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

% *Decision delivered on: 29.11.2022*

\+ **ITA 268/2022**

PR. COMMISSIONER OF INCOME TAX -7 ..... Appellant
Through: Mr Puneet Rai, Sr. Standing Counsel and Ms Adeeba Mujahid, Jr. Standing Counsel with Mr Nikhil Jain, Adv. for Revenue.

versus

PEC LTD. ..... Respondent
Through: None.

\+ **ITA 269/2022**

PR. COMMISSIONER OF INCOME TAX -7 ..... Appellant
Through: Mr Puneet Rai, Sr. Standing Counsel and Ms Adeeba Mujahid, Jr. Standing Counsel with Mr Nikhil Jain, Adv. for Revenue.

versus

RITES LIMITED ..... Respondent
Through: None.

\+ **ITA 270/2022**

PR. COMMISSIONER OF INCOME TAX -7 ..... Appellant
Through: Mr Puneet Rai, Sr. Standing Counsel and Ms Adeeba Mujahid, Jr. Standing Counsel with Mr Nikhil Jain, Adv. for Revenue.

versus

RITES LIMITED ..... Respondent
Through: None.

**CORAM:**
**HON'BLE MR. JUSTICE RAJIV SHAKDHER**
**HON'BLE MS. JUSTICE TARA VITASTA GANJU**
**[Physical Court Hearing/Hybrid Hearing (as per request)]**

**RAJIV SHAKDHER, J. (ORAL):**

1. A common question of law arises for consideration in the aforementioned appeals.

1.1 Although the matters are at the notice stage, we are inclined to consider the question of law proposed on behalf of the appellant/revenue. Therefore, these appeals are admitted, and the following question of law is framed for consideration:

"*Whether in the facts and circumstances of the case, the Income Tax Appellate Tribunal [hereafter referred to as "Tribunal"] erred in allowing deduction of expenses undertaken under the Corporate Social Responsibility (CSR) endeavour under Section 37 of the Income Tax Act, 1961 [in short "Act"]?*"

2. As would be evident from the cause title of the appeals before us, two orders in the aforementioned appeals i.e., ITA No.269/2022 and ITA No.270/2022 pertain to a company i.e., RITES Ltd. RITES Ltd is owned by the Government of India. The assessment years, which are under consideration in the aforementioned appeals, are the following:

| ***Sr.No.*** | ***Case No.*** | ***Assessment Year*** |
|---|---|---|
| *1.* | *ITA No.268/2022* | *2013-2014* |
| *2.* | *ITA No.269/2022* | *2014-2015* |
| *3.* | *ITA No.270/2022* | *2013-2014* |

3. The expenses incurred by the respondents/assessees in the aforementioned Assessment Years (AYs), which were disallowed by the

assessing officer in each of the assessment years are detailed out hereafter:

| ***Item No.*** | ***Title of the case*** | ***Assessment Year*** | ***Amount of CSR expenditure in question*** |
|---|---|---|---|
| *1.* | PCIT-7 Vs PEC Limited | *2013-2014* | *Rs. 3,79,19,732-* |
| *2.* | PCIT-7 Vs RITES Limited | *2014-2015* | *Rs. 5,32,92,063-* |
| *3.* | PCIT-7 Vs RITES Limited | *2013-2014* | *Rs. 6,44,00,000-* |

4. The argument advanced on behalf of the appellant/revenue is, that the respondent/assessees could have claimed a deduction under Section 37 of the Act only if all the conditions prescribed in the said provision were fulfilled:

4.1 According to Mr Puneet Rai, who appears on behalf of the appellant/revenue, the expenditure qua which deduction is claimed was not incurred wholly and exclusively for the purposes of carrying on business or profession.

4.2 To put it more specifically, it is Mr Rai's contention, that the funds utilized by the respondent/assessee to effectuate its CSR obligation involved application of income and not an expense which had been incurred wholly and exclusively for the purposes of carrying on business.

4.3 In support of this plea, Mr Rai relies upon the amendment brought about in Section 37(1) of the Act by way of insertion of Explanation 2. The contention is that Explanation 2 appended to sub-section (1) of Section 37 of the Act is clarificatory in nature, and therefore would be applicable *qua* the assessment years in issue, concerning each of the respondents/assessees.

5. The Income Tax Appellate Tribunal [in short "Tribunal"], however,

has taken a contrary view.

5.1 *Inter alia*, the Tribunal has relied upon Circular No.1 dated 21.01.2015 to reach a conclusion that the amendment brought about in Section 37(1) of the Act by way of Explanation 2 would not operate *vis-à-vis* the assessment years in issue.

5.2 The Tribunal's view, in this regard, emerges upon a perusal of paragraph 17 of the order dated 12.01.2021 passed in ITA No.269/2022. For the sake of convenience, the said observations are extracted hereafter:

> *"17. AO has disallowed claim of the assessee company qua CSR expenditure by misinterpreting the provisions contained under section 37(1) of the Act by observing that since CSR expenditure is not incurred for the purpose of carrying on the business, such expenditure cannot be allowed under the existing provisions of section 37 of the Act. Even Explanation 2 to section 37(1) of the Act is prospective in nature to be effective from 01.04.2015 and is applicable to the expenses incurred with reference to section 135 of the Companies Act, 2013 that too after 01.04.2015, so Explanation (2) to section 37(1) of the Act is not applicable to the present case also. Moreover, expenses claimed by the assessee company have been incurred as per guidelines of the Ministry concerned with approval of the Board to the best business interest of the assessee company. So AO, without examining the nature of the expenses, disallowed the claim mechanically even by ignoring the rule of consistency."*

6. We have heard the submissions advanced by Mr Rai.

6.1 According to us, it would be useful to extract the relevant parts of the Section 37(1) in order to decide the issue at hand.

> ***"37(1)*** *Any Expenditure (not being expenditure of the nature described in Sections 30 to 36 and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly or exclusively for the purposes of the business or profession shall be allowed in computing the income*

*chargeable under the head " Profits and gains of business or profession.*
*xxx xxx xxx*
*Explanation 1 ; xxx xxx xxx*
*Explanation 2 ; For the removal of doubts , it is hereby declared that for the purposes of Sub section (1), any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in Section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purposes of business or profession."*

7. A plain reading of the aforesaid extract of Section 37 would show, that in order to claim deduction under Section 37 of the Act, the expenditure incurred should be one that:

(i) Does not fall in any of the provisions referred to therein i.e., Sections 30 to 36.

(ii) Should not be in the nature of a capital expenditure or personal expenses of the assessee.

(iii) And lastly, the expenditure should have been laid out or expended wholly or exclusively for the purposes of business or profession.

7.1 If these conditions are met, then the expense incurred can be deducted while computing the income chargeable under the head "profits and gains of business or profession."

8. In the instant case, the respondent/assessee has sought to seek deduction of amounts spent to progress its CSR obligation, and sought deduction against the income chargeable under the head "profits and gains of business or profession."

8.1 The deduction claimed was disallowed by the assessing officer.

9. The matter, consequently, travelled to the Tribunal.

9.1 The Tribunal, as noted above, ruled in favour of the respondent/assessee.

9.2 The Tribunal has opined, that Explanation 2 inserted in Section 37(1) was prospective in nature, and therefore was not applicable in the assessment years in issue.

10. It is required to be noticed, that Explanation 2 was inserted in Section 37 *via* Finance (No.2) Act, 2004 w.e.f. 01.04.2015. Furthermore, what emerged during the course of the hearing was, that the memorandum which was published along with Finance (No.2) Bill 2014 clearly indicated that the amendment would take effect from 01.04.2015 and, accordingly, would apply in relation to assessment year 2015-2016 and the subsequent years.

10.1 This is plainly evident upon perusal of the following extract from the memorandum:

> "*The existing provisions of section 37(1) of the Act provide that deduction for any expenditure, which is not mentioned specifically in section 30 to section 36 of the Act, shall be allowed if the same is incurred wholly and exclusively for the purposes of carrying on business or profession. As the CSR expenditure (being an application of income) is not incurred for the purposes of carrying on business, such expenditures cannot be allowed under the existing provisions of section 37 of the Income-tax Act. Therefore, in order to provide certainty on this issue, it is proposed to clarify that for the purposes of section 37(1) any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and hence shall not be allowed as deduction under section 37. However, the CSR expenditure which is of the nature described in section 30 to section 36 of the Act shall be allowed deduction under those sections subject to fulfilment of conditions, if any, specified therein.*
>
> ***This amendment will take effect from 1st April, 2015 and will,***

***accordingly, apply in relation to the assessment year 2015-16 and subsequent years.***"

[ Emphasis is ours]

11. This position is also exemplified in the circular dated 21.01.2015 issued by the Central Board of Direct Taxes (CBDT). The relevant extract of the said circular is extracted hereafter:

> *"13.3 The provisions of section 37(1) of the Income-tax Act provide that deduction for any expenditure, which is not mentioned specifically in section 30 to section 36 of the Income-tax Act, shall be allowed if the same is incurred wholly and exclusively for the purposes of carrying on business or profession. As the CSR expenditure (being an application of income) is not incurred for the purposes of carrying on business, such expenditures cannot be allowed under the provisions of section 37 of the Income-tax Act. Therefore, in order to provide certainty on this issue, said section 37 has been amended to clarify that for the purposes of sub-section (1) of section 37 any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 shall not be deemed to have been incurred for the purpose of business and hence shall not be allowed as deduction under said section 37. However, the CSR expenditure which is of the nature described in section 30 to section 36 of the Income-tax Act shall be allowed as deduction under those sections subject to fulfillment of conditions, if any, specified therein.*
>
> *13.4 Applicability:-* ***This amendment takes effect from 1st April, 2015 and will, accordingly, apply in relation to the assessment year 2015-16 and subsequent years****."*
>
> [ Emphasis is ours]

12. Clearly, if there was any doubt, the same has been removed both by the memorandum issued along with the Finance Bill, as well as the aforementioned circular issued by the CBDT.

13. It is well established that circulars are binding on the revenue. [See: ***Catholic Syrian Bank Vs. CIT*** (2012) 343 ITR 270 (SC)]

14. Therefore, for the appellant/revenue to contend in the aforementioned appeals, that the Tribunal had erred in law in sustaining the deduction claimed by the respondents/assessees under Section 37(1) of the Act is an argument, which cannot be accepted.

15. Accordingly, the question of law is decided against the appellant/revenue and in favour of the respondents/assessees.

16. The above-captioned appeals are disposed of in the aforesaid terms.

**RAJIV SHAKDHER, J**

**TARA VITASTA GANJU, J**

**NOVEMBER 29, 2022**
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