* **IN THE HIGH COURT OF DELHI AT NEW DELHI**
DECIDED ON: 5th August, 2013

\+ ITA 101/2000
M/S USHA MICRO PROCESS CONTROLS LTD. ..... Appellant

Through: Mr. Prakash Kumar, Advocate.
versus

COMMISSIONER OF INCOME TAX ..... Respondent
Through: Mr. Sanjeev Sabharwal, Sr. Standing Counsel.

CORAM:
HON'BLE MR. JUSTICE S. RAVINDRA BHAT
HON'BLE MR. JUSTICE NAJMI WAZIRI

% **MR. JUSTICE S. RAVINDRA BHAT (OPEN COURT)**

1. The appeal under section 260A of the Income Tax Act, 1961 impugns the order of the Income Tax Appellate Tribunal (ITAT) dated 30.12.1999.

2. This Court had by order dated 09.1.2001 framed the following question of law:

> *"Whether Tribunal was justified in holding that the levy of Rs. 4 lakhs in respect of redemption fine and personal penalty was in the nature of fine and penalty and are not to be allowed as deductible business expenditure while computing total income of the assessee?"*

3. Briefly, the facts are that the petitioner had imported some software during the relevant Assessment Year i.e. 1985-86. It had sought to re-export the software after making some declarations. The customs authorities were of the opinion that the appellant's action was not legal and directed it to pay differential duties. In addition its Managing Director was made personally liable to penalty. The goods were sought to be confiscated. The matter was carried in appeal. Eventually the Customs, Excise and Gold (Control) Appellate Tribunal (CEGAT) decided the matter on 30.5.1999. The

Tribunal directed the deletion of personal penalty but proceeded to uphold the order in so far as the fine in lieu of confiscation is concerned–to Rs. 4,00,000/-; the original amount was Rs. 10,00,000/-.

4. For Assessment Year 1985-86, the assessee had claimed Rs. 4,00,000/- as deductible under Section 37(1) of the Income Tax Act.

5. The appellant claimed benefit of Section 37(1) of the Income Tax Act in respect of payments made towards the penalty as well as redemption fine. The CIT appeals had granted the benefit to the appellant; however regular appeals before the ITAT succeeded.

6. The appellant relies upon the decision of the CEGAT especially paragraph Nos. 18 and 19 to say that the Explanation to Section 37(1) of the Income Tax Act which can be the only rationale for refusal to permit the claim as a deduction was inapplicable. Learned counsel also relied upon the judgment of Madras High Court reported as *Commissioner of Income Tax* v. *N.M. Parthasarathy*, 1995 (212) ITR 105 as well as the ruling of the Supreme Court in *M/s. Prakash Cotton Mills Pvt. Ltd.* v. *Commissioner of Income Tax (Central), Bombay,* 1993 (201) ITR 684.

7. Learned counsel for respondent Mr. Sabharwal argued that the impugned order ought not to be interfered with since the Tribunal took the note of the relevant tests and considered the scheme of enactment while concluding that the amount of Rs.4,00,000/- involved in the present case fell under the explanation of Section 37 (1) of the Income Tax Act.

8. The observations of the CEGAT are pertinent. They are extracted below:

> *18. Keeping in view the totality of the facts and circumstances of the case, we reduce the fine in lieu of the confiscation to Rs. 4,00,000.00 (Rupees four lacs only).*

> *19. Now coming to the penalty, we would like to observe that in the foregoing paragraphs we have held the importation of hardware as authorised and regarding the importation of software, the appellants had requested for the re-exportation of the software and had also placed on record to the effect that the software which was sent with the hardware was not ordered by the appellants and the appellants were keen for sending them back. There is complete absence of the elements of mens reg (sick) and the valuation of the hardware has been taken at a higher figure due to difference of opinion.*

9. In *Prakash Cotton Mills Pvt. Ltd.'s* case (supra), the Supreme Court pertinently observed that whenever an authority has to decide whether to grant or refuse deduction under section 37(1) of the Income Tax Act, the governing test would be whether the amount payable is compensatory in nature. In *N.M. Parthasarathy's* case (supra), the identical situation where redemption fine under the Customs Act was in issue, the Court after examining the scheme of the enactment held as follows:

> *"22. Coming to the facts of the case on hand, the goods belonging to the assessee had been confiscated under section 111(d) of the Customs Act, 1962, read with section 3 of the Imports and Exports (Control) Act, 1947. However, under section 125 of the Customs Act, 1962, an option had been given to the owner assessee to pay, in lieu of such confiscation, a fine of Rs. 1,84,000 which had been reduced on appeal to Rs. 84,000 and the goods had been cleared exercising the option. If the seized goods, without the exercise of option, had been confiscated once and for all, it goes without saying that the property in the goods shall vest in the Government, in the sense of the Government becoming the absolute owner thereof. The fine amount, whatever be its quantification, that is to say, whether it is equivalent to or below the value of the goods seized, cannot at all, in such a situation, be stated to be penal in nature, notwithstanding its nomenclature, but it is reparatory or compensatory in nature. Once it is compensatory in nature, its goes without saying that the authority has to allow deduction*

> *under section 37(1) of the Income Tax Act as laid down by the apex court in the two latest decisions aforecited. Further, the expenses incurred by way of payment of fees to advocates in defending penalty proceedings must also be construed as an allowable deduction. We, therefore, answer questions Nos. 1 and 4 in the affirmative and against the Revenue."*

10. In the present case, this Court notices that originally the penalty which the appellant had been directed to pay was deleted by the CEGAT. What remained was the confiscation; the appellant was given the choice of redeeming the goods by depositing redemption fine as is evident from combined reading of paragraph Nos. 18 and 19 of CEGAT order. The Tribunal went so far as to say that valuation of goods in question was on the basis of difference of opinion. Nevertheless, that being the rationale for deletion of penalty, the Tribunal felt that the order of confiscation did not require to be upset, instead redemption fine was reduced to Rs. 4,00,000/-. On a proper application of the ruling in *M/s. Prakash Cotton Mills Pvt. Ltd.'s* case (supra), this Court is of the opinion that the amount of redemption fine in the present case was compensatory and therefore, fell outside the mischief of explanation of Section 37(1) of the Income Tax Act.

11. In the above conclusion, the question of law framed is answered in favour of the appellant/assessee and against the Revenue. The appeal is allowed in above terms.

S. RAVINDRA BHAT, J
(JUDGE)

NAJMI WAZIRI, J
(JUDGE)

AUGUST 5, 2013/mv