IN THE INCOME TAX APPELLATE TRIBUNAL
COCHIN BENCH, COCHIN
BEFORE S/SHRI CHANDRA POOJARI, AM & GEORGE GEORGE K., JM

I.T.A. No.142/Coch/2017
Assessment Year : 2012-13

M/s. Kerala State Industrial Development Corporation Ltd., Keston Road, Kowdiar, Trivandrum-695 003. [PAN:AAACK 9434D]	**Vs.**	The Assistant Commissioner of Income-tax, Circle-1(1), Trivandrum.
(Assessee-Appellant)		**(Revenue-Respondent)**

Assessee by	Shri Roopesh R., CA
Revenue by	Shri Alok Nath Mitra, CIT(DR)

Date of hearing	05/02/2019
Date of pronouncement	07/02/2019

O R D E R

Per CHANDRA POOJARI, AM:

This appeal filed by the assessee is directed against the order of the CIT, Trivandrum dated 27/03/2017 passed u/s. 263 of the I.T. Act and pertains to the assessment year 2012-13.

2. On examination of the assessment records, the CIT found that the 'Value of advance share investment amounting to Rs.25,00,000/- was allowed as deduction even though it was capital in nature. The ineligible deduction thus allowed resulted in an under assessment to the tune of Rs.25 lakhs. Further, the

2.1 The CIT(A) observed that an expenditure of Rs.12.36 lakhs incurred towards Corporate Social Responsibility (CSR) – Free Education to Girl child – included in 'other expenses' was allowed as deduction. As per Explanation 2 to section 37(1) of the Act, any expenditure incurred by the assessee on the activities relating to CSR referred to in section 135 of the Companies Act, 2013 shall not be deemed to be an expenditure incurred by the assessee for the purpose of business or profession.

2.2 The CIT(A) relied on the judgment of the Apex Court in the case of CIT Vs Madras Refineries Ltd. (313 ITR 334), wherein it was observed that neither the High Court nor the Tribunal concerned had given specific finding to the effect that the said CSR expenditure is allowable as business expenditure. In this case also, since there is no specific reason to show that the CSR expense claimed was incurred wholly and exclusively for the purpose of business of the assessee, allowing it as expenditure u/s. 37 of the Act, was not in order.

2.3. The CIT(A) observed that as the Assessing Officer failed to take notice of these while completing the assessment, the assessment passed on 20.03.2015 was treated as erroneous and prejudicial to the interests of revenue. Hence, a notice was issued to assessee on 20.12.2016 proposing to revise the assessment by invoking the provisions of section 263 of the Income tax Act, 1961.

3. The first issue is with regard to deduction of Rs.25,00,000/- which was value of advance share investment. The Ld. AR stated that the assessee had financed the project promoted by Manila Electronics Pvt. Ltd. (MEPL) by way of share capital and also loan. It was submitted that due to various problems faced by MEPL, it defaulted in repayment of loan. It was submitted that to revive the project, by way of One Time Settlement, the assessee agreed to settle the loan outstanding by remitting Rs.25 lakhs and to convert loan portion of Rs.25 lakhs into equity on the condition that the shares held by assessee in MEPL on the date of conversion does not exceed 50%. According to the Ld. AR, on this basis, the funds remitted by MEPL Rs.25 lakhs was adjusted against loan and the balance loan amount of Rs.25 lakhs was treated as advance for shares by assessee in its books. However, since MEPL could not bring in additional equity to keep the shares held by assessee at 50%, the shares were not allotted far Rs.25 lakhs treated as advance for shares. It was submitted that due to continuous losses, entire networth of MEPL were eroded and became negative as on 31/03/2013 Rs. 86.82 lakhs as against the share capital of Rs. 86.82 lakhs the accumulated loss was Rs.210.13 lakhs, resulting in negative networth of Rs.124.06 lakhs. It was submitted that there was no operation in the company and it had also sold substantial part affixed assets. Since the networth had fully eroded, assessee had created provision for the entire shares held in MEPL, including the advance for shares, since it also takes the character of shares. For this proposition, the Ld. AR relied upon decision of Kerala High Court in case of

Nedungadi Bank Ltd (264 ITR 545) wherein depreciation of securities was held as stock-in-trade. He also stated that the same was claimed in accordance with AS 13 concerning accounting of investments.

4. The Assessing Officer opined that advance share investment/ share application money cannot assume the character of stock-in-trade. The assessee countered the views of Assessing Officer by stating that irrespective of the fact whether shares are allotted or not, the money given as share advance was not refundable and this can be utilized only for allotment of shares. Hence, the amount paid as advance has to be considered as investment in the form of shares even though the allotment had not been completed.

5. On examination of the assessment records, the CIT found that there was a significant difference between securities held as stock-in-trade on which diminution in value was claimed in accordance with decision in the case of Nedungadi Bank cited supra and application of decision on advance for share. The CIT observed that advance for share has no character of stock-in-trade and an advance always carries a tag of conditional or unconditional change including return. It is an intermediary stage of allotment and once share is allotted. it can be transferred through specific modes like sale, buy-back etc. in accordance with provisions of law. Therefore, it was observed that diminution of value of share advance does not get covered in diminution of value of securities held as stock-

in-trade- Hence, the CIT held that the assessment order was erroneous and prejudicial to interests of revenue which necessitated revision and he direct the Assessing Officer to enhance income by Rs.25,00,000/-.

6. The next issue is with regard to allowance of CSR expenses. The Ld. AR stated that assessee-Company is a Government of Kerala Undertaking. It had formulated a programme 'Free education for child' as part of its Golden Jubilee Celebrations. It was submitted that the Board of Directors, which comprises of Government Secretaries and other nominees as Members, decided to give special attention to those who need care such as the marginalized and weaker sections of the society and under this programme, scholarship was provided to 50 girls belonging to widow-headed poor families from different Districts across Kerala. The scheme of scholarship provided for subsidy in the educational fee and other fee paid to respective institutions till Degree level education which is a welfare measure for uplifting the weaker section of the society. Being a public sector company, it was submitted that it was not formed just to make profit alone but was supposed to achieve larger objectives for the society and the State. Hence, it incurred the expenditure towards Free Education for Child.

6.1 With respect to the issue of disallowing the expenditure incurred towards CSR expenses, the assessee submitted that the Corporate Social Responsibility expenses hds been incurred by the assessee as per the provisions of a Central Government Statute viz. Companies Act, 1953 enacted by Government of India.

Hence, it was submitted that the assessee had to incur such expenditure as per law if it has to do the business. The Ld. AR further submitted that explanation to section 37(1) of IT Act 1961 was inserted by the Finance Act, 2014 and hence, it is applicable only from 01-04-2014 i.e. from assessment 2015-16 only. The Ld. AR also brought to attention the decision of ITAT Raipur Bench in case of Jindal Steel Ltd.

7. After examining the assessment records and the arguments of the assessee, the CIT found that the assessing officer had not examined the issue in right perspective and erred in making a decision without following due process of law. According to the CIT, allowing a claim of expense depends on being

(a) Permissible as a deduction in Chapter IV-D (eg., section 31,32 etc)
(b) Not impermissible as a deduction in Chapter IV-D(eg., section 40A(3).

7.1 The CIT found that the sums were deducted under head Corporate Social Responsibility. According to the CIT, the law explicitly provided w.e.f AY 2015-16 that the sums were not permissible as a deduction and the amendment brought in Finance Act, 2014 was already in statute book at the time of completion of assessment and its retrospective applicability was also to be examined at the stage of assessment as to whether the expense is allowable as a deduction. It was observed that even if the sums which were booked under Corporate Social Responsibility was allowable on the basis of nomenclature, the nature of expense which makes it allowable as a deduction under Chapter IV-D

has to be considered. In the case of assessee, it was found that the expense was for a noble cause being free education of girl child. According to the CIT, this explanation has no bearing on the income of the assessee as it has not gone into augmentation of profits. According to the CIT, the law indeed contains provisions for incurring expenses for noble causes (eg., section 80G), hence, it cannot be said that the expenses charged under 'Corporate Social Responsibility' were incurred wholly and exclusively for business. Hence, the CIT held that the decision of Assessing Officer was erroneous and prejudicial to interests of revenue and directed the Assessing Officer to disallow the CSR expenses claimed. The CIT relied on the judgment of the Gauhati High Court in the case of CIT Vs. Jawahar Bhattacharjee (2012) (341 ITR 434)(FB). He also relied on the judgment of the Rajasthan High Court in the case of CIT Vs. Emery Stone Manufacturing Co.(1995) (213 ITR 843) wherein it was held that failure to apply the correct provision of law as may be applicable in given facts of the case will be resulting in an erroneous order. Further, the CIT relied on the judgment of the Supreme Court in the case of Malabar Industrial Co. Ltd. Vs. CIT (2000) (243 ITR 83) wherein it was held as under:

> A. The CIT has to be satisfied of twin conditions, namely, (i) the order of the AO sought to be revised is erroneous; and (ii) it is prejudicial to the interests of the Revenue. If one of them is absent—if the order of the ITO is erroneous but is not prejudicial to the Revenue or if it is not erroneous but is prejudicial to the Revenue—recourse cannot be had to section 263(1) of the Act.

B. The phrase 'prejudicial to the interests of the Revenue' is not an expression of art and is not defined in the Act. Understood in its ordinary meaning it is of wide import and is not confined to loss of tax.

C. The scheme of the Act is to levy and collect tax in accordance with the provisions of the Act and this task is entrusted to the Revenue. If due to an erroneous order of the ITO, the Revenue is losing tax lawfully payable by a person, it will certainly be prejudicial to interests of revenue.

Thus, the CIT invoked the provisions of section 263 of the Act and directed the Assessing Officer to revise die assessment order.

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8. Against this, the assessee is in appeal before us.

9. We have heard the rival submissions and perused the record. Section 263 of the Income-tax Act seeks to remove the prejudice caused to the revenue by the erroneous order passed by the Assessing Officer. It empowers the Commissioner to initiate suo moto proceedings either where the Assessing Officer takes a wrong decision without considering the materials available on record or he takes a decision without making an enquiry into the matters, where such inquiry was prima facie warranted. The Commissioner is well within his powers to treat an order as erroneous on the ground that the Assessing Officer should have made further inquiries before accepting the wrong claims made by the assessee. The Assessing Officer cannot remain passive in the face of a claim, which calls for further enquiry to know the genuineness of it. In other words, he must carry out investigation where the facts of the case so require and

also decide the matter judiciously on the basis of materials collected by him as also those produced by the assessee before him. The Assessing Officer was statutorily required to make the assessment under Section 143(3) after scrutiny and not in a summary manner as contemplated by Sub-section (1) of Section 143. The Assessing Officer is therefore, required to act fairly while accepting or rejecting the claim of the assessee in cases of scrutiny assessments. The Assessing Officer should protect the interests of the revenue and to see that no one dodged the revenue and escaped without paying the legitimate tax. The Assessing Officer is not expected to put blinkers on his eyes and mechanically accept what the assessee claims before him. It is his duty to ascertain the truth of the facts stated and the genuineness of the claims made in the return. The order passed by the Assessing Officer becomes erroneous when an enquiry has not been made before accepting the genuineness of the claim which resulted in loss of revenue.

9.1 In the present case, with regard to allowability of value of advance share investments of Rs.25 lakhs as deduction cannot be considered as valid deduction to be allowed by the Assessing Officer. The value of advance share investments cannot be considered as shares so as to consider diminution in its value. The advance for share investments takes the character of shares only when it was allotted. Until then, it has to be treated as advance for share investments. Therefore, diminution in value of advance for shares cannot be considered as diminution in the value of securities which was not held as stock in trade so as to

grant deduction. Without making any enquiry, the Assessing Officer accepted the assessee's claim. The failure on the part of the Assessing Officer to make necessary enquiry rendered the assessment order erroneous which also resulted in loss to the revenue. Hence, the order of the CIT cannot be held as erroneous. The CIT's approach was correct. Therefore, the CIT exercised his power conferred u/s. 263 of the Act in setting aside the assessment. Being so, we uphold the findings of the CIT on this issue. Accordingly, the above ground of appeal of the assessee is dismissed.

9.2 With regard to the claim of CSR expenses, we find that a similar issue came up for consideration before this Tribunal wherein it was held as under:

> *"9. We have heard the rival submissions and perused the material on record. The assessee is a Government of India Undertaking, working under the Ministry of Health and Family Welfare. The Government of India had issued certain Guidelines dated 09.04.2010 to all Central Public Sector Enterprises on CSR. The Guidelines issued by the Central Government dated 09.04.2010, is placed at pages 9 to 27 of the paper book filed by the assessee. As per the Guidelines as indicated under "5. Funding", all PSUs should mandatorily spend a percentage of net profit for CSR activities. The CSR expenses that has been incurred by the assessee is based on the specific directions of the Government of India and the AO in the assessment order passed u/s. 143(3) dated 19.03.2015 had allowed the CSR expenditure.*
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> *9.1 The following explanation was introduced in the I.T. Act ay Finance Act, 2014:*
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> > *"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 (18 of 2013) shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession"*

9.2 The "Notes on Clauses" of Finance Bill, 2014 states as under:

"Clause 13 of the Bill seeks to amend section 37 of the Income-tax Act relating to general expenditure

The existing provisions contained in sub-section (1) of the aforesaid section provide that, 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 and 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".

It is proposed to insert a new Explanation in sub-section(1) of section 37 so as to clarify that the purpose of sub-section (1) of the said section, 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 the business or profession."

This amendment will take effect from 1st April, 2015 and will, accordingly, apply in relation to assessment near 2015-16

(emphasis supplied)

9.3 The ITAT, Raipur Bench in the case of Jinclal Power Ltd (supra) had held that Explanation 2 to section 37(1) of the I.T. Act is prospective. The relevant findings of the Tribunal reads as follows:

"This disabling provision, as set out in Explanation 2 to Section 37(1), refers only to such corporate social responsibility expenses as under Section 135 of the Companies Act, 2013, and, as such, it cannot have any application for the period not covered by this statutory provision which itself came into existence in 2013. Explanation 2 to Section 37(1) is, therefore, inherently incapable of retrospective application any further."

9.4 It was specifically mentioned in the notes on clauses explaining the Finance Bill 2014, that the "Explanation 2" is applicable only from the assessment year 2015-2016. This also implies that CSR expenditure incurred by the assessee upto the assessment year 2014-2015 is an allowable business expenditure u/s 37 of the I.T. Act.

9.5 The CSR expenses that has been incurred by the assessee is based on the specific directions of the Government of India and the AO in the assessment order passed u/s. 143(3) dated 19.03.2015 had allowed the CSR expenditure. The CSR expenses has been incurred as per the directions of Government of India. The Hon'ble Kerala High Court in the case of Travancore Titanium Products Ltd. (supra) had held that a Government Undertaking is duty bound to comply with Government orders. The relevant finds of the Hon'ble jurisdictional High Court reads as follows:

> *"Being a company under the control of the Government, it is bound to comply with the Government orders and the Board of Directors itself is constituted with the Government secretaries and other nominees as members.*
>
> *Therefore, the claim of deduction has to be considered with reference to the peculiar circumstances of the company which has no discretion in regard to the payment of the service charges to the government as it is bound to comply with the government orders. So much, so, we are of the view that the parameters applicable in the case of a private company that too with respect to the claim for business expenditure, are exactly not applicable in the case of Public Sector Company whether it is under the control of the State Government or Central Government.*
>
> *In fact, many public sector companies are not formed just to make profit alone but are supposed to achieve larger objectives for the society and the State.*
>
> *By making payment of service charge, the respondent company has discharged only the obligation under Government orders. It cannot carry on business by violating Government orders and remain as a defaulter to the Government.*

9.6 The ITAT Mumbai bench in the case of Hindustan Petroleum Corporation Ltd. (96 1TD 186) had held CSR expenditure incurred by Government Undertaking is an allowable deduction. The relevant finding of the ITAT Mumbai Benches reads as follows:

> *"Expenditure incurred by assessee, a company owned by the Government of India and working under its control and directions, towards implementation of 20 point programme as per specific directions of the Government though voluntary in nature and not forced by any statutory obligation, is allowable as business expenditure.*

Merely because an expenditure is in the nature of donation, it does not cease to be an expenditure deductible under s. 37(1)."

9.7 The Commissioner of Income tax had mentioned in his order that the "Apex Court (313 1TR 334 SC) CIT vs. Madras Refineries Ltd., while hearing the allowability of CSR expenses observed that neither the High Court nor the Tribunal concerned had given specific finding to the effect that the said CSR expenditure is allowable as business expenditure." In the above mentioned case, the Apex court has not given any decision on merits of the case. It had only given an observation and remitted the issue back to the Tribunal to give specific finding to the effect that the said CSR expenditure is allowable as business expenditure.

9.8 Since, the assessee had incurred CSR expenses to comply with the directions of Govt. of India, following the above observations made by High Court of Kerala and IT AT, Mumbai Bench, the expenditure incurred is incidental to the assessee's business and ought to be allowed as deduction u/s. 37 of the I.T. Act.

9.9 Therefore, the A.O. had taken a possible view and the assessment order cannot be stated to be erroneous or prejudicial to the interest of the Revenue, warranting interference u/s 263 of the I.T. Act. Therefore, we set aside the impugned order of the CIT passed u/s 263 of the I.T. Act. It is ordered accordingly.

10. In the result, the appeal filed by the assessee is allowed."

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9.3 In view of the above discussion, we find that the Assessing Officer has taken one possible view with regard to CSR expenses. Accordingly, we vacate the findings of the CIT on this issue u/s. 263 of the Act. Hence, this ground of appeal of the assessee is allowed.

10. In the result, the appeal of the assessee is partly allowed.

Order pronounced in the open Court on this 7th February, 2019

sd/-	sd/-
(GEORGE GEORGE K.)	(CHANDRA POOJARI)
JUDICIAL MEMBER	ACCOUNTANT MEMBER

Place: Kochi
Dated: 7th February, 2019
GJ
Copy to:
1. M/s. Kerala State Industrial Development Corporation Ltd., Keston Road, Kowdiar, Trivandrum-695 003.
2. The Assistant Commissioner of Income-tax, Circle-1(1), Trivandrum.
3. The Pr. Commissioner of Income-tax, Trivandrum.
4. D.R., I.T.A.T., Cochin Bench, Cochin.
5. Guard File.

By Order

(ASSISTANT REGISTRAR)
I.T.A.T., Cochin