordships to follow the wrong path until you fall over the edge of the cliff." Here we find that there are overriding considerations which compel us to reconsider and review the decision in Cloth Traders' case (supra). In the first place, the decision in Cloth Traders' case (supra) was rendered by this Court on 4th May, 1979, and immediately thereafter, within a few months, Parliament introduced s. 80AA with retrospective effect from 1st April, 1968, with a view to overriding the interpretation placed on s. 80M in Cloth Traders' case (supra). The decision in Cloth Traders'

case (supra) did not, therefore, hold the field for a period of more than a few months and it could not be said that any assessee was misled into acting to its detriment on the basis of that decision. There was no decision of this Court in regard to the interpretation of sub- s. (1) of s. 80M prior to the decision in Cloth Traders' case (supra) and there was therefore no authoritative pronouncement of this Court on this question of interpretation on which an assessee could claim to rely for making its fiscal arrangements. The only decision in regard to the interpretation of sub-s. (1) of s. 80M given by any High Court prior to the decision in Cloth Traders' case (supra), was that of the Gujarat High Court in Addl. CIT vs. Cloth Traders P. Ltd. (supra) and that decision took precisely the same view which we are inclined to accept in the present case. It is, therefore, difficult to see how any assessee can legitimately complain that any hardship or inconvenience would be caused to it if the decision in Cloth Traders' case was overturned by us. If despite the decision of the Gujarat High Court in Addl. CIT vs. Cloth Traders P. Ltd. (supra), the assessee proceeded on the assumption, now found to be erroneous, that the Gujarat High Court decision was wrong and the deduction permissible under sub- s. (1) of s. 80M was liable to be calculated with reference to the full amount of dividend received by the assessee, the assessee can have only itself to blame. Knowing fully well that the Gujarat High Court had decided the question of interpretation of sub-s. (1) of s. 80M in favour of the Revenue and there was no decision of this Court taking a different view, no prudent assessee could have proceeded to make its financial arrangements on the basis that the decision of the Gujarat High Court was erroneous. Moreover, we find, for reasons we have already discussed, that the decision in Cloth Traders' case is manifestly wrong because it has failed to take into account a very vital factor, namely, that the deduction required to be made under sub-s. (1) of s. 80M is not from the gross total income but from "such income by way of dividends". There is also another circumstance which makes it necessary for us to reconsider and review the decision in Cloth Traders' case and that is the decision in Cambay Electric Supply Co.'s case (supra). The decision in Cloth Traders' case is inconsistent with that in Cambay Electric Supply Co.'s case. Both cannot stand together. If one is correct, the other must logically be wrong and vice versa. It is, therefore, necessary to resolve the conflict between these two decisions and harmonise the law and that necessitates an inquiry into the correctness of the decision in Cloth Traders' case. It is for this reason that we have reconsidered and reviewed the decision in Cloth Traders' case and on such reconsideration and review, we have come to the conclusion that the decision in Cloth Traders' case is erroneous must be overturned."

11. In our opinion, the view of the Tribunal is flawed for the following reasons.

11.1. Firstly, the Tribunal has failed to appreciate the various ways in which demerger takes place. A demerger is a legal device used, very often by assessees, to restructure their business operations. It is a process that is, in a sense, a merger in the reverse. Demerger can, ordinarily, take place in two ways i.e. by way of "spin-off" or by way of "split-off". A spin-off can take place in various ways, including by transferring, an undertaking/unit to a new or a subsidiary company, in which, shares are offered to the shareholders of the demerged company i.e. the original company. A Split-off occurs when the demerged entity segregates itself into various independent companies whereby the original or the parent company ceases to exist.

11.2. In this particular case, one of the undertakings of the demerged company i.e. NIIT Ltd. was transferred to another existing company i.e. NIIT Technologies Ltd./appellant/assessee. Thus, the resulting company, i.e. NIIT Technologies Ltd. was already in existence, and therefore, the argument that the deduction can be claimed only by the demerged company, which was in existence, and that the word “assessee” has been carefully used by the legislature, only to include the demerged company, is, misconceived. The legislature has used the word “assessee” having regard to the various ways in which the schemes are structured. Illustratively, two very broad mechanisms often used have been adverted to hereinabove.

11.3. Secondly, having regard to the fact that the deduction claimed by the appellant/assessee under the provisions of Section 35DD of the Act was allowed in the earlier AYs i.e. AY 2004-2005 to 2006-2007, the same should not have been disallowed in the AYs in issue i.e. 2007-2008 and 2008-2009 based on reasoning which does not comport with a plain reading of the provisions of Section 35DD of the Act, and the understanding of how a demerger scheme operates. The interpretation of such provisions should align, wherever possible,

with how ordinary men of commerce construe such business structuring operations.

11.4. Accordingly, the question of law no. (i), as framed in ITA 213/2020 and 214/2020, is answered in favour of the appellant/assessee and against the revenue.

Disallowance under Section 14A of the Act: -

12. The facts, as culled out above, would show that the disallowance under Section 14A of the Act has been considerably scaled down by the Tribunal by restricting it to administrative expense [expenses covered under Rule 8D(2)(iii) of the Rules] and, that too, to 0.5% of the value of the assets, which yielded income exempt from tax during the period under consideration. This issue concerns both, AY 2007-2008 and AY 2008-2009.

12.1. It is not in dispute that Rule 8D of Rules was made part of the Rules only on 24.03.2008, and therefore, could have impacted the concerned assessees, if at all, only in AY 2008-2009 and onwards. Furthermore, it is required to be noticed (something which is not disputed) that the appellant/assessee on its own, had triggered disallowance to the extent of 20% of the total expenses of the treasury division in AY 2007-2008; which was pegged at Rs. 5,62,842/-. The appellant/assessee, however, had earned in the same period, income by way of dividend amounting to Rs. 1,66,74,318/-, which was exempt from tax, via investment in various mutual funds.

12.2. In AY 2008-2009, the appellant/assessee, excluded, by way of disallowance, Rs. 7,79,063/-, being proportionate time-cost of designated employees making investments. This amount, according to the appellant/assessee, was duly verified and certified by its auditors. As against this, the appellant/assessee had earned income by way of dividend which was

exempt from tax, via investments in fully paid equity shares of NIIT GIS Ltd. and mutual funds units, aggregating to Rs. 38,63,71,350/-.

12.3. The authorities below triggered the provisions of Rule 8D of the Rules even for AY 2007-2008 when the same came into force only in AY 2008-2009. [See ***Godrej & Boyce Mfg. Co. Ltd. vs. DCIT, Mumbai & Anr.*** (2017) 394 ITR 449 (SC) and ***CIT vs. Essar Teleholdings Ltd.***[1] **(2018)** 401 ITR 445 (SC)]

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[1]"***Important principles of statutory interpretation***

22. The legislature has plenary power of legislation within the fields assigned to them; it may legislate prospectively as well as retrospectively. It is a settled principle of statutory construction that every statute is prima facie prospective unless it is expressly or by necessary implications made to have retrospective operations. Legal maxim *nova constitutio futuris formam imponere debet non praeteritis* i.e. a new law ought to regulate what is to follow, not the past, contain a principle of presumption of prospectivity of a statute.

23. Justice G.P. Singh in *Principles of Statutory Interpretation* (14th Edn. in Chapter 6), while dealing with operation of fiscal statute, elaborates the principles of statutory interpretation in the following words:

> "Fiscal legislation imposing liability is generally governed by the normal presumption that it is not retrospective and it is a cardinal principle of the tax law that the law to be applied is that in force in the assessment year unless otherwise provided expressly or by necessary implication. The above rule applies to the charging section and other substantive provisions such as a provision imposing penalty and does not apply to machinery or procedural provisions of a taxing Act which are generally retrospective and apply even to pending proceedings. But a procedural provision, as far as possible, will not be so construed as to affect finality of tax assessment or to open up liability which had become barred. Assessment creates a vested right and an assessee cannot be subjected to reassessment unless a provision to that effect inserted by amendment is either expressly or by necessary implication retrospective. A provision which in terms is retrospective and has the effect of opening up liability which had become barred by lapse of time, will be subject to the rule of strict construction. In the absence of a clear implication, such a legislation will not be given a greater retrospectivity than is expressly mentioned; nor will it be construed to authorise the Income Tax Authorities to commence proceedings which, before the new Act came into force, had by the expiry of the period then provided, become barred. But unambiguous language must be given effect to, even if it results in reopening of assessments which had become final after expiry of the period earlier provided for reopening them. There is no fixed formula for the expression of legislative intent to give retrospectivity to a taxation enactment. …"

24. A three-Judge Bench of this Court in *Govind Das* v. *CIT* [*Govind Das* v. *CIT*, (1976) 1 SCC 906 : 1976 SCC (Tax) 133] , noticing the settled rules of interpretation laid down following in para 11: (SCC pp. 914-15)

> "*11*. Now it is a well-settled rule of interpretation hallowed by time and sanctified by judicial decisions that, unless the terms of a statute expressly so provide or necessarily require it, retrospective operation should not be given to a statute so as to take away or

impair an existing right or create a new obligation or impose a new liability otherwise than as regards matters of procedure. The general rule as stated by Halsbury in Vol. 36 of *Laws of England* (3rd Edn.) and reiterated in several decisions of this Court as well as English courts is that

'all statutes other than those which are merely declaratory or which relate only to matters of procedure or of evidence are prima facie prospective and retrospective operation should not be given to a statute so as to affect, alter or destroy an existing right or create a new liability or obligation unless that effect cannot be avoided without doing violence to the language of the enactment. If the enactment is expressed in language which is fairly capable of either interpretation, it ought to be construed as prospective only'.

If we apply this principle of interpretation, it is clear that sub-section (6) of Section 171 applies only to a situation where the assessment of a Hindu Undivided Family is completed under Section 143 or Section 144 of the new Act. It can have no application where the assessment of a Hindu Undivided Family is completed under the corresponding provisions of the old Act. Such a case would be governed by Section 25-A of the old Act which does not impose any personal liability on the members in case of partial partition and to construe sub-section (6) of Section 171 as applicable in such a case with consequential effect of casting of the members' personal liability which did not exist under Section 25-A, would be to give retrospective operation to sub-section (6) of Section 171 which is not warranted either by the express language of that provision or by necessary implication. Sub-section (6) of Section 171 can be given full effect by interpreting it as applicable only in a case where the assessment of a Hindu Undivided Family is made under Section 143 or Section 144 of the new Act. We cannot, therefore, consistently with the rule of interpretation which denies retrospective operation to a statute which has the effect of creating or imposing a new obligation or liability, construe sub-section (6) of Section 171 as embracing a case where assessment of a Hindu Undivided Family is made under the provisions of the old Act. Here in the present case, the assessments of the Hindu Undivided Family for Assessment Years 1950-1951 to 1956-1957 were completed in accordance with the provisions of the old Act which included Section 25-A and the Income Tax Officer was, therefore, not entitled to avail of the provision enacted in sub-section (6) read with sub-section (7) of Section 171 of the new Act for the purpose of recovering the tax or any part thereof personally from any members of the joint family including the petitioners."

xxx **xxx** **xxx**

45. The Constitution Bench in *CIT* v. *Vatika Township (P) Ltd.* [*CIT* v. *Vatika Township (P) Ltd.*, (2015) 1 SCC 1] , after noticing the principle of statutory interpretation, as noted above, has laid down the following in paras 36, 37 and 39: (SCC p. 25)

"*36.* In *CIT* v. *Scindia Steam Navigation Co. Ltd.* [*CIT* v. *Scindia Steam Navigation Co. Ltd.*, AIR 1961 SC 1633] , this Court held that as the liability to pay tax is computed according to the law in force at the beginning of the assessment year i.e. the first day of April, any change in law affecting tax liability after that date though made during the currency of the assessment year, unless specifically made retrospective, does not apply to the assessment for that year.

Answer to the reference

37. When we examine the insertion of the proviso in Section 113 of the Act, keeping in view the aforesaid principles, our irresistible conclusion is that the intention of the

legislature was to make it prospective in nature. This proviso cannot be treated as declaratory/statutory or curative in nature.

***

Reasons in support

39. The first and foremost poser is as to whether it was possible to make the block assessment with the addition of levy of surcharge, in the absence of proviso to Section 113? In *Suresh N. Gupta* [*CIT* v. *Suresh N. Gupta*, (2008) 4 SCC 362] itself, it was acknowledged and admitted that the position prior to the amendment of Section 113 of the Act whereby the proviso was added, whether surcharge was payable in respect of block assessment or not, was totally ambiguous and unclear. The Court pointed out that some assessing officers had taken the view that no surcharge is leviable. Others were at a loss to apply a particular rate of surcharge as they were not clear as to which the Finance Act, prescribing such rates, was applicable. It is a matter of common knowledge and is also pointed out that the surcharge varies from year to year. However, the assessing officers were indeterminative about the date with reference to which rates provided for in the Finance Act were to be made applicable. They had four dates before them viz.: (*Suresh N. Gupta case* [*CIT* v. *Suresh N. Gupta*, (2008) 4 SCC 362] , SCC p. 379, para 35)

(*i*) Whether surcharge was leviable with reference to the rates provided for in the Finance Act of the year in which the search was initiated; or

(*ii*) the year in which the search was concluded; or

(*iii*) the year in which the block assessment proceedings under Section 158-BC of the Act were initiated; or

(*iv*) the year in which block assessment order was passed."

46. As noted above, that Rule 8-D has again been amended by the Income Tax (Fourteenth Amendment) Rules, 2016 w.e.f. 2-6-2016, by which Rule 8-D sub-rule (2) has been substituted by a new provision which is to the following effect:

"**8-D. (2)** The expenditure in relation to income which does not form part of the total income shall be the aggregate of following amounts, namely—

(*i*) the amount of expenditure directly relating to income which does not form part of total income; and

(*ii*) an amount equal to one per cent of the annual average of the monthly average of the opening and closing balances of the value of investment, income from which does not or shall not form part of total income:

Provided that the amount referred to in clause (*i*) and clause (*ii*) shall not exceed the total expenditure claimed by the assessee."

47. The method for determining the amount of expenditure brought in force w.e.f. 24-3-2008 has been given a go-by and a new method has been brought into force w.e.f. 2-6-2016, by interpreting Rule 8-D retrospective, there will be a conflict in applicability of 5th & 14th Amendment Rules which clearly indicates that the Rule has a prospective operation, which has been prospectively changed by adopting another methodology.

48. One of the submissions raised by the learned counsel for the assessee also needs to be noticed. The learned counsel for the assessee submits that it is well settled that subordinate legislation ordinarily is not retrospective unless there are clear indication to the same. Reliance has been placed on the judgment of this Court in *State of Jharkhand* v. *Shiv*

12.4. Furthermore, though the Tribunal has restricted the disallowance to administrative expenditure, and that too, is pegged at 0.5% for the value of investments, which gave rise to income that was exempt from tax, it failed to examine as to whether the provisions of Section 14A of the Act were, in the first

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Karampal Sahu [*State of Jharkhand* v. *Shiv Karampal Sahu*, (2009) 11 SCC 453 : (2009) 2 SCC (L&S) 640] . In para 17, following has been stated: (SCC pp. 459-60)

> "*17.* Ordinarily, a subordinate legislation should not be construed to be retrospective in operation. The Circular Letter dated 7-5-2003 was given a prospective effect. The father of the respondent died on 19-5-2000. There is nothing to show that even the Circular dated 9-8-2000 had been given retrospective effect. In any view of the matter, as the State of Jharkhand in the Circular Letter dated 7-5-2003 adopted the earlier circular letters issued by the State of Bihar only in respect of cases where death had occurred after 15-10-2000 i.e. the date from which the State of Jharkhand came into being, the High Court [*Shiv Kampal Sahu* v. *State of Jharkhand*, 2005 SCC OnLine Jhar 507 : (2006) 2 AIR Jhar R 148] , in our opinion, committed a serious error in giving retrospective effect thereto indirectly which it could not do directly. Reasons assigned by the High Court, for the reasons aforementioned, are unacceptable."

There is no indication in Rule 8-D to the effect that Rule 8-D intended to apply retrospectively.

49. Applying the principles of statutory interpretation for interpreting retrospectivity of a fiscal statute and looking into the nature and purpose of sub-section (2) and sub-section (3) of Section 14-A as well as purpose and intent of Rule 8-D coupled with the Explanatory Notes in the Finance Bill, 2006 and the Departmental understanding as reflected by Circular dated 28-12-2006, we are of the considered opinion that Rule 8-D was intended to operate prospectively.

50. It is relevant to note that the impugned judgment [*CIT* v. *Essar Teleholdings Ltd.*, 2011 SCC OnLine Bom 2016] in this appeal relies on the earlier judgment of the Bombay High Court in *Godrej & Boyce Mfg. Co. Ltd.* v. *CIT* [*Godrej & Boyce Mfg. Co. Ltd.* v. *CIT*, 2010 SCC OnLine Bom 1174 : (2010) 328 ITR 81] , where the Division Bench of the Bombay High Court after elaborately considering the principles to determine the prospectivity or retrospectivity of the amendment has concluded that Rule 8-D is prospective in nature. Against the aforesaid judgment of the Bombay High Court dated 12-8-2010 [*Godrej & Boyce Mfg. Co. Ltd.* v. *CIT*, 2010 SCC OnLine Bom 1174 : (2010) 328 ITR 81] an appeal was filed in this Court which has been decided vide its judgment in *Godrej & Boyce Mfg. Co. Ltd.* v. *CIT* [*Godrej & Boyce Mfg. Co. Ltd.* v. *CIT*, (2017) 7 SCC 421] . This Court, while deciding the above appeal, repelled the challenge raised by the assessee regarding vires of Section 14-A. In para 36 of the judgment, this Court noticed that with regard to retrospectivity of provisions Revenue had filed appeal, hence the said question was not gone into the aforesaid appeal. In the above case, this Court specifically left the question of retrospectivity to be decided in other appeals filed by the Revenue. We thus have proceeded to decide the question of retrospectivity of Rule 8-D in these appeals.

51. In view of our opinion as expressed above, dismissal of the appeal by the Bombay High Court is fully sustainable. As held above, Rule 8-D is prospective in operation and could not have been applied to any assessment year prior to Assessment Year 2008-2009."

place, applicable, to the facts and circumstances arising in the present case. The Tribunal's view, as contained in paragraph 6 and 6.1 of the impugned order, is extracted hereafter.

> "**6.** Regarding the administrative expenses for earning the exempt income is concerned, we find that Hon'ble Delhi in the case of ACB India Ltd. (supra) and the Special Bench in the case of ACIT Vs Vireet Investment Private Limited (supra) has held it for considering disallowance towards administrative expenses, the investment which has yielded exempt income during the year under consideration should only be considered.
> **6.1** The assessee before the Ld. CIT(A) has accepted 20% of the certain expenses towards salary etc. of employees engaged in investment activity. Thus, the contention of the assessee that no expenses have been incurred for earning the exempt income is not acceptable and some expenses on salary, rent and other office expenses definitely goes toward earning of the exempt income. In absence of any bifurcations of the expenses, a reasonable estimate has to be made for such disallowance. Respectfully, following the decision of the Hon'ble Delhi High Court in the case of ACB India Ltd (supra) and special bench Tribunal in the case of Vireet Private Limited (supra), we direct the Assessing Officer to restrict the disallowance at 0.5 % of the value of assets which has yielded exempt income during the year under consideration. The ground of the appeal of the assessee is accordingly partly allowed."

12.5. As would be evident, the Tribunal's reasoning is based on an approach where it assumes that no income can be earned without incurring expenditure; the assessee (in this case, the appellant/assessee) is not required to segregate expenditure, in its account (we would assume administrative expenditure); the onus is on the appellant/assessee to show that no expenditure has been incurred; and lastly, since disallowance has been made by the AO, it is obvious that he was not satisfied with the correctness of the claim made by the appellant/assessee in respect of such expenditure incurred to earn income exempt from tax.

12.6. To understand this line of reasoning, it would be apposite to extract the relevant part of Section 14A of the Act.

> "[Expenditure incurred in relation to income not includible in total income.
>
> 14A. [(1)] For the purposes of computing the total income under this Chapter, no deduction shall be allowed in respect of expenditure incurred by the assessee in relation to86 income which does not form part of the total income under this Act.]

> [(2) The Assessing Officer shall determine the amount of expenditure incurred in relation to such income which does not form part of the total income under this Act in accordance with such method as may be prescribed, if the Assessing Officer, having regard to the accounts of the assessee, is not satisfied with the correctness of the claim of the assessee in respect of such expenditure in relation to income which does not form part of the total income under this Act.
>
> (3) The provisions of sub-section (2) shall also apply in relation to a case where an assessee claims that no expenditure has been incurred by him in relation to income which does not form part of the total income under this Act :]
>
> [Provided that nothing contained in this section shall empower the Assessing Officer either to reassess under section 147 or pass an order enhancing the assessment or reducing a refund already made or otherwise increasing the liability of the assessee under section 154, for any assessment year beginning on or before the 1st day of April, 2001.]"

12.7. A careful perusal of Section 14A(2) of the Act would show that the AO is required to make a determination of the expenditure incurred, concerning the income which does not form part of the total income, if the AO is not satisfied, having regard to the accounts of the assessee, as to the correctness of claims made by the assessee about such expenditure.

12.8. Sub-section 3 of Section 14A of the Act makes it clear that the parameters stipulated in the said provision will also apply where the assessee claims that no expenditure has been incurred by him concerning income that doesn't form part of the total income under the Act.

13. Therefore, what emerges is, if the assessee claims a certain amount of expenditure was incurred by him to earn the income which does not form part of the total income, the AO is required to examine the accounts, and thus, satisfy himself as to the correctness of the claim made by the assessee about the expenditure incurred in that regard. It is when an AO is not satisfied as to the correctness of the claim made by the assessee, about the expenditure said to have been incurred by him on such income which does not form part of the total income under the Act, he then proceeds to determine the amount of expenditure, by following such method as is prescribed, i.e., Rule 8D of the Rules.

13.1. This methodology, as envisaged under Rule 8D of the Rules, is required to be followed even where the assessee claims that no expenditure was incurred by him concerning income which does not form part of the total income under the Act.

13.2. The approach of the Tribunal has been that, since a disallowance was made, it follows logically, that the AO was not satisfied. This, according to us, is not what is envisaged under the provisions of Section 14A of the Act. The satisfaction has to be arrived at by the AO having regard to the assessee's accounts and not otherwise. Concededly, there is nothing in the record to suggest that the AO examined the accounts from this perspective.

13.3. Furthermore, in our view, because the appellant/assessee had itself offered an amount which could be disallowed under Section 14A of the Act, the onus shifted onto the revenue to ascertain, after examination of the accounts, as to whether or not the appellant's/assessee's claim was correct. It is only after the aforesaid exercise was conducted, could the AO have taken recourse to the prescribed method i.e. Rule 8D of the Rules, for determining the expenditure, which, according to him, needed to be disallowed under Section 14A of the Act.

13.4. We would assume, for the moment, that the revenue could take recourse to Rule 8D of the Rules in both AYs, i.e. 2007-2008 and 2008-2009, although, as indicated above, it could have been triggered perhaps only in AY 2008-2009.

13.5. Given the aforesaid position, we are of the view that the Tribunal in calculating the disallowance as per the provisions of Rule 8D(2)(iii) of the Rules was not in order. In this context, the observations made by a division bench of this Court in ***H.T. Media Ltd. vs. Pr. CIT*** (2017) 399 ITR 576 (Del), being apposite, are extracted hereafter.

"***Failure of the AO to record satisfaction***

32. The question regarding the failure of the AO to record his dissatisfaction with the correctness of the Assessee's claim regarding administrative expenses of Rs. 3 lakhs arises in ITA 349 of 2015. Mr Raghvendra Singh is not entirely right in his submission that there is no question framed about the failure by the AO to record his satisfaction. In ITA 349 of 2015, the question framed by this Court by the order dated 15th October 2015 is in fact in two parts: viz., (i) Whether the AO recorded a proper satisfaction in terms of Section 14A (2) and Rule 8 (D) of the Rules and (ii) in calculating the disallowance at 0.5% of average value of investments as per clause (iii) of Rule 8 D (2) of the Rules?

33. The contention of Mr. Singh is that if there was a valid recording of satisfaction by the AO as required by Rule 8D (1), then there was no option available to the AO other than to apply Rule 8D (2) of the Rules. Therefore, even according to the Revenue, the applicability of Rule 8D (2) hinges on the recording of the AO in terms of Rule 8D (1) that he was not satisfied with the Assessee's claim regarding expenditure incurred to earn the exempt income.

34. The Assessee had explained that Rs. 3 lakhs was being disallowed voluntarily as an "expenditure which could be attributable for earning the said income." The Assessee explained that the disallowance had been determined on the basis of cost of finance department in the ratio of exempt income to total turnover. On that basis the disallowance in AY 2005-06 was upheld by CIT (A) at Rs. 1 lakh. The disallowance for this AY was worked out as Rs. 1,42,404/- and since the Assessee had already made a disallowance of Rs. 3 Lacs, no further disallowance was called for.

35. In order to disallow this expense the AO had to first record, on examining the accounts, that he was not satisfied with the correctness of the Assessee's claim of Rs. 3 lakhs being the administrative expenses. This was mandatorily necessitated by Section 14 A (2) of the Act read with Rule 8D (1) (a) of the Rules.

36. In para 3.2 of the assessment order, the AO records that, in answer to the query posed by the AO requiring it to produce calculation for disallowances, the Assessee "submitted that they have not incurred any expenditure for earning the dividend income." Thereafter, in para 3.3, the AO records "I have considered the submissions of the Assessee and found not to be acceptable." Thereafter, the AO proceeded to deal with the said provisions of Section 14A and Rule 8D and observed, in para 3.3.1, that making of investment, maintaining or continuing investment and time of exit from investment are well informed and well coordinated management decisions that, in relation to earning of income, are embedded in indirect expenses. It is then stated in para 3.4 that, in view of the above, the provisions of sub-section (2) of Section 14A and Rule 8D of the Rules are in operation and therefore, will strictly be adhered to by the Assessee. In para 3.6 of the assessment order, after discussing Section 14A(1) read with Rule 8D and referring to the decision of the Bombay High Court in ***Godrej and Boyce Mfg. Co. Ltd v. DCIT*** [2017] 394 ITR 449 (SC) , the AO simply stated that "in view of the facts and circumstances and legal position on the issue as discussed above, I am satisfied that the Assessee had incurred expenses to manage its investments which may yield exempt income, and Assessee grossly failed to calculate such expenses in a reasonable manner to ascertain to ascertain the true and correct picture of its income and expenses."

37. In the considered view of this Court, the above observations of the AO in the assessment order are of a broad general nature not with particular reference to the facts of the case on hand.

38. The Court is also unable to agree with Mr. Singh that on this aspect there are concurrent findings of both the CIT (A) as well as the ITAT. The CIT (A) disallowed the exempt expenses by merely repeating what the AO had stated about the cost that is built into so called 'passive' investments and simply recorded that the AO was bound to Rule 8D and, therefore, was justified in determining administrative costs at 0.5%. Here again, the CIT (A) failed to note that without the mandatory requirement, under Section 14A of the Act and Rule 8D of the Rules, of satisfaction being recorded being met, the question of applying Rule 8D (1) did not arise.

39. Turning now to the order of the ITAT, in para 33, it recorded the submission of the AR that the AO did not record any satisfaction about the Assessee not properly offering expenditure incurred in relation to the exempt income at Rs. 3 lakhs. The ITAT reproduced the contents of para 3.3.1 of the assessment order, which has been extracted by this Court hereinbefore, which contains general observations regarding earning of exempt income. This cannot be accepted as a recording by the AO of satisfaction regarding the claim of the Assessee after examining its accounts. Again, in para 34 of its order, the ITAT simply reproduced para 3.3.6 of the assessment order where, again, no reasons have been provided but only a conclusion has been reached that the AO was "satisfied that the Assessee had incurred expenses to manage its investments which may yield exempt income, and Assessee grossly failed to calculate such expenses in a reasonable manner to ascertain the true and correct picture of its income and expenses."

40. Consequently on the aspect of administrative expenses being disallowed, since there was a failure by the AO to comply with the mandatory requirement of Section 14 A (2) of the Act read with Rule 8D (1) (a) of the Rules and record his satisfaction as required thereunder, the question of applying Rule 8D (2) (iii) of the Rules did not arise. The question framed in ITA 549 of 2015 is answered accordingly."

13.6. Thus, having regard to the aforesaid, the question of law no. (ii), as framed in ITA 213/2020 and 214/2020, is also decided in favour of the appellant/assessee and against the revenue.

Commuted/discounted one-time lease rent: -

14. It is relevant to note that, vis-à-vis this aspect of the matter, while the Tribunal has agreed with the appellant/assessee, the one-time lease rent was incurred by it to run its business both, effectively and efficiently, the Tribunal has gone on to hold that the amount involved should be spread over the tenure of the lease, albeit, in equal proportion. The reasoning of the Tribunal is given in paragraph 9.6 to 9.9 of the impugned orders; the same is extracted hereafter.

"9.6 We have heard the rival submission and perused the relevant material on record. The assessee has filed a copy of the lease deed under reference. In terms of the lease deed, the assessee has made following payments to GNIDA:

(a) one-time lease premium of ₹ 2,83,56,515/-

(b) commuted one time lease rent of ₹ 77,98,042/-

9.7 As far as payment of one-time lease premium is concerned, the assessee has capitalized the said amount in its books of accounts. The Ground No. 4 of the appeal of the Revenue is factually incorrect because the premium has already been capitalized by the assessee and the issue in dispute is only in respect of the commuted one timely lease rent.

9.8 The Ld. CIT(A) after considering the decisions on the issue of when a particular expenditure has to be considered as capital expenditure, in the case of Empire Jute Co. Vs CIT 124 ITR 1 (SC); Lakshmiji Sugar Mills Co P Ltd Vs CIT 82 ITR 376 (SC) and Madras Auto Services (P) Ltd 233 ITR 468 (SC) allowed the claim of the assessee observing as under:

> *"8.5.2 The appellant submitted that it had claimed deduction of Rs.77,98,042 on account of payment of commuted lease rentals to Greater Noida Authority for Plot No. 2A taken on lease situated in Greater Noida Industrial Development Area District, Gautam Budh Nagar. The appellant had the option to either pay (a) the advance annual rent on yearly basis ; or (b) commuted one time lease rent for the period of lease and no lease rent would be payable by the appellant during the lease period. The appellant opted for option (b). The deed of lease was executed on 12th January, 2007. The lease term is of 90 years commencing from 12th January, 2007, with the right of the Greater Noida Industrial Development Authority reserved. It is submitted that the appellant under the lease deed with the Greater Noida Industrial Development Authority has agreed to develop SEZ in Greater Noida by constructing the project with integrated, ready to use office space and land and social infrastructure, etc. The appellant is obligated under the lease deed to complete the construction of the whole project and facilities within 7 years. It is submitted that the object and purpose of such lease deed, is only to facilitate IT Industries and IT enabled services and expansion of the business of the appellant. That apart from the aforesaid benefit, which is in the revenue field, there is no advantage in the capital field as there is no acquisition of any capital asset inasmuch the plot of land is not under the ownership of the appellant and remains the property of Greater Noida Industrial Development Authority. It is submitted that payment of commuted lease rentals did not result in creation of a capital asset having enduring benefit in the capital field. The amount in question was essentially revenue expenditure allowable deduction.*
>
> *8.5.3 Hon'ble Supreme Court in the case of Empire Jute Co. v CIT: 124 ITR 1, held that the test of enduring benefit is not certain or conclusive test in determining whether the expenditure is capital or revenue in nature and it cannot be applied blindly and mechanically without regard to the particular facts and circumstances of a given case. The Supreme Court further laid down that what is material to consider is the nature of the advantage in a commercial sense and it is only where the advantage is in the capital field that the expenditure would be disallowable on an application of this test. If the advantage consists merely in facilitating the assessee's trading operations or enabling the management and conduct of the assessee's business to be carried*

on more efficiently or more profitably while leaving the fixed capital untouched, the expenditure would be on revenue account, even though the advantage may endure for an indefinite future.

8.5.4 In the case of Lakshmiji Sugar Mills Co. P. Ltd. v. CIT : 82 ITR 376, Hon'ble Supreme Court held that the contribution made by the assessee under a statutory obligation for the development of roads which were originally the property of the Government and remained so even after the improvement had been done, being expenditure incurred for running of the business efficiently and conveniently and not for acquiring a capital asset was of revenue nature and not of a capital nature.

8.5.5 In the case of Madras Auto Service (P) I imited (233 ITR 468) the assessee tenant had spent the amounts in question in order to construct a new building after demolishing the old building. The new building, however, from inception was to belong to the lessor and not to the assessee. The assessee, however, had the benefit of the existing lease in respect of the new building at the agreed rent for a period of 39 years The assessee claimed deduction for the entire amount spent on construction of the building as revenue expenditure. Hon'ble Supreme Court in the said case observed:

> "In order to decide whether this expenditure is revenue expenditure or capital expenditure, one has to look at the expenditure from a commercial point of view. What advantage did the assessee get by constructing a building which belonged to somebody else and spending money for such construction? The assessee got a long lease of a newly constructed building suitable to its own business at a very concessional rent. The expenditure, therefore, was made in order to secure a long lease of new and more suitable business premises at a lower rent. In other words, the assessee made substantial savings in monthly rent for a period of 39 years by expending these amounts. The saving in expenditure was a saving in revenue expenditure in the form of rent. Whatever substitutes for revenue expenditure should normally be considered as revenue expenditure. Moreover, the assessee in the present case did not get any capital asset by spending the said amounts The assessee, therefore, could not have claimed any depreciation. Looking to the nature of the advantage which the assessee obtained in a commercial sense, the expenditure appears to be revenue expenditure."

8.5.6 The above decisions of Apex Court are squarely applicable in the case of the appellant. In the case of the appellant, also it did not acquire title / ownership of any capital asset. The plot of land on which construction would be carried on by the appellant under the lease deed of 99 years, would remain the property of Greater Noida Industrial Development Authority at all times. In lieu of incurring the expenditure, the appellant would be entitled to enjoy the property as a tenant under long term lease. Such an advantage even though, enduring in nature, could not be regarded as in the capital field as the expenditure only facilitates the carrying out of business more efficiently and profitably by making available suitable premises for the business of the appellant. The expenditure on account of commuted lease rentals paid by the appellant company has been incurred in respect of premises used wholly and exclusively for the purposes of the business of the company; and the same represents commuted payment in lieu of regular lease rental and hence is in

the nature of revenue expenditure. In view of the above, the AO has erred in making the disallowance of the commuted lease rentals. The appeal is allowed in this ground no. 7 of appeal. Since appeal is allowed in ground no. 7 of appeal, therefore, the plea of the appellant in ground no. 8 of appeal is infructuous and not necessary to be adjudicated."

9.9 We find that the Ld. CIT(A) has distinguished the expenditure in the capital field and expenditure incurred only to facilitate the carrying of the business more efficiently and profitably, which is revenue in nature. The one-time premium paid by the assessee has already been considered by the assessee as capital expenditure. The assessee had the option to pay the lease rental on year-to-year basis or as a one-time expenditure. The assessee has substituted the revenue expenditure which was to be paid on year-to-year basis and the nature of the expenditure remained same though it has been paid as a composite payment. Thus, it is clear that the expenditure incurred by the assessee is not capital expenditure. The expenditure was to be incurred on year to year basis for the period of lease of 90 years. The lesser gave the assessee two option. The first option was to pay on year to year basis and claim the same as revenue expenditure. The second option was provided by the lessor was to pay a composite amount for the period of lease as onetime payment. The lessor provided some benefit for making onetime payment. The assessee has chosen the second option and paid the entire lease rent of 90 years as composite onetime payment. Thus, in our opinion, the liability of 90 years has been paid in one year only. In such circumstances, the liability of lease rent relatable to year under consideration would be 1/90th of the amount paid and balance amount would be pre-paid advance rent only. The assessee is entitled to claim 1/90th of the amount every year till the period of lease of 90 years as revenue expenditure. Even according to the matching principles of income and expenditure the entire expenditure is not justified for allowance in one year (i.e. the year under consideration) when the income corresponding to expenditure of subsequent years will be reflected in relevant year only. **The expenditure not being relatable to the year under consideration cannot be allowed as revenue expenditure in the instant year. For the year under consideration, only 1/90th of the amount of Rs.77,98,042/- has been incurred wholly and exclusively for the purposes of the business for the year under consideration.** Accordingly, we allow 1/90th of Rs.77,98,042/- as revenue expenditure in the year and balance be characterized as advance rent in the financial statement as on 31.03.2007. Accordingly, the Ground Nos. 3 & 4 of the appeal of the Revenue are partly allowed."

[Emphasis is ours]

14.1. As is evident from the reasoning adopted by the Tribunal, the Tribunal while finding no difficulty with the stand of the appellant/assessee that, although, paying commuted and discounted one-time lease rent gave the appellant/assessee an enduring benefit, it allowed the appellant/assessee to run its business effectively.

14.2. Having said that the Tribunal, in our opinion, needlessly went on to direct that the amount incurred i.e. Rs. 77,98,042/- should be spread equally over the tenure of the lease. As correctly argued on behalf of the appellant/assessee, this was not the stand of the revenue before the Tribunal. The stand of the revenue was that the one-time lease rent amount paid to GNIDA was capital expenditure and not that it needed to be deferred over the tenure of the lease. As has been correctly argued on behalf of the appellant/assessee, there is no concept of deferred revenue expenditure under the Act. An expenditure can be spread over a time span, only if it so provided, in the Act. Section 35DD of the Act, which we have discussed above, is one such example. The observations of the Supreme Court in ***Taparia Tools Ltd. vs. JCIT***, (2015) 372 ITR 605 (SC), being relevant in this regard, are extracted for the sake of convenience.

> "14. The High Court has also observed that it was a case of deferred interest option. Here again, we do not agree with the High Court. **It has been explained in various judgments that there is no concept of deferred revenue expenditure in the Act except under specified sections, i.e. where amortization is specifically provided, such as Section 35-D of the Act**.
>
> (Emphasis is ours)
>
> 15. What is to be borne in mind is that the moment [the] second option was exercised by the debenture holder to receive the payment upfront, liability of the assessee to make the payment in that very year, on exercising of this option, has arisen and this liability was to pay the interest @ Rs. 55 per debenture. In Bharat Earth Movers v. CIT [2000] 245 ITR 428/112 Taxman 61 (SC), this Court had categorically held that if a business liability has arisen in the accounting year, the deduction should be allowed even if such a liability may have to be quantified and discharged at a future date. Following passage from the aforesaid judgment is worth a quote:
>
> > "**The law is settled: if a business liability has definitely arisen in the accounting year, the deduction should be allowed although the liability may have to be quantified and discharged at a future date. What should be certain is the incurring of the liability. It should also be capable of being estimated with reasonable certainty though the actual quantification may not be possible. If these requirements are satisfied the liability is not a contingent one. The liability is in praesenti though it will be discharged at a future date. It does not make any difference if the future date on which the liability shall have to be disharged is not certain.**"
>
> (Emphasis is ours)

The present case is even on a stronger footing inasmuch as not only the liability had arisen in the assessment year in question, it was even quantified and discharged as well in that very accounting year.

16. Judgment in ***Madras Industrial Investment Corpn. Ltd. v. CIT*** [1997] 225 ITR 802/91 Taxman 340 (SC) was cited by the learned counsel for the Revenue to justify the decision taken by the courts below. We find that the Court categorically held even in that case that the general principle is that ordinarily revenue expenditure incurred wholly and exclusively for the purpose of business is to be allowed in the year in which it is incurred. However, some exceptional cases can justify spreading the expenditure and claiming it over a period of ensuing years. It is important to note that in that judgment, it was the assessee who wanted spreading the expenditure over a period of time and had justified the same. It was a case of issuing debentures at discount; whereas the assessee had actually incurred the liability to pay the discount in the year of issue of debentures itself. The Court found that the assessee could still be allowed to spread the said expenditure over the entire period of five years, at the end of which the debentures were to be redeemed. By raising the money collected under the said debentures, the assessee could utilise the said amount and secure the benefit over number of years. This is discernible from the following passage in that judgment on which reliance was placed by the learned counsel for the Revenue herself:

> "15.. The Tribunal, however, held that since the entire liability to pay the discount had been incurred in the accounting year in question, the assessee was entitled to deduct the entire amount of Rs.3,00,000 in that accounting year. This conclusion does not appear to be justified looking to the nature of the liability. It is true that the liability has been incurred in the accounting year. But the liability is a continuing liability which stretches over a period of 12 years. It is, therefore, a liability spread over a period of 12 years. Ordinarily, revenue expenditure which is incurred wholly and exclusively for the purpose of business must be allowed in its entirety in the year in which it is incurred. It cannot be spread over a number of years even if the assessee has written it off in his books over a period of years. However, the facts may justify an assessee who has incurred expenditure in a particular year to spread and claim it over a period of ensuing years. In fact, allowing the entire expenditure in one year might give a very distorted picture of the profits of a particular year. Thus in the case of Hindustan Aluminium Corporation Ltd. vs. CIT, (1982) 30 CTR (Cal) 363: (1983) 144 ITR 474 (Cal) the Calcutta High Court upheld the claim of the assessee to spread out a lump sum payment to secure technical assistance and training over a number of years and allowed a proportionate deduction in the accounting year in question.
>
> 16. Issuing debentures at a discount is another such instance where, although the assessee has incurred the liability to pay the discount in the year of issue of debentures, the payment is to secure a benefit over a number of years. There is a continuing benefit to the business of the company over the entire period. The liability should, therefore, be spread over the period of the debentures."

17. Thus, the first thing which is to be noticed is that though the entire expenditure was incurred in that year, it was the assessee who wanted the spread over. The Court was conscious of the principle that normally revenue expenditure is to be allowed in

the same year in which it is incurred, but at the instance of the assessee, who wanted spreading over, the Court agreed to allow the assessee that benefit when it was found that there was a continuing benefit to the business of the company over the entire period.

18. What follows from the above is that normally the ordinary rule is to be applied, namely, revenue expenditure incurred in a particular year is to be allowed in that year. Thus, if the assessee claims that expenditure in that year, the IT Department cannot deny the same. However, in those cases where the assessee himself wants to spread the expenditure over a period of ensuing years, it can be allowed only if the principle of 'Matching Concept' is satisfied, which upto now has been restricted to the cases of debentures.

19. In the instant case, as noticed above, the assessee did not want spread over of this expenditure over a period of five years as in the return filed by it, it had claimed the entire interest paid upfront as deductible expenditure in the same year. In such a situation, when this course of action was permissible in law to the assessee as it was in consonance with the provisions of the Act which permit the assessee to claim the expenditure in the year in which it was incurred, merely because a different treatment was given in the books of account cannot be a factor which would deprive the assessee from claiming the entire expenditure as a deduction. It has been held repeatedly by this Court that entries in the books of account are not determinative or conclusive and the matter is to be examined on the touchstone of provisions contained in the Act [See - ***Kedarnath Jute Mfg. Co. Ltd. v. CIT*** [1971] 82 ITR 363 (SC); ***Tuticorin Alkali Chemicals & Fertilizers Ltd. v. CIT*** [1997] 227 ITR 172/93 Taxman 502 (SC); ***Sutlej Cotton Mills Ltd. v. CIT*** [1979] 116 ITR 1 (SC) and ***United Commercial Bank v. CIT*** [1999] 240 ITR 355/106 Taxman 601 (SC).

20. At the most, an inference can be drawn that by showing this expenditure in a spread over manner in the books of account, the assessee had initially intended to make such an option. However, it abandoned the same before reaching the crucial stage, inasmuch as, in the income tax return filed by the assessee, it chose to claim the entire expenditure in the year in which it was spent/paid by invoking the provisions of Section 36(1)(iii) of the Act. Once a return in that manner was filed, the AO was bound to carry out the assessment by applying the provisions of that Act and not to go beyond the said return. There is no estoppel against the Statute and the Act enables and entitles the assessee to claim the entire expenditure in the manner it is claimed.

21. In view of the aforesaid discussion, we are of the opinion that the judgment and the orders of the High Court and the authorities below do not lay down correct position in law. The assessee would be entitled to deduction of the entire expenditure of Rs. 2,72,25,000 and Rs. 55,00,000 respectively in the year in which the amount was actually paid. The appeals are allowed in the aforesaid terms with no orders as to costs."

14.3. We are also of the view that the Tribunal was wrong in applying the matching principle and directing that one-time lease rent should be spread equally over the tenure of the lease. As indicated hereinabove, the annual lease rent that the appellant/assessee was required to pay if it had chosen the said

route, was Rs. 7,08,913/-. The commuted and discounted value of the one-time lease rent was eleven (11) times the annual rent; which in absolute terms was much lower than the amount that would have accrued as rent over the entire tenure of the lease i.e. 99 years. This was the option exercised by the appellant/assessee. As is evident, taking the present value or time value of the money into account, a lumpsum figure was proposed to the appellant/assessee for securing leasehold rights for 90 years. The lumpsum amount paid by the appellant/assessee, as adverted to above, was far less than the amount that it would have to pay if it were to choose the other option i.e. pay the lease rent on an annual basis for 90 years at the rate of Rs. 7,08,913/-.

14.4. The matching principle, which is an accounting concept, requires entities to report expenses, at the same time, as the revenue. In other words, the revenue is matched with the expense, in the income and expenditure statement, for a particular period. Given the facts obtaining in this case, the matching principle would have no applicability. The appellant/assessee chose to incur the liability of a crystallised amount in the period relevant to the AY in issue i.e. AY 2007-2008, and therefore, it was entitled to seek deduction of the amount which fulfilled the following attributes.

i. The expenditure was not in the nature of capital expenditure or a personal expense.

ii. It was expended fully and exclusively for the purposes of the business and;

iii. It did not fall within the realm of any provision of the Act which prohibited the appellant/assessee from claiming this deduction.

14.5. Thus, we are of the view that question nos. (i) and (ii), as framed in ITA 215/2020, should also be decided in favour of the appellant/assessee and against the revenue. It is ordered accordingly.

Conclusion: -

15. For the foregoing reasons, the above-captioned appeals are allowed. As indicated hereinabove, all four questions of law, as framed, are decided in favour of the appellant/assessee, and against the revenue.

16. There shall, however, be no order as to costs.

RAJIV SHAKDHER, J.

TALWANT SINGH, J.

JULY 05, 2021 *Click here to check the corrigendum, if any*