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

% *Date of Decision: 06.01.2023*

\+ **ITA 3/2023**

PR. COMMISSIONER OF INCOME TAX-7 .....Appellant
Through: Mr Puneet Rai, Sr. Standing Counsel.

versus

M/S STEEL AUTHORITY OF INDIA LTD. .....Respondent
Through: Ms Vidhi Gupta and Ms Shweta Kumar, Advocates for Mr Alakh Kumar, Advocate.

CORAM:
HON'BLE MR. JUSTICE RAJIV SHAKDHER
HON'BLE MS. JUSTICE TARA VITASTA GANJU

[Physical Hearing/Hybrid Hearing (as per request)]

RAJIV SHAKDHER, J (ORAL):

CM APPL.159/2023

1. This is an application filed on behalf of the appellant/revenue seeking condonation of delay in filing the appeal.

1.1 As per the averments made in the application, there is a delay of 146 days in filing the appeal.

1.2 The impugned order, which has been passed by the Income Tax Appellate Tribunal [in short, "Tribunal"] is dated 28.02.2022.

2. Except for a laconic assertion made in paragraph 3 of the application, that the delay occurred on account of "administrative reasons beyond the control of the Appellant", there is no explanation given in the application.

3. Mr Puneet Rai, learned senior standing counsel, who appears on

behalf of the appellant/revenue, however, across the bar, says that the delay occurred in the instant matter and several other matters as well, because of the pendency of the matters in which appeals could not to be filed during the period when Covid-19 was raging.

4. Although the reason furnished by Mr Rai is not the reason which has been articulated in the application, we are inclined to condone the delay.

4.1 It is ordered accordingly.

5. The application is, accordingly, disposed of in the aforesaid terms.

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6. This appeal is directed against the order dated 28.02.2022 passed by the Tribunal.

7. Mr Rai, who as indicated above, appears on behalf of the appellant/revenue, says that the impugned order is flawed, as the expenditure incurred by the respondent/assessee towards Corporate Social Responsibility [in short, "CSR"] is not amenable to deduction under Section 37(1) of the Income Tax Act, 1961 [hereafter referred to as "Act"].

8. It is Mr Rai's contention, that neither the Commissioner of Income Tax (Appeals) [in short, "CIT(A)"] nor the Income Tax Appellate Tribunal [in short "Tribunal"] dealt with the issue *qua* which findings were returned by the Assessing Officer [in short, "AO"] concerning whether or not the expenditure was in the nature of capital expenditure, and therefore, deduction under Section 37(1) of the Act, as sustained by the Tribunal, is completely erroneous.

8.1 For this purpose, Mr Rai has drawn our attention to paragraph 9.4 of the order passed by the AO.

9. We have perused the record, as well as the orders passed by the

Tribunal, CIT(A) and AO.

10. A perusal of the assessment order dated 27.12.2016 would show, that the deduction claimed by the respondent/assessee, which is a Public Sector Undertaking (PSU), was denied on two grounds.

10.1 First, that it was in the nature of capital expenditure.

10.2 Second, that Explanation 2, which was inserted to Section 37(1) by Finance Act, 2014, would come in the way of the respondent/assessee.

11. Insofar as the first aspect is concerned, as to whether the expenditure was in the nature of capital expenditure, the AO, without detailing out which part of the CSR expenditure was directed towards capital assets, straightaway concluded that the expenditure on account of social responsibility is to be treated as capital expenditure by taking into account, albeit illustratively, the purposes for which the recipient utilized the funds. The error in the AO's approach is apparent from the following: Firstly, there is nothing on record to suggest that funds were given for a particular purpose and secondly, deductibility under Section 37 cannot depend upon how the funds are spent by the recipient. The capital asset in which funds are funnelled by the recipient is not the asset of the payer i.e., the assessee. The assessee provided funds in discharge of its obligation as mandated by law on the advise of the Department of Public Enterprises. It cannot be said that an obligation placed on the assessee by law was not connected wholly and exclusively to its business.

11.1 The AO's approach, which, as noted above, was erroneous, is evident, if one were to peruse paragraph 9.4 of the AO's order. For the sake of convenience, the said paragraph on which reliance is placed by Mr Rai is extracted hereafter:

> *"9.4 I have gone through the submissions of the assessee and find the same untenable. Corporate Social Responsibilities expenditure is made of enduring long term benefits for communities, cultures and societies in which the assessee company operates. These include establishments of medical facilities, sanitation, building of schools and houses, building vocational training center etc. The expenditure has to come out of the permanent corpus of the assessee company and cannot be debited as revenue expenditure at par with other expenses like commission, hospitality, entertainment, advertisement etc. For these reasons, the expenditure on account of social responsibilities is being treated as capital expenditure and added back to the total income of the assessee. Assessee further contended that explanation 2 to section 37(1) of Income Tax Act introduced by Finance Act, 2014 is not retrospective...."*

12. Since the AO ruled against the respondent/assessee, an appeal was filed with the CIT(A).

12.1 The respondent/assessee specifically raised the issue with regard to the expense incurred as not being in the nature of capital expenses.

13. The CIT(A), concededly, concentrated on whether or not the expenditure towards CSR was wholly and exclusively incurred for business purposes.

13.1 This is evident from the following observations made in the CIT(A)'s order:

> *"9.2 I have gone through facts of the case, the order of the AO and submission filed by the appellant. Explanation 2 to section 37 of the act inserted by finance Act 2014 clearly provides that CSR expenses referred to in Section 135 of the companies act are not allowed as deduction under section 37 of the act because Rule 4(1) of the CSR Rules exclude the activities undertaken in pursuance of the normal course of business of company.*
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> *9.3 In this case, since the AY involved is prior to the introduction of CSR rules and explanation 2 to section 37 of the Act, therefore, the only test for allowing deduction u/s 37 of the act is that whether it is wholly & exclusively for the purpose business or not?*
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> *9.4 In this regard, the arguments of the assessee are that CSR activities are mandated by Department of Public Enterprises. The mandate by Govt. Of India does not in itself can be taken as the reason for incurring the expenditure wholly and exclusively for business purpose. For*

example, CSR Rules do mandate for CSR activities but at the same time, the rules bar the activities undertaken in pursuance of normal course of business of company.

9.5 It is important to note that no mandate of any nature is required for an entity to incur expenditure wholly & exclusively for the business. However, mandate is essential only for the activities which are beyond the scope of activities conducted for business run by particular entity. The assessee has, nowhere, demonstrated the direct nexus of incurring the expenditure with the running of business of entity. Further, the assessee has not explained that if it was a case of business expenditure, in that case, the question of issuing mandate by Department of Public Enterprises would have not arisen. Accordingly, the AO has rightly disallowed CSR expenses in the case..."

14. Being aggrieved, the respondent/assessee preferred an appeal with the Tribunal.

14.1 The Tribunal, after noticing the grounds on which the appellant/revenue had disallowed the expenses incurred by the respondent/assessee towards CSR, which was that it was not in the nature of capital expenses and not wholly and exclusively incurred for the purpose of business, also adverted to whether or not Explanation 2 of Section 37(1) was retrospective in nature.

14.2 This aspect of the matter emerges upon a perusal of paragraph 8 of the order passed by the Tribunal, which is extracted hereafter:

"8. We have considered rival submissions and perused the materials on record. Undisputedly, the departmental authorities have disallowed the CSR expenses, firstly, on the reasoning that it is of capital nature, and secondly, it is not incurred wholly and exclusively for the purpose of business. As per section 135 of the Companies Act, 2013, every company having net worth of Rs. 500/- crores or more, or turnover of Rs. 1000/- crores or more, or a net profit of Rs. 5 crores or more during the immediately preceding financial year has to spent a certain percentage out of their profit towards CSR activities. Prior to amendment to section 37(1) of the Act by the Finance Act, 2014 by insertion of
Explanation – 2, CSR expenses were allowed as deduction under section 37(1) of the Act, as, there was no specific bar either under section 37(1) of the Act or under any other provision for claiming deduction for CSR

> *expenses. There are number of judicial precedents which have expressed the aforesaid view, some of these decisions have been cited before us by learned counsel for the assessee. Thus, prior to insertion of Explanation – 2 to section 37(1) of the Act, w.e.f., 01.04.2014, as per settled legal position, it is an allowable expenditure under Section 37(1). A specific bar for allowing such expenditure under section 37(1) of the Act was brought to the statue by Finance Act, 2014 effective from 01.04.2014. Therefore, the amendment, no doubt, will apply prospectively. Thus, following the various judicial precedents cited before us, we hold that CSR expenses incurred by the assessee are allowable as deduction under section 37(1) of the Act. This ground is allowed."*

15. In our view, as indicated above, Mr Rai's arguments *vis-a-vis* the allowability of deduction concerning expenses on CSR are flawed, for the following reasons:

(i) Insofar as whether or not expenditure is capital in nature, as observed hereinabove, apart from a bald conclusion by the AO, there is nothing on record, which would show that the respondent/assessee had directed investment of funds, which were offered in fulfilment of discharge of its legal obligation, in a capital asset.

(ii) Although the respondent/assessee lost before the CIT(A), the appellant/revenue did not file cross-objections before the Tribunal in the appeal preferred by the respondent/assessee.

(iii) A perusal of paragraph 8 of the Tribunal's order shows, that the Tribunal had, based on previous decisions, concluded that the CSR expenses incurred are allowable under Section 37 of the Act.

16. The conditions for allowing deduction under Section 37 of the Act are broadly the following:

(a) That the expenditure is not in the nature of capital expenditure.

(b) That the expenditure is laid out or expended wholly and exclusively for the purposes of the business or profession.

(c) That the deduction *qua* the expenditure incurred is not of the nature as specified under Sections 30 to 36 of the Act.

17. Insofar as the third criterion is concerned, there is no dispute, that the expenditure claimed does not fall under any of the sections referred to in 37(1) of the Act i.e., Sections 30 to 36.

17.1 As far as the other aspects are concerned, as noted by the Tribunal, in the past, CSR expenses had been allowed as deductible expenditure under Section 37(1) of the Act.

18. Therefore, the only aspect, which appears to have been agitated before the Tribunal, was that Explanation 2 appended to Section 37(1) of the Act was retrospective in nature.

18.1 This Explanation was inserted, as noted above, by Finance Act, 2014 with effect from 01.04.2015.

18.2 That the Explanation appended to Section 37(1) of the Act is prospective has been held by this Court in order dated 29.11.2022 passed in a bunch of appeals, the lead matter being ITA 268/2022, titled ***PR. COMMISSIONER OF INCOME TAX -7 Vs. PEC LTD***.

19. Thus, for the aforementioned reasons, we are not inclined to interfere with the order of the Tribunal. According to us, no substantial question of law arises for consideration.

20. The appeal is, accordingly, closed.

RAJIV SHAKDHER, J

TARA VITASTA GANJU, J

JANUARY 6, 2023/pmc