IN THE INCOME TAX APPELLATE TRIBUNAL
MUMBAI "I" BENCH: MUMBAI

BEFORE JUSTICE (RETD.) SHRI C.V. BHADANG, PRESIDENT
AND
SHRI VIKRAM SINGH YADAV, ACCOUNTANT MEMBER

ITA No.	A.Y.	Appellant	Respondent
3159/Mum/2004	1999-2000	The Bank of Nova Scotia, Mittal Towers, B Wing, Nariman Point, Mumbai-400020 [PAN: AAACB1536H]	Asst. Commissioner of Income Tax, Range-1(1), Scindia House, Ballard Pier, Mumbai-400038
7158/Mum/2004	2000-2001		Joint Director of Income Tax, International Taxation-3, Scindia House, Ballard Pier, Mumbai-400038
2285/Mum/2005	2001-2002		Deputy Director of Income Tax, International Taxation-1(1), Scindia House, Ballard Pier, Mumbai-400038
3488/Mum/2004	1999-2000	DDIT(IT)-1(1), Room No. 117, Scindia House, Ballard Pier, N.M. Road, Mumbai-400038	The Bank of Nova Scotia, Mittal Towers, B Wing, Nariman Point, Mumbai-400020 [PAN: AAACB1536H]
7217/Mum/2004	2000-2001	DDIT(IT)-3(2), Room No. 132, 1st Floor, Scindia House, Ballard Pier, N.M. Road, Mumbai-400038	
2286/Mum/2005	2001-2002		

C.O. No.	A.Y.	Appellant	Cross-Objector
174/Mum/2013 *(in ITA No. 3159/M/04)*	1999-2000	Director of Income Tax (IT)-II, Mumbai	The Bank of Nova Scotia, Mittal Towers, B Wing, Nariman Point,
175/Mum/2013 *(in ITA No. 7158/M/04)*	2000-2001		

176/Mum/2013 *(in ITA No. 2285/M/05)*	2001-2002		Mumbai-400020 [PAN: AAACB1536H]

For Assessee :	Shri Nishant Thakkar a/w Ms. Jasmin Amalasadvala
For Revenue :	Shri Krishna Kumar, Sr.DR

Date of Hearing :	01-04-2026
Date of Pronouncement :	25-06-2026

ORDER

PER VIKRAM SINGH YADAV, A.M :

These are cross appeals filed by the Assessee and the Revenue, and the cross-objections by the Revenue in respect of respective order(s) of the Learned Commissioner of Income Tax (Appeals)-XXXI, Mumbai ['Ld.CIT(A)'], pertaining to Assessment Years (AY) 1999-2000 to 2001-02 wherein the respective grounds of appeal read as under:

Assessee's grounds of appeal in ITA No. 3159/Mum/2004 pertaining to Assessment Year 1999-2000

> *"In disregarding the tax neutrality claimed in respect of interest of Rs. 86,239,455 received by the Appellant on funds placed with its head office/overseas branches, and the interest of Rs 1,077,963 paid by the Appellant in respect of funds placed with it by its head office/overseas branches."*

Revenue's ground of appeal in ITA No. 3488/Mum/2004 pertaining to Assessment Year 1999-2000

> *"Whether on the facts and circumstances of the case and in law, the Ld.CIT(A) has erred in deleting the addition of Rs.87,53,126/- on account of expenditure incurred in earning income exempt u/s 10(15) of the IT.Act, 1961."*

Revenue's ground of appeal in cross-objection No.174/Mum/2013 pertaining to Assessment Year 1999-2000

"Whether provision of section 14A of the I.T. Act will be applicable in the event it is held that the interest received by the Indian branch from its Head Office is not taxable in the hands of Indian branch office."

Assessee's grounds of appeal in ITA No. 7158/Mum/2004pertaining to Assessment Year 2000-2001

"1. In considering each branch/head office of the same legal entity as separate and distinct entities under the provisions of the Act.

2. In disregarding the tax neutrality of interest of Rs 60,004,090 received by the Appellant on funds placed with its head office/overseas branches, and the interest of Rs 56,09,516 paid by the Appellant in respect of funds placed with it by its head office/overseas branches.

3. Without prejudice to the above, in upholding the disallowance under provisions of section 40(a)(i) of Act in respect of interest paid to overseas branches amounting to Rs 56,09,516.

4. In denying the exemption claimed in respect of interest income earned on overseas placements with non-residents banks, amounting to Rs 199,461.

5. In disallowing the interest of Rs 10,300,131 paid to the Reserve Bank of India for default in maintaining Statutory Liquidity Ratio."

Revenue's grounds of appeal in ITA No. 7217/Mum/2004pertaining to Assessment Year 2000-2001

"1. On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in deleting the addition of Rs. 82,94,531/- on account of expenditure incurred for earning interest on tax free bonds exempt u/s 10(15)(iv)(h) of the IT Act, 1961.

2. On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in holding broken period interest as expenses amounting to Rs. 2,61,45,470/-.

3. i) On the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in holding that, provision in respect of Standard Assets amounting to Rs. 2,16,29,000/- was not a permissible adjustment within the meaning of Explanation below section 115JA, ignoring the fact that amount set aside against standard Assets represented reserves within the meaning of clause (b) of Explanation below section 115JA.

ii) Without prejudice to the above, on the facts and in the circumstances of the case and in law, the Ld. CIT(A) erred in not following the distinction between reserve and provision as explained by Supreme Court in the case of Vazir Sultan Tobacco Co. Ltd. V. CIT (1981) 132 ITR 559 (SC).

The appellant prays that the order of the Ld. CIT(A) on the above grounds set aside and that of the AO restored."

Revenue's ground of appeal in Cross-objection No.175/Mum/2013 pertaining to Assessment Year 2000-2001

"Whether provision of section 14A of the I.T. Act will be applicable in the event it is held that the interest received by the Indian branch from its Head Office is not taxable in the hands of Indian branch office."

Assessee's grounds of appeal in ITA No. 2285/Mum/2005 pertaining to Assessment Year 2001-2002

"1. In considering each branch/head office of the same legal entity as separate and distinct entities under the provisions of the Act.

2. In disregarding the tax neutrality of interest of Rs 27,857,575 received by the Appellant on funds placed with its head office/overseas branches, and the interest of Rs 8,069,725 paid by the Appellant in respect of funds placed with it by its head office/overseas branches.

3. Without prejudice to the above, in upholding the disallowance under provisions of section 40(a)(i) of the Act in respect of interest paid to overseas branches amounting to Rs 8,069,725.

4. In simultaneously taxing the interest paid to the head office/overseas branches, amounting to Rs 8,069,725, as interest income in the Appellant's hand, under the provisions of section 115A of the Act.

5. In denying the exemption claimed in respect of interest income earned on overseas placements with non-residents banks, amounting to Rs 771,043.

6. In not admitting an additional ground of appeal raised by the Appellant during the course of the appellate proceedings. The additional ground is for claiming a deduction under section 37(1) of the Act, for the expatriate salary expense of Rs 14,596,718 borne by the head office of the Appellant, in respect of services rendered by the expatriates in India, wholly and exclusively in connection with the operations of the Indian branch of the Appellant."

Revenue's grounds of appeal in ITA No. 2286/Mum/2005 pertaining to Assessment Year 2001-2002

"1. On the facts and in the circumstances of the case and in law, the Ld. CIT(A) has erred in holding that the assessing officer was not justified in attributing interest cost of Rs. 86,00,191/- as costs incurred to earning the income.

2. On the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in disapproving the action of the assessing officer in disallowing an amount of Rs. 91,46,883/- as interest expenses incurred for earning interest on tax free bonds.

3. On the facts and circumstances of the case and in law, the Ld. CIT(A) has erred in disapproving the action of the assessing officer disallowing broken period interest paid on securities purchased during the year under consideration amounting to Rs. 5,26,87,347/- on the ground that it is a part of the capital cost of the assets."

Revenue's ground of appeal in Cross-objection No.176/Mum/2013 pertaining to Assessment Year 2001-2002

"Whether provision of section 14A of the I.T. Act will be applicable in the event it is held that the interest received by the Indian branch from its Head Office is not taxable in the hands of Indian branch office."

2. We firstly take up the grounds of appeal taken by the Revenue in its respective appeals. In the Revenue's appeal for A.Ys. 1999-2000, 2000-01 and 2001-02, the Revenue has challenged the action of the ld. CIT(A), wherein he has deleted the addition on account of expenditure incurred for earning interest on tax free bonds exempt u/s. 10(15)(iv)(h) of the Act.

3. With the consent of both the parties, the case of the assessee for A.Y. 2000-01 was taken as lead case, wherein briefly, the facts of the case are that the assessee had earned interest income amounting to Rs. 1,22,25,000/- on tax free NABARD bonds of 1996-97 and 1997-98 series which was claimed as exempt u/s. 10(15)(iv)(h) of the Act. The Assessing Officer referring to the provisions of Section 10 of the Act, the CBDT Circular no. 780 dated 04.10.1999 issued in the context of Section 10(23G) of the Act, and the decisions of various Coordinate Benches as well as the Hon'ble Courts held that the assessee is eligible for exemption u/s. 10(15)(iv)(h) of the Act only in respect of "net interest" income and not the "gross interest" income. The Assessing Officer also referred to the provisions of Section 14A of the Act and it was held that in view of the express mandate, no deduction can be allowed to the assessee in respect of the expenditure that it has incurred in earning exempt income. It was held by the Assessing officer that the exemption can be granted to the assessee in respect of that

income only, which is clearly and unambiguously defined u/s. 10 of the Act and the expenditure incurred in earning such an exempt income cannot be allowed by way of deduction and therefore, it is only the "net interest" income which can be allowed as the exempt income. Regarding assessee's argument that it has sufficient interest free funds for making investment in the 1996-97 and 1997-98 series of NABARD bonds, it was held that for want of proof of specific correlation between the funds available on the date of the investment and the investments so made, the contentions so advanced by the assessee cannot be accepted. The Assessing Officer thereafter proceeded and worked out proportionate expenses in earning tax free interest income which was determined at Rs. 82,94,531/- and the exemption claimed by the assessee was revised to the figure of Rs. 39,30,469/- as against the figure of Rs. 1,22,25,000/-, and the exemption u/s. 10(15)(iv)(h) was accordingly restricted to Rs. 39,30,469 as against Rs. 1,22,25,000/- claimed by the assessee.

4. The assessee thereafter carried the matter in appeal before the ld. CIT(A) and necessary submissions were made. The ld. CIT(A) referring to the assessee's financials for the year ended 31/03/2000 recorded his findings stating that the assessee had sufficient own funds to finance the acquisition of tax free Securities. Further, he relied on the order passed by him in assessee's case for A.Y. 1999-2000, dated 24.12.2003, wherein, under identical facts and circumstances of the case, the matter was decided in favour of the assessee and basis the same, the Assessing Officer was directed to delete the disallowance so made by him. Against the said findings, the Revenue is in appeal before us.

5. During the course of hearing, the ld. DR relied on the findings of the Assessing Officer. In his submissions, the ld. AR submitted that the matter is squarely covered by the decision of the Coordinate Benches in assessee's own case right from A.Y. 1998-99 to A.Y. 2005-06 and our

reference was drawn to the decision of the Coordinate Bench in *ITA No. 6818/Mum/2006 &Ors.,* dated 21.04.2023, pertaining to A.Y. 2002-03, wherein the relevant findings are contained in para 6.2 of its order which read as under:

> *"6.2 We have heard the submissions made by rival sides and have examined the orders of authorities below. The CIT(A) in the impugned order has given finding of fact that the assessee has surplus interest free funds in the form of capital and reserves to cover the investment made. Purportedly, no fresh investments were made in the impugned assessment year. The assessee had made investments in NABARD tax free bonds in assessment year 1996-97 and 1997-98. Similar disallowance u/s. 14A of the Act was made by the Assessing Officer in assessment year 1998-99 for earning tax free interest income. The Co-ordinate Bench vide order dated 24/03/2006 (supra) deleted the disallowance. The Hon'ble Apex Court in the case of South Indian Bank Ltd. vs. CIT (supra) has reiterated the legal position, "that the proportionate disallowance of interest is not warranted u/s.14A of the Income Tax Act for investment made in tax free bonds/ securities which yielded tax free dividend and interest to assessee bank in those situation where, the interest free own funds available with the assessee, exceeded their investment.". The Revenue has not disputed the fund position as highlighted by the CIT(A) in the impugned order. Thus, taking into consideration entire facts of the case and the law expounded by Hon'ble Apex Court in this regard, we find no merit in ground no. 1 of the appeal, hence, the same is dismissed.*

6. It was submitted by the ld AR that it is the same bonds which were purchased/invested way back in 1996-97 and 1997-98 in respect of which the assessee has earned tax free interest income which has been claimed as exempt u/s. 10(15)(iv)(h) of the Act and no fresh investments have been made during the year under consideration. It was submitted that the Coordinate Benches have already recorded the finding in the earlier assessment years that the assessee had surplus interest free funds in the form of capital and reserves and no borrowings have been utilized for making the investments,and therefore, following the principle of consistency, the appeal of the Revenue be dismissed and the order of ld. CIT(A) be upheld.

7. We have heard the rival contentions and perused the material available on record. Admittedly, the NABARD tax free bonds were

purchased by the assessee in year 1996-97 and 1997-98 and no fresh investments have been made during the year under consideration. In this regard, we find that matter first came up for consideration before the Coordinate Bench in A.Y 1998-99 wherein similar disallowance was made by the Assessing officer invoking provisions of Section 14A of the Act and the Coordinate Bench vide its order dated 24/03/2006 has deleted the disallowance accepting the assessee's contention regarding availability of interest free funds for making the investments. In A.Y 1999-2000, we find that the ld CIT(A) referring to the financial statements of the assessee for the year ended 31/03/1997, 31/03/1998 and 31/03/1999 has stated that in the year of acquiring tax free bonds, the assessee had sufficient funds available which were interest free. Similar findings have been recorded by the ld CIT(A) for A.Y 2000-2001 and A.Y 2001-02. The said findings of the ld CIT(A) remain unrebutted before us. Therefore, where the same investments continued to be held by the assessee and no fresh investments have been made during the year under consideration, and the matter relating to availability of interest free funds to make the said investments already stood examined by the Coordinate Benches in earlier years, we see no reason to deviate from the view so taken by the Coordinate Benches and find that the ld CIT(A) has rightly deleted the addition so made by the AO and we accordingly upheld the findings of the ld CIT(A).

8. In the result, the sole ground of appeal taken by the Revenue in its appeal for A.Y. 1999-2000, ground no. 1 in its appeal for A.Y. 2000-01 and ground no. 2 in its appeal for A.Y. 2001-02 are dismissed.

9. In its appeal for A.Y. 2000-01 and 2001-02, the Revenue has challenged the action of the ld. CIT(A) in allowing the broken period interest claimed by the assessee. In this regard, briefly, the facts of the case are that during the course of assessment proceedings for A.Y 2000-01, the Assessing Officer observed that the assessee has paid a

sum of Rs. 2,61,45,472/- by way of broken period interest on securities which formed part of its closing stock as on 31.03.2000, and following the decision of Hon'ble Supreme Court in case of *Vijaya Bank Ltd. vs. Additional Commissioner of Income Tax (187 ITR 541)*, it was held that the broken period interest paid by the assessee forms part of the composite price which it had paid for purchasing the securitiesand therefore, the interest paid by the assessee is capital in nature and accordingly, it was held that the assessee is not entitled to claim of deduction for the broken period interest paid during the year under consideration and the addition of Rs. 2,61,45,472/- was made.

10. The assessee thereafter carried the matter in appeal before the ld. CIT(A) and necessary submissions were made. The ld. CIT(A) following the decision of the Hon'ble Bombay High Court in case of *American Express International Banking Company Ltd. v. CIT* reported in *258 ITR 601* decided the matter in favour of the assessee and the Assessing Officer was directed to allow the broken period interest. Against the said findings, the Revenue is in appeal before us.

11. During the course of hearing, the ld. DR relied on the findings of the Assessing Officer. In his submissions, the ld. AR submitted that all the securities were held under current category i.e, as stock-in-trade and reference was drawn to the financial statements for the year ended 31/03/2000 and the submissions made before the Assessing officer during the course of assessment proceedings. It was submitted that the matter is covered by the decision of the Coordinate Bench in assessee's own case for A.Y. 2002-03 and the relevant findings of the Coordinate Bench are contained at para 9.2 of its order which read as under:

> *"9.2. We have heard the submissions made by rival sides. It is no more res- integra that broken period interest is an allowable deduction. The CIT(A) has granted relief to the assessee by placing reliance on the decision of Hon'ble Jurisdictional High Court. There are catena of judgements allowing deduction in respect of broken period interest. The*

Hon'ble Supreme Court of India has dismissed the SLP of the Department in the case of State Bank of India (supra), thereby upholding the order of Hon'ble Karnataka High Court allowing broken period interest as deduction. Thus, we find no infirmity in the impugned order on this issue. Ergo, ground No.4 of the appeal is dismissed."

12. It was further submitted by the ld AR that the matter now stands covered by the decision of the Hon'ble Supreme Court in case of *Bank of Rajasthan Ltd. v. Commissioner of Income Tax*[*2024] 167 taxmann.com 430.* It was submitted that in the said decision, the Hon'ble Supreme Court has referred to earlier decision in Vijaya Bank Ltd as well as decision of the Hon'ble Bombay High Court in case of American Express International Banking Company and held that where securities were held as stock-in-trade, broken period interest has to be allowed as revenue expenditure. It was accordingly submitted that both following the principle of consistency as well as in light of the decision of the Hon'ble Supreme Court in case of Bank of Rajasthan, the appeal of the Revenue be dismissed.

13. We have heard the rival contentions and perused the material available on record. In case of Bank of Rajasthan Ltd *(supra),* the matter for consideration before the Hon'ble Supreme Court was whether deduction for broken period interest can be claimed by the Banks. The Hon'ble Supreme Court referred to its earlier decisions in case of Vijay Bank and held that the same was distinguished by the Hon'ble Bombay High Court in case of American Express International Banking Corporation and which was approved in its earlier decision in case of Citi Bank NA wherein it was held that interest paid for the broken period should not be considered as part of purchase price but should be allowed as revenue expenditure. The Hon'ble Supreme Court thereafter examined the matter relating to whether the securities are held by the Banks as stock-in-trade or not. It held that the Banks are required to purchase Government securities to maintain the SLR and as per RBI's guideline dated 16th October 2000, there are three categories of

securities: HTM (Held to Maturity), AFS (Available for Sale) and HFT(Held for Trade). As far as AFS and HFT are concerned, it was held by the Hon'ble Supreme Court that when these two categories of securities are purchased, obviously, the same are not investments but are always held by Banks as stock-in-trade. Therefore, the interest accrued on the said two categories of securities will have to be treated as income from the business of the Bank and after the deduction of broken period interest is allowed, the entire interest earned or accrued during the particular year is put to tax, thereby, the real income earned on the securities is brought to tax. It was held by the Hon'ble Supreme Court that in these two categories of securities, the benefit of deduction of interest for the broken period will therefore be available to Banks. Regarding securities of the HTM category, it was held that these securities are usually held for a long term till their maturity and are usually valued at cost price or face value. In many cases, Banks hold the same as investments where the securities are held till maturity and are not transferred before or where they are purchased at their cost price or face value. Whether the Bank has held HMT security as investment or stock-in-trade will depend on the facts of each case and is a matter which is within the knowledge of the assessee and where on facts, if it is found that HMT Security is held as an investment, the benefit of broken period interest will not be available and the position will be otherwise if it is held as a trading asset. Thereafter, referring to the facts of the case before it, it was held by the Hon'ble Supreme Court that as the securities were treated as stock-in-trade, interest on broken period cannot be considered as capital expenditure and will have to be treated as revenue expenditure and allowed as a deduction.

14. In the instant case, we find that though there is no material available on record in terms of exact classification of securities as to whether the same are in nature of HTM, AFS and HFT, at the same time, we find that it is a consistent stand of the assessee right from the

assessment proceedings that all the securities are held as stock-in-trade as can be seen from para 7.1 of the assessment order where the Assessing officer has take cognizance of the assessee' submission that the securities constitute its stock-in-trade as they are treated as current investments in its books of accounts, that accrued interest upto the year end is accounted for in the profit/loss account and closing stock is accounted at cost, exclusive of the broken period interest. The Assessing officer thereafter at para 7.2.4 of the assessment order records his finding stating that the assessee pays broken period interest in respect of all the securities purchased during the year, including those securities which are subsequently sold during the year. The Assessing officer further held that the entire amount paid by the assessee by way of broken period interest is capital in nature, however the profit/loss account is adversely affected only by the amount which corresponds to the broken period interest paid by the assessee in respect of those securities which form part of its closing stock and disallowance is restricted to broken period interest in respect of securities purchased during the year and which continued to be in closing stock. We therefore find that the Assessing officer has not disputed that the securities were purchased and held by the assessee as stock-in-trade, that the profit/loss account in respect of securities sold during the year is not affected meaning thereby the profit/loss on sale of such securities has been offered and brought to tax, that the securities purchased which remained unsold were held as part of closing stock. Similar factual position exists for A.Y 2001-02 where the securities were held as stock-in-trade. In light of these undisputed facts, we find that the matter stands covered by the decision of the Hon'ble Supreme Court in case of Bank of Rajasthan (supra) in favour of the assessee and against the Revenue.

15. In the result, ground no. 02 in Revenue's appeal for A.Y. 2000-01 and ground no. 03 in Revenue's appeal for A.Y. 2001-02 are dismissed.

16. In Revenue's appeal for A.Y. 2000-01, it has challenged the action of ld. CIT(A), wherein he has held that provision in respect of standard assets amounting to Rs. 2,16,29,000/- was not a permissible adjustment within the meaning of Explanation to Section 115JA of the Act.

17. In this regard, briefly, the facts of the case are that the assessee has originally filed its return of income declaring income under the normal provisions at Rs. 20,80,40,797/- and book profits as per Section 115JA was computed at Rs. 8,37,06,890/-. The returned income as per the normal provisions was considered as taxable income, being higher than the MAT income. Thereafter, the assessee filed a revised return of income on 18.10.2001 showing total income of Rs. 3,50,95,682/- and MAT income was determined at Rs. 8,37,06,890/- and since MAT income was higher than the income as per the normal provisions, the same was considered for the purposes of computation of tax payable by the assessee. Thereafter, during the course of assessment proceedings, the assessee vide letter dated 20.02.2003 submitted that its income under the revised return of income is taxable under the provisions of Section 115JA of the Act. However, a sum of Rs. 2,16,29,000/- being provision for standard assets has been considered as a disallowable item while computing the book profits, however, the same is an allowable deduction while computing the book profits u/s. 115JA of the Act. In support, reliance was placed on the Coordinate Mumbai Benches decision in case of *Maharashtra State Electricity Board vs JCIT [2002] 82 ITD 422 (Mum.).* The submissions so filed by the assessee were considered but not found acceptable to the Assessing Officer. As per Assessing Officer, Explanation (c) to Section 115JA(2) clearly provides for disallowance of the provisions made while computing the book profits for the purposes of Section 115JA of the Act. Further, the decision in case of *Maharashtra State Electricity Board (supra)*was

distinguished as in that case, the issue under consideration was whether MSEB was subject to the provisions of Section 115JA or not and in that background, it was held that the Tribunal was not concerned with the provision made for bad debts.

18. Against the said order and the findings of the Assessing Officer, the assessee carried the matter in appeal before the ld. CIT(A) and it was submitted that for a particular provision to be added back in computing the book profits for the purposes of MAT liability for a particular year, it would have to fall within one of the adjustments prescribed in Section 115JA of the Act. It was submitted that Section 115JA provides that the amount or amount set aside towards provision made for meeting liabilities, other than ascertained liabilities are to be added back for computing book profits and in the instant case, the assessee had made a provision for standard assets which amounts to restating the value of an asset, that is loan or advance by the assessee and therefore, the same should not be added back while computing the book profits for MAT purposes and in support, reliance was placed on the decision of Coordinate Calcutta Benches in case of *Usha Martins Industries Ltd. vs. Joint Commissioner of Income Tax (81 TTJ 518)*.

19. The ld. CIT(A) following the decision in case of *Maharashtra State Electricity Board (supra)*as well as in case of *Usha Martins Industries Ltd. (supra)* held that the provision for standard assets are provision for assets and not liabilities and accordingly, should not be added in computing the book profits and the Assessing Officer was directed not to add the provision for standard assets, for the purposes of computing the book profits u/s. 115JA of the Act.Against the said findings, the Revenue is in appeal before us.

20. During the course of hearing, the ld. DR relied on the order of the Assessing Officer while the ld. AR supported the order of the ld. CIT(A).

It was submitted that the amount debited to the profit/loss account as provision for standard asset was ex-facie not covered by the explanation (c) to section 115JA of the Act and reliance was placed on the decision of the Special Bench of the Tribunal in case of *Usha Martin Industries Ltd.(supra)* which was upheld by the Hon'ble Delhi High Court in case of *CIT v. Eicher Ltd.[2006] 287 ITR 117* and thereafter the Hon'ble Supreme Court in case of *Commissioner of Income-tax, Delhi vs. HCL Comnet Systems & Services Ltd. [2008] 174 Taxman 118 (SC)/[2008] 305 ITR 409 (SC),* held that the debt is the amount receivable by the assessee and not any liability payable by the assessee and, therefore, any provision made towards irrecoverability of the debt cannot be said to be a provision for liability. It was further submitted that Section 115JA has no application to the assessee as it is governed by the provisions of the Banking Regulation Act 1949 and in view of section 29, it is not required to prepare its accounts as per Part II and III of schedule VI of the Companies Act and in support, reliance was placed on the decision of Coordinate Benches in case of *Standard Chartered Bank v. JCIT [2019] 104 taxmann.com 236 (Mumbai-Trib.)* wherein, it was held that Section 115JA would not be applicable to the assessee being a banking company maintaining its account under the Banking Regulation Act, 1949. Further, reliance was placed on the decision of the Coordinate Delhi Benches in case of Bank of Tokyo Mitsubishi UFJ Ltd vs ADIT [2014] 49 taxmann.com 441 (Delhi-Trib.).

21. We have heard the rival contentions and perused the material available on record. We find that though the amount debited to the profit/loss account as provision for standard asset was not covered by the explanation (c) to section 115JA of the Act, however, the same is covered by explanation (g) to section 115JA of the Act which has been brought in by the Finance Act, 2009 with retrospective effect from 1-4-1998. Explanation (g) talks about “the amount or amounts set-aside as provision for diminution in the value of the any asset” and thus, it will

cover provision for standard assets. The said amendment has been brought in apparently after the decision of the Hon'ble Supreme Court in case of HCL Comnet Systems and Services Ltd. Therefore, as per the provisions of section 115JA as applicable for the impugned assessment year 2000-2001, in view of explanation (g) to section 115JA, the books profits needs to be adjusted by provisions for standard assets so made by the assessee in the profit/loss account and the contentions raised by the ld AR in this regard cannot be accepted.

22. At the same time, a related contention which has been raised by the ld AR is that the provisions of section 115JA are not applicable to the assessee, being a banking company maintaining its accounts under the Banking Regulations Act, 1949 and in view of Section 29, it is not required to prepare its accounts as per Part II and III of schedule VI of the Companies Act as supported by the decisions of the Coordinate Benches and therefore, the whole exercise of working out the adjustments to the books profits is in effect academic in nature and therefore, the ground of appeal so raised by the Revenue be dismissed.

23. On a query from the Bench as to whether such an objection on applicability of section 115JA can be raised at this stage especially where the assessee has itself computed its income u/s 115JA of the Act in its return of income, it was submitted by the ld AR that it is permissible for the assessee to raise this objection for the limited purposes of opposing the ground raised by the Revenue and in support, reliance was placed on the decision of the Hon'ble Bombay High Court in case of B.*R.Bamasi vs CIT [1972] 83 ITR 223 (Bom)* and the relevant findings therein read as under:

> *"In the second reference the Tribunal has decided one additional point. It is a point of law. As stated earlier, the assessee filed a voluntary return on the 28th March, 1952. Nonetheless, the Income-tax Officer issued a notice to the assessee under section 34(1)(a) on 9th of July, 1952, and then proceeded to assess the assessee under that section. The assessee raised before the Tribunal a contention that the notice under section 34(1)(a) having been issued in spite of*

the assessee having filed a return in proper time, it was invalid and that the appeal filed by the department before the Tribunal should be dismissed. In support of his contention that the notice was invalid in law the assessee relied upon the decision of the Supreme Court in Commissioner of Income-tax v. Ranchhoddas Karsondas [1959] 36 ITR 569; [1960] 1 SCR 114 (SC). The Tribunal, however, did not allow the assessee to raise that contention on the ground that it had been raised only at the time of the arguments in the appeal before the Tribunal as a fresh ground and that if the ground was allowed to be urged and it succeeded, the result would be that the entire assessment proceedings would have to be held invalid and even the assessment on the undisputed amount of the income against which the assessee had not appealed would thereupon go by the board. The assessee had contended before the Tribunal that he wanted to urge that ground only for having the appeal of the department dismissed and stated that he did not want to disturb the assessment as already made by the Appellate Assistant Commissioner. The Tribunal, however, held that it could not permit a legal and an illegal order to stand side by side because once the plea was allowed to be raised and it was accepted the entire order of the Appellate Assistant Commissioner would stand vitiated. The Tribunal refused to allow the assessee to raise and argue that ground because of such difficulty which the Tribunal felt would arise.

Now there is no doubt that, as the assessee had already filed a voluntary return, the notice under section 34(1)(a) was wrongly issued and the proceedings of assessment which took place in pursuance of that notice are invalid. This is the ratio laid down by the Supreme Court in its said judgment in the case of Commissioner of Income-tax v. Ranchhoddas Karsondas [1959] 36 ITR 569 ; [1960] 1 SCR 114 (SC). Mr. Joshi has not disputed this position. The only question is whether the Tribunal was entitled in law to refuse to allow the assessee to urge that ground in the appeal before it. Now a Division Bench of this High Court in Commissioner of Income-tax v. Hazarimal Nagji & Co. [1962] 46 ITR 1168 (Bom.), after considering the relevant sections of the Income-tax Act and the relevant Rules made thereunder, held that the powers of the Appellate Tribunal are similar to the powers of an appellate court under the Civil Procedure Code. It has further held that the respondent in an appeal is undoubtedly entitled to support the decree which is in his favour on any grounds which are available to him, even though the decision of the lower court in his favour may not have been based on those grounds. It has further held that if the appellant in his challenge to the decree of the lower court is entitled to take a new ground not agitated in the court below by leave of the court, there appears to be no reason why a respondent in support of the decree in his favour passed by the lower court should not be entitled to agitate a new ground and subject to the same limitation. A Division Bench of the Allahabad High Court has taken a similar view in Kanpur Industrial Works v. Commissioner of Income-tax [1966] 59 ITR 407 (All.). That judgment has considered the position of an appeal under section 33 of the Income-tax Act along with the relevant Rules and that of an appeal under the Code of Civil Procedure and the provisions of Order XLI, rule 22. The judgment holds that when the department files an appeal for an increase in the assessed income, the subject-matter of the appeal is the increase claimed by the department and the assessee can urge any ground of defence even though it might have been rejected by the Appellate Assistant Commissioner for showing that there should be no

increase. It has further held that that the assessee is not liable to be assessed at all is a ground for showing that there should be no further assessment and the department's appeal can therefore be resisted on that ground and that there is no incongruity in maintaining the assessment order passed against the assessee and yet refusing to increase it on the ground that he was not liable to be assessed at all. The judgment points out however that if the Tribunal accepts the ground of defence that the assessee was not liable to be assessed, it can only refuse to increase the assessed income as only such an order would be within the scope of the appeal filed by the department and any other order such as annulling the assessment would be outside the scope of the appeal. That judgment holds that the position of an appeal under section 33 of the Income-tax Act and an appeal under the Code of Civil Procedure is identical. A Full Bench of the Madras High Court has in Venkata Rao v. Satyanarayanamurthy ILR 1944 Mad. 147; AIR 1943 Mad. 698 [FB], held that it was open to a respondent in appeal who had not filed cross-objection with regard to the portion of the decree which had gone against him to urge in opposition to the appeal of the plaintiff a contention which if accepted by the trial court would have necessitated the total dismissal of the suit, but the decree in so far as it was against him would stand. The judgment of the Tribunal in our case clearly shows that, although the assessee wanted to raise a new point as a ground of defence in the appeal, he specifically stated that he wanted to rely upon it only for the purpose of having the appeal by the department for enhancement in income-tax dismissed. But even if the assessee had not made such a statement, the above judgment shows that the assessee would be entitled to raise a new ground, provided it is a ground of law and does not necessitate any other evidence to be recorded, the nature of which would not only be a defence to the appeal itself, but may also affect the validity of the entire assessment proceedings. If the ground succeeds, the only result would be that the appeal would fail. The acceptance of the ground would show that the entire assessment proceedings were invalid, but yet the Tribunal which hears that appeal would have no power to disturb or to set aside the order in favour of the appellant against which the appeal has been filed. The ground would serve only as a weapon of defence against the appeal. If the respondent has not himself taken any proceedings to challenge the order in appeal, the Tribunal cannot set aside the order appealed against. That order would stand and would have full effect in so far as it is against the respondent. The Tribunal refused to allow the assessee to take up this ground under an incorrect impression of law that if the point was allowed to be urged and succeeded, the Tribunal would have not only to dismiss the appeal, but also to set aside the entire assessment. The point would have served as a weapon of defence against the appeal, but it could not be made into a weapon of attack against the order in so far as it was against the assessee."

24. We find that as far as applicability of section 115JA to the banking companies are concerned, the Coordinate Mumbai Benches in case of *Standard Chartered Bank (supra)* has held that the provisions of

section115JA are not applicable and the relevant findings therein read as under:

> *"**8.** We have considered rival submissions and perused material on record. The main plank of assessee's argument against applicability of section 115JA of the Act is, assessee being a banking company maintaining its accounts under the Banking Regulations Act, 1949, the provision contained under section 115JA of the Act will not apply. Undisputedly, the assessee is a banking company and has opened its branches in India after obtaining permission of the RBI. Therefore, the assessee is governed under the Banking Regulations Act, 1949. Section 115JA of the Act provides for computation of total income chargeable to tax to be an amount equal to 30% of the book profit in case such income is less than 30% of the book profit. However, sub- section (2) of section 115JA of the Act mandates that the company for the purpose of section 115JA of the Act has to prepare its Profit & Loss Account in accordance with the provisions of Part-II & III of Schedule- VI of the Companies Act, 1956. Undisputedly, the assessee being governed under the Banking Regulations Act, 1949, is not required to prepare its Profit & Loss Account under the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. That being the case, the provisions of section 115JA of the Act are not applicable to the assessee. The Tribunal, Mumbai Bench, in Krung Thai Bank PCL v. Jt. DIT (International Taxation) [2011] 16 taxmann.com 239/[2012] 49 SOT 70 (Mum)(URO) has held that the provisions of section 115JB of the Act, which is more or less pari-materia to section 115JA of the Act, can only come into play when the assessee is required to prepare its Profit & Loss Account in accordance with the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956. It was observed by the Branch that the starting point of computation of minimum alternate tax (MAT) is the result shown by such Profit & Loss Account. Since, in case of Banking company, the provisions of Schedule-VI of the Companies Act, 1956 are not applicable, as, they are required to prepare their accounts under the provisions of Banking Regulations Act, the provision of section 115JB will not be applicable. The other decisions cited by the learned Sr. Counsel for the assessee also support this view. Further, the Tribunal, Mumbai Bench, in Maharashtra State Electricity Board v. Jt. CIT [2002] 82 ITD 422 (Mum.), has held that since the assessee is not constituted as a company under the Companies Act, 1956, the provisions of section 115JA of the Act cannot be applied. While doing so, the Bench further observed that since the assessee Corporation is not required to distribute any dividend, it cannot be considered to be a company under the Companies Act, 1956. The facts involved in assessee's case are more or less identical to the facts of MSEB (supra). In view of the aforesaid, we hold that the provisions of section 115JA of the Act are not applicable to the assessee. This ground is allowed."*

25. In light of the aforesaid discussion, following the decision of the Hon'ble Bombay High Court in case of B.R. Bamasi *(supra),* for the

limited purposes of adjudication of the ground of appeal so taken by the Revenue, we accept the alternate contention so raised by the ld AR and hold that the ground so raised by the Revenue becomes academic where the provisions of section 115JA are itself not applicable to the assessee company, being a banking company governed under the Banking Regulations Act, 1949 and not required to prepare its Profit & Loss Account under the provisions of Part-II & III of Schedule-VI of the Companies Act, 1956.

26. In the result, ground no. 03 in Revenue's appeal for A.Y. 2000-01 is dismissed as infructious.

27. In Revenue's appeal for A.Y. 2001-02, the Revenue has challenged the action of the ld. CIT(A) in holding that the Assessing Officer was not justified in attributing interest cost of Rs.86,00,191/- as cost incurred in earning of income which is eligible for concessional tax rate of 20% under the provisions of Section 115A of the Act.

28. In this regard, briefly, the facts of the case are that during the course of assessment proceedings, the Assessing Officer observed that the assessee has earned interest income amounting to Rs. 2,69,89,233/- from foreign currency loans given to Indian Corporates which is taxable as per concessional rate under Section 115A of the Act. Referring to the provisions of Section 115A, the Assessing Officer stated that it applies to interest income of a non-resident on account of loans extended in foreign currency. Further, reference was drawn to the words "interest received" used in Section 115A(1)(a)(ii) whereas the words used in Section 115A(1)(B) are "the amount of income by way of interest referred to in sub-clause (ii)". It was held that the lower rate of tax of 20% is to be applied to the amount of income arising to the assessee from interest received by it, which is covered by the provisions of Section 115A(1)(a)(ii) of the Act.It was held that where the lower rate of tax is not applied to the net income arising to the assessee, the

assessee would be reducing its tax liability by claiming set-off of the expenditure incurred in earning income covered by Section 115A against remaining income which is chargeable to tax at a much higher rate and which can never be the intention of the legislature. Further, the assessee was asked to submit details of the expenditure incurred in earning this income and as per the submissions of the assessee, the interest cost attributed to the deposits covered by the provisions of Section 115A(1)(a)(ii) comes to Rs. 86,00,191/-. Accordingly, the Assessing Officer worked out the net interest income amounting to Rs. 1,77,89,042/- which is eligible for concessional tax rate of 20% under the provisions of Section 115A of the Act.

29. The assessee thereafter carried the matter in appeal before the ld. CIT(A) and reference was drawn to the provisions of Finance Act,1976, whereby provisions of Section 115A were introduced in the statute. Reference was also drawn to the CBDT circular No. 684, dated 06.06.1994 (208 ITR (ST) 8). Further, reference was drawn to Article 10 and 11 of India-Canada Tax Treaty which talks about taxation on gross basis. The ld. CIT(A) considered the submissions so filed by the assessee and noted that his predecessor CIT(A) examined the similar issue in A.Y. 1997-98, wherein vide order dated 31.12.2000, the matter was decided in favour of the assessee and subsequently, the Mumbai Benches of the Tribunal have confirmed the said view and has held that the interest income on foreign currency loans are taxable on gross basis u/s. 115A of the Act and following the same, the matter was decided in favour of the assessee. Against the said order, the Revenue is in appeal before us.

30. During the course of hearing, the ld. DR relied on the order of the Assessing Officer, whereas the ld. AR supported the findings of the ld. CIT(A). It was submitted that in respect of A.Y. 1999-2000, the AO himself has not raised any dispute on the gross basis of taxation and

for A.Y. 2000-2001, the ld. CIT(A) has decided the matter in favour of the Revenue. However, the Revenue has not filed any appeal against the said findings of the ld. CIT(A) and it is only in A.Y. 2001-02, where the Revenue has challenged the action of the ld. CIT(A). It was submitted that the matter is squarely covered by the decision of Coordinate Benches for various assessment years starting from A.Y. 2002-03 to A.Y 2010-11 and our reference was drawn to the Coordinate Bench decision for A.Y. 2002-03, wherein the relevant findings are contained at paragraph 7.1 of its order which reads as under:

> *"7.1 We have heard the submissions made by rival sides. We find that in assessment year 1997-98 identical disallowance was made by Assessing Officer, the CIT(A) deleted the same, the Revenue carried the issue in appeal before the Tribunal in ITA No.306/Mum/2001. The Co-ordinate Bench vide order dated 21/04/2004 dismissed the ground raised in the appeal of Revenue by observing as under:-*
>
> > *"3. We have heard the rival submissions and also perused the orders of authorities below. Parties appearing before us have respectively relied upon the order of A.O and CIT(A). Since the introduction of section 115A certain changes have been made and with the passage of time the Finance Act 1994 has also carried out certain amendments in the said section w.e.f. 1/4/95 the scope and effect of the amendments was explained by CBDT in Circular No.684 dated 6/6/94(208 ITR 08(St.), relevant page-43. This CBDT circular and related provisions of IT Act has been elaborately discussed by the first appellate authority. On careful examination of the entire issue it is abundantly clear that the legislature has intended to tax the interest only on gross basis. Further in support of his arguments Id. A.R has also cited Article 10& 11 of DTAA with Canada. Notification No.10503(F No.505/2/87-FTD) reference 229 ITR 44(St.) Further it has also been mentioned that section 90(2) of IT Act also provides that the provisions of this Act shall apply to the extent they are more beneficial to that assessee. The order of the first appellate authority is quite elaborate on this subject and needs no interference, therefore, under the totality of the circumstances and in view of the specific provisions of the Act we hereby dismiss this ground of the Revenue."*
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> *The Revenue has failed to distinguish the above order of Tribunal. Hence, following the order of Co-ordinate Bench in assessee's own case on the same issue, we have no hesitation in dismissing ground No.2 of the Department's appeal."*

31. We have heard the rival contentions and perused the material available on record. Sub-section (1) of Section 115A *interalia* provides that where the total income of a foreign company includes any income by way of interest received from an Indian concern on monies borrowed or debt incurred by the Indian concern in foreign currency, the amount of income tax calculated shall be at the rate of 20 percent on the amount of income by way of interest so referred included in the total income. Sub-section (3) further provides that no deduction in respect of any expenditure or allowance shall be allowed to the assessee under section 28 to 44C and section 57 in computing its income referred to in sub-section (1). The provisions thus provides for gross basis of taxation without deduction in respect of any expenditure or allowance in relation to such income. In other words, the gross interest receipts are brought to tax and neither the assessee can claim nor the Assessing officer can determine and allow any expenditure or allowance in relation to such interest receipts. The Coordinate Benches have consistently held that the legislature has intended to tax interest income on gross basis and there cannot be any dispute in this regard. Therefore, in the instant case, the gross interest receipts of Rs. 2,69,89,233/- is eligible for concessional tax rate of 20% under the provisions of Section 115A of the Act and the findings of the ld CIT(A) are confirmed.

32. Before parting, a question that arises for consideration is where the assessee has incurred certain expenditure in relation to earning and receipt of such interest income as referred to in Section 115A, what happens to such expenditure for the purposes of computing the gross total income and how the provisions of sub-section (3) of section 115A have to be read in this regard. Since the said issue has not been agitated or any arguments been advanced by either of the parties, the same has not been dealt with by us.

33. In the result, ground no. 01 in Revenue's appeal for A.Y. 2001-02is dismissed.

34. Now, we take up the grounds of appeal taken by the assessee in its respective appeals.

35. In assessee's appeal for A.Y. 1999-2000, 2000-01 and 2001-02, the assessee has challenged the action of ld. CIT(A) in disregarding the tax neutrality claimed in respect of interest received by the assessee on funds placed with its head office/overseas branches and interest paid by the assessee in respect of funds placed with it by its head office/overseas branches.

36. With the consent of the parties, the case of the assessee in A.Y. 2000-01 was taken as a lead case, wherein, briefly, the facts of the case are that during the course of assessment proceedings, the Assessing Officer, from perusal of the details filed by the assessee and the computation filed along with the return of income, observed that the assessee has received a sum of Rs. 6,00,04,090/- by way of interest on its balances lying in NOSTRO accounts with its head office/overseas branches and the assessee has not offered this income for taxation and the necessary explanation was called for as to why this sum should not be brought to tax. In its submission, the assessee submitted that the interest received by it on its balances lying in its overseas account with its head office/overseas branches should not be brought to tax for the reason that the branches of the Bank in India and the branches of the bank outside India and the head office constitute one single entity and they cannot arise any profit as a result of the transaction between two parts of the same entity.

37. The submissions so filed by the assessee were considered but not found acceptable to the Assessing officer. As per the Assessing Officer, the NOSTRO accounts maintained by the assessee with its branches

overseas are nothing but the bank account of the Indian branch with the head office/overseas branches. The interest earned by the Indian branch on the balances lying in the accounts overseas is the income of the Indian branch and accordingly, credited to its account maintained in India in respect of operations carried out by the Indian branch in India. It was held that the funds raised by way of deposits by the Indian branch which are temporarily placed in the NOSTRO accounts are shown in the balance sheet also. Thus, the interest arising to the Indian branch from such funds is income of the assessee in respect of operations carried out by the assessee in India. It was further held by the AO that the source of this deposit is ultimately the banking operations carried out by the assessee in India and therefore, the interest earned from the placement of such funds by their deposit overseas is covered by the definition of income accruing or arising directly or indirectly out of business connection in India and such income is covered by the provisions of Section 9(1)(i) of the Act read with the explanation thereto.

38. Further, reference was drawn to the provisions of Section 9(1)(v)(c) of the Act and it was held by the Assessing officer that the interest in question is paid by a non-resident that is the head office of the assessee bank and the said interest is payable in respect of debt incurred or money borrowed and used for the purposes of business or profession carried on by such person in India and reference was drawn to the explanatory note to the Finance Bill,1976. Further, reference was drawn to the Circular No. 740 dated 17.04.1992 issued by the Central Board of Direct Taxes, wherein, it has been clarified that the branch of a foreign company/concern in India is a separate entity for the purposes of taxation and the interest paid/payable by such branch to its head office or any branch located abroad would be liable to tax in India and would be governed by the provisions of Section 115A of the Act and consequently, the tax would have to deducted on the interest remitted

as per the provisions of Section 195 of the Act. Further, reference was drawn to the provisions of Article 7(2) of the Double Taxation Avoidance Agreement (DTAA), wherein, it has been provided that the profits of the company's establishment are to be computed as if it were a distinct and separate entity engaged in same or similar activities under the same or similar conditions and dealing only independently with the enterprise of which it is a common establishment. It was accordingly held by the Assessing Officer that for the purpose of computing the income of the assessee in India, the branch has to be considered as a separate entity and the contentions so advanced by the assessee were rejected and the sum of Rs. 6,00,04,090/- being interest income arising to the assessee from its funds lying in overseas accounts with its overseas branches were brought to tax.

39. The Assessing Officer further noted that the assessee has paid a sum of Rs. 6,70,355/- to its head office/overseas branches on account of funds obtained from them and the assessee was asked to show cause as to why the deduction for the said payment should not be disallowed in terms of provisions of Section 40(a)(i) of the Act. Rejecting the argument of the assessee that the interest payment by the permanent establishment to its head office is not in the nature of income because it is a payment to self, it was held by the Assessing Officer that had it been so then the assessee should also not have treated this payment to be an expense in its hands, whereas, the assessee has claimed deduction for the payment of this interest in its accounts from which it is clear that the assessee itself is treating this interest payment to be an expenditure in its hands and where the payment is claimed to be an expenditure in the hands of the permanent establishment correspondingly, the receipt in the hands of the head office would be the nature of income of the head office. It was accordingly held that on account of the failure of the assessee to deduct TDS and in terms of the provisions of Section 40(a)(i) of the Act, the claim of deduction of Rs.

6,70,355/- on account of payment of interest to the head office/branch office is disallowed.

40. The assessee thereafter carried the matter in appeal before the ld. CIT(A).As per ld. CIT(A), the assessee being a foreign bank is permitted by the Reserve Bank of India to undertake banking business in India, it receives as a part of its banking business, deposits in designated foreign currencies under various schemes stipulated by the RBI for example FCNR(B) scheme and one of the permitted lending options is to lend the amount so received in the overseas overnight call money market in which institutions like banks participate. The Indian branches of the assessee therefore, places the deposits received by them with their overseas branches and for tax purposes it has claimed exemption in respect of the net amount of interest. It was noted by the ld CIT(A) that the main contention of the assessee for claiming this exemption is that the said interest is receipt of the payment to self and therefore, cannot be construed as income or expenditure. The ld. CIT(A) however, did not find the submissions so made by the assessee as acceptable and relied on his findings for A.Y. 1999-2000 as well as the decision of Coordinate Mumbai Benches in case of *Credit Agricole Indosuez (ITA Nos. 2089 to 2091/Bom/1991 and ITA Nos. 2472, 1954 and 1955/Bom/1991), dated 09.03.1998*. Referring to the decision in the case of Credit Agricole Indosuez (supra), the ld CIT(A) noted that the Coordinate Bench in the said case had held that what was to be determined in the case of assessee foreign bank was not its world income but only the income attributable to its permanent establishment in India in terms of the Double Taxation Avoidance Agreement between India and France. As the income of the assessee from the permanent establishment in India was to be assessed as a separate unit from its overall world income, both the receipts and payment of interest from/to head office and overseas branches had to be taken into consideration, while determining the income of the assessee. The assessee bank had sought

to contend before the ITAT that receipt/payment of interest from/to head office and overseas branches represented receipts/payment from self, as the head office of the assessee bank together with its branches constituted a single organization and had sought to rely on the decision of Calcutta High Court in the case of *Betts Hartley Huett & Co. (116 ITR 425)* and an earlier decision of ITAT Bombay *dated 20.08.1982 in the case of City Bank, N.A.* in support of the contention. The Coordinate Bench however held that the facts of the assessee bank's case were distinguishable from the facts in the above cases and subsequently vide its order dated 20.09.2000, had also refused to make any reference on the issue to Bombay High Court *(R.A. No. 762 & 763/Mum/98)* and rejected the reference applications made by the assessee bank.

41. It was held by the ld CIT(A) that the contention of the appellant bank that such interest payment to head office etc. would have to be ignored, as it was a transaction with self cannot be accepted. The maxim that in computation of income of an entity, receipts from different parts within the entity should be ignored is applicable only in the situation of computation of the global income of the entity. When we have to determine, not the global income of the appellant bank, but only a part of its income, which has accrued or arisen in India, the above maxim would not be applicable. It was held that Calcutta High Court in the case of Betts Hartley Huett & Co. *(Supra)* had primarily held that since no commission was charged by the Indian branch of the assessee company on purchases made on behalf of the head office, no such notional commission should be construed to have accrued to the Indian branch. The impossibility of application of the above maxim, in the matter of computation of Indian income of a non-resident assessee under Indian I.T. Act can be illustrated with the help of a practical example. If a non-resident, who manufactures goods abroad has a selling branch in India, which procures orders from customers in India, delivers goods and collects sale proceeds of goods and remits such sale

proceeds abroad, and in return receives a sales commission from the head office, or is allowed to sell goods at a price higher than the price at which such goods are transferred to it by the head office and retain the difference, is it to be concluded that no income has accrued to the non-resident in India from its sales activities because the transactions between the head office and the selling branch would have to be ignored, as transactions with self. For that matter if the Indian branch of the appellant bank was permitted by R.B.I. to invest all its funds, including funds borrowed from India, abroad, would it mean that no income has accrued to the appellant bank in India.

42. On the question of deduction of tax at source on payment of interest to head office/overseas branch, it was held by the ld CIT(A) that it would be illogical to hold that the appellant bank would be entitled to deduction in respect of interest paid on funds borrowed either in India or abroad for the purpose of business in India, in computation of its business income under Indian I.T. Act without complying with other relevant provisions like section 195 and section 40(a)(i) of the Act. In fact, the CBDT in no uncertain terms has clarified the issue in its Circular No. 740 dated 17.04.1996 which explains that the branch of a foreign' company/concern in India is a separate entity for the purpose of taxation and interest paid/payable by such branch to its head office or any branch abroad would be liable to tax in India. Consequently, tax would have to be deducted accordingly on the interest remitted as per the provisions of Section 195 of the Act. It is an established principle of international taxation that computation of income of a PE is always in accordance with the provisions of the domestic law. Therefore, there remains no doubt that the appellant has failed to comply with the provisions of section 195 of the I.T. Act and therefore the payment of interest to Head Office/overseas branch does not remain allowable in terms of provisions of section 40(a) (i) of the I.T. Act. The action of the A.O. was upheld and the ground of appeal so taken by the assessee

Further, the A.O. was directed to take the correct amount of interest paid to Head Office/overseas branches at Rs. 56,09,516/- instead of Rs. 6,70,355/- for the purpose of disallowance under section 40(a)(i) of the I.T. Act.

43. Against the said order and the findings the ld. CIT(A), the assessee is in appeal before us. During the course of hearing, the ld. AR submitted that the assessee had three sources of overseas interest income namely interest income received from money lying with head office/overseas branches, interest income from third party overseas bank and interest income from foreign currency loans provided to the Indian corporates outside of India. Regarding interest income from third party overseas bank, it was submitted that the same is a subject matter of separate ground of appeal and wherein, the assessee has claimed the same to be non-taxable u/s. 9(1)(v)(c) of the Act and the matter stand covered by the earlier decision of the Coordinate Benches. Regarding interest income from foreign currency loans provided to the Indian corporates outside India, it was submitted that the same has been duly offered to tax on gross basis u/s. 115A of the Act and in that case, the dispute is limited to gross versus net basis of taxation and the same is again subject matter of separate ground of appeal and covered in favour of the assessee by the earlier decision of the Coordinate Bench.It was accordingly submitted that as far as subject grounds of appeal is concerned, the limited dispute relates to interest income received from money lying with the head office/overseas branches and interest paid to head office/overseas branches. It was submitted that the assessee in its computation of income has reduced the interest received by the Indian branch office from the head office/overseas branches from the profit determined in the profit and loss account and the amount paid by the Indian branch office to the head office/overseas branches was also added to the profit determined in the profit and loss account, thereby, keeping a consistent stand that the transaction between the assessee

and its head office/overseas branches are transaction with itself and therefore, tax neutral. It was submitted that the matter stands covered by the decision of the Hon'ble Delhi High Court in case of *Commissioner of Income-tax (International Taxation) vs. Bank of Tokyo-Mitsubishi UFJ Ltd. [2024] 162 taxmann.com 872 (Delhi) [28-05-2024],* the decision of the Special Bench in case of *Sumitomo Mitsui Banking Corporation vs.DDIT [2012] 19 taxmann.com 364 (Mum.) (SB)*as well as the decision of the Coordinate Benches in assessee's own case for A.Y.2002-03 to 2005-06, wherein, the Tribunal has allowed the ground of appeal raised by the assessee and dismissed the grounds raised by the Revenue in effect holding that the transactions between head office/overseas branches and permanent establishment are transactions with self and therefore, tax neutral. It was accordingly submitted that following the same, the necessary relief be provided to the assessee.

44. The ld. DR has been heard, who has relied on the order passed by the Assessing Officer as well as that of the ld. CIT(A).

45. We have heard the rival contentions and pursued the material available on record. The limited contention which has been raised before us relates to tax neutrality of the transactions between the assessee and its head office/overseas branches whereby interest received by the assessee from its head office/overseas branches not chargeable to tax in India and interest payment by the assessee to its head office/overseas branches not allowable for tax purposes under the domestic laws. The contention of tax neutrality is premised on the proposition that the assessee and its head office/overseas branches are one and same; and one cannot make profit from itself. We find that the said issue came up for consideration before a five-member Special Bench in case of Sumitomo Mitsui Banking Corporation *(supra)* in the context of chargeability of interest paid by the branch to the Head office

and deductibility of interest so payable in the hands of the branches in India. It was held by the Special Bench that the Branch office and the head office, of which the branch office is part, are not independent persons under the domestic laws and they are assessable to tax as one person and not assessed to tax separately in India. Further, referring to the decision of the Hon'ble Supreme Court in case of Sir Kikabhai Premchand and Hon'ble Calcutta High Court in case of Betts Hartley Huett & Co Ltd, it was held that the position under the domestic law is clear that one cannot make profit out of itself and if the payment of interest made by the Indian Branch to its head office overseas of which it is part is payment to self, it cannot give rise to any income which is chargeable to tax in India as per domestic laws. It was accordingly held that such interest payment cannot be brought to tax in the hands of the head office in India and also, cannot be claimed as expenditure in the hands of the branch office in India.

46. Following the aforesaid decision of the Special Bench in case of *Sumitomo Mitsui Banking Corpn.(supra),* the Coordinate Mumbai Bench in case of *ACIT vs. Credit Agricole Indosuez Ramon House, ITA No. 6615/Mum/2003, dated 12.09.2012, for A.Y. 1997-98*, directed the Assessing Officer to exclude the amount of interest / commission received by the Indian PE from its overseas HO / branches and also not to grant deduction in respect of interest incurred towards overseas HO/branches and the relevant findings reads as under:

> *"23. We have heard the rival submissions and perused the relevant material on record. It is apparent from para nos.55 and 56 of the Special Bench order that under the provisions of the Income-tax Act, 1961 the taxable entity is only one i.e. overseas GE and the PE in India is a part of that entity. It is the overseas GE which has been held to be chargeable to tax in respect of income attributable to the PE in India. Once mutuality is found between overseas HO and branch in India, there can be no interest income by the Indian branch from its overseas HO or branches under the provisions of the Act. It is relevant to mention that the Special Bench of the Tribunal, while laying down this proposition, has duly considered the case of Dresdner Bank AG in its order. The later order passed by the Mumbai*

Bench of the Tribunal in Oman International Bank S.A.O.G. (supra) has also taken similar view. In view of the fact that the Special Bench of the Tribunal in the case of Sumitomo Mitsui Banking Corpn. has held that no interest / commission received by the Indian PE from the HO can be charged to tax, there can be no question of following any contrary view expressed by the division bench of the Tribunal prior to the passing of the order by the Special Bench.

24. Here we will like to record that the learned AR has very fairly admitted that the interest paid by the Indian PE to its overseas HO/branches should also not be allowed as deduction so as to bring symmetry between interest income and interest incurred from or to HO. The impugned order is, therefore, set aside and the matter is restored to the file of A.O. to exclude the amount of interest / commission received by the Indian PE from its overseas HO / branches and also not to grant deduction in respect of interest incurred towards overseas HO / branches."

47. Recently, the Coordinate Mumbai Benches in case of *DDIT vs. M/s. American Express Bank Ltd., ITA No. 3487/Mum/2004, dated 17.06.2026*, has taken note of the fact that the Hon'ble Bombay High Court has agreed with the ratio propounded by the Special Bench and the question of law sought to be raised by the Revenue as to "whether ITAT was justified in holding that interest received by the Indian PE of the foreign bank from its head office and other overseas branches is not chargeable to tax in computing the total income" was not entertained as not being a substantial question of law in view of the settled position that no person can make profit out of itself and the relevant findings of the Coordinate Bench reads as under:

"9. We have considered rival submissions, in light of the decisions relied upon and perused the materials on record. It is evident, at the stage of assessment proceeding, the assessee had claimed that the interest received from the head office and overseas branches is not taxable in India under the domestic law as it is a receipt from self to self, hence, covered under the principles of mutuality. The assessee has also preferred to be covered under the domestic law and not under the provisions of India-USA Double Taxation Avoidance Agreement ('DTAA' for short). In case of Sumitomo Mitsui Banking Corporation (supra), a five-member Special Bench of ITAT has decided identical issue in favour of the assessee by holding that the interest received from and paid to head office and foreign branches is not taxable either at the hands of PE or at the hands of the head office or foreign branches, applying the principles of mutuality under the domestic law. In case of Director of Income-tax (IT) vs. Credit Agricole Indosuez (supra), the Hon'ble Bombay High Court has agreed with the ratio

propounded by the ITAT(SB). In fact, in assessee's case in A.Y. 1998-99, the co-ordinate bench has decided an identical issue in similar lines. Thus, respectfully following the judicial precedents referred to above, we uphold the decision of ld. First appellate authority while dismissing the ground."

48. In light of the aforesaid discussion and in absence of any contrary authority brought to our notice or any change in law, we direct the Assessing Officer not to tax the interest income received by the assessee on funds placed with its head office/overseas branches and at the same time, do not allow any deduction in respect of interest paid by the assessee in respect of funds placed with its overseas head office/branches while computing its income under the domestic tax laws.

49. In the result, the sole ground of appeal in assessee's appeal for A.Y. 1999-2000, ground no. 1 to 3 in assessee's appeal for A.Y. 2000-01 and A.Y. 2001-02 are hereby allowed.

50. In assessee's appeal for A.Y.2001-02, the assessee has challenged the action of the ld. CIT(A) in sustaining the action of the Assessing Officer in taxing the interest paid to the head office/overseas branches amounting to Rs. 80,69,725/- as interest income in terms of Section 115A of the Act.

51. During the course of hearing, the ld. AR submitted that the ground is consequential to the ground no. 2 and 3, the amount being payment by the assessee to head office/overseas branches, being payment to self, is not taxable in the hands of the assessee. It was further submitted that the matter is covered by the decision of Coordinate Benches in assessee's own case for A.Y.2004-05, wherein the Coordinate Bench has held that the amount paid by the permanent establishment to head office/overseas branches is payment to self and thus, not taxable. Further, reliance was placed on the decision of Special Bench in case of *Sumitomo Mitsui Banking Corpn. vs. Deputy Director of Income-tax (IT),*

Range-2(1), Mumbai, [2012] 19 taxmann.com 364 (Mum.) (SB), wherein it was held that payment by the Indian branch office to head office/overseas branches is payment to self and therefore, not taxable in India in the hands of the head office/overseas branches.

52. The ld. DR has been heard, who has relied on the order passed by the lower authorities.

53. We have heard the rival contentions and perused the material available on record. In light of our earlier discussion while disposing off the assessee's grounds of appeal where we have held that the transactions between the Indian branch office and the head office/overseas branches are transactions with itself, the payment of interest by the branch office to the head office/overseas branches cannot be held to be income in hands of the Head office/overseas branches and hence, the question of invoking the provisions of section 115A doesn't arise for consideration. Further, the matter stands covered by the earlier decision of the Coordinate Bench in assessee's own case as well as the decision of the Special Bench in case of Sumitomo Mitsui Banking Corporation*(Supra).* In the result, the ground no. 04 so raised by the assessee in its appeal for A.Y 2001-02 is hereby allowed.

54. Now, coming to the cross objections filed by the Revenue for A.Y.1999-2000, 2000-01 and 2001-02, wherein the Revenue has taken a common ground stating that in the event, it is held that the interest received by the Indian branch from its head office is not taxable in the hands of the Indian branch office, then in such a situation, the provision of Section 14A will be applicable.

55. Heard both the parties and considered the material available on record. In this regard, we find that the matter is covered by the decision of Special Bench of the Tribunal in case of *JP Morgan Chase Bank v. JCIT, (ITA No. 9189/Mum/2004, dated 10.10.2025)*, In the said case, the

issue before the Special Bench was whether Section 14A would be applicable if a receipt falls within the ambit of "*doctrine* of mutuality". The Special Bench held that the "*doctrine* of mutuality" relates to a notion that a person cannot make profit from himself, an amount received from oneself is not regarded as income and is therefore not subjected to tax, only such income that comes within the definition of Section 2(24) is subject to tax and therefore, where the Division Bench takes the view that the interest received by the Indian branch office is covered by the "*doctrine* of mutuality", then by its very nature, such income will not fall within the scope of income as defined in Section 2(24) and Section 4 of the Act based on various judicial precedents that consistently recognize this position. Referring to the provisions of section 14A and the legislative intent behind the introduction, it was held by the Special Bench that the said provisions were introduced to deal with income which are exempt under specific provisions of the Act, but are otherwise includable in total income and the receipt under the principle of mutuality are of a different character, they are not exempt income, but are simply not income at all and therefore Section 14A has no application to such receipts and the matter on the issue raised before the Special Bench was answered in negative.

56. In light of our earlier discussion while disposing off the assessee's grounds of appeal where we have held that the transactions between the Indian branch office and the head office/overseas branches, doesn't give raise to any taxable event, being transactions with itself, following the decision of the Special Bench, the provisions of Section 14A cannot be applied to such transactions.

57. Before parting, a question that arises for consideration is where in relation to earning of aforesaid receipts from head office/overseas branches where the said receipts are held not taxable as the transaction does not give rise to any taxable event, whether the expenditure

incurred by the assessee in relation to such receipts can be claimed and allowed for tax purposes. In other words, where receipts are in respect of non-taxable events and are excluded and not brought to tax, on principle of parity, the expenditure incurred for generating such receipt should also be excluded and cannot be claimed for tax purposes. We find that the matter under consideration before the Special Bench was limited to the application of provisions of Section 14A of the Act, where the interest received by the Indian branch from its head office is held not taxable on the principle of mutuality. Since the said issue has not been agitated or any arguments been advanced by either of the parties and the cross objection so filed by the Revenue were limited to applicability of Section 14A of the Act, we have not dealt with the said issue.

58. In light of the same, the cross objections so raised by the Revenue for the relevant assessment years are hereby dismissed.

59. In assessee's appeal for A.Y. 2000-01 and A.Y 2001-02, the assessee has challenged the action of the ld. CIT(A) in denying the exemption claimed by the assessee u/s 9(1)(v) of the Act in respect of interest income earned on overseas placements of funds with non-resident banks.

60. Briefly, the facts of the case in A.Y 2000-2001, being the lead case, are that the assessee in its return of income has claimed exemption on interest earned amounting to Rs. 1,99,461/- from funds placed outside India with banks other than its own branches. The Assessing Officer disallowed the claim for exemption on the basis that since the funds placed with the banks outside India are sourced mainly via the deposits received by the Indian branches, they are covered within the provisions of Section 9 read with Section 5 of the Act as it emanates from the Indian operations and such interest is payable in respect of debt

incurred or monies borrowed and used for the purpose of business carried on by such person in India and the provisions of section 9(1)(v) are attracted.

61. The assessee thereafter, carried the matter in appeal before the ld. CIT(A) and reference was drawn to the provisions of Section 9(1)(v) of the Act. It was submitted that Section 9(1)(v) talks about three types of interest income received by a non-resident which could be deemed to accrue or arise in India. It was submitted that in the instant case, the interest income is neither received from the Government or from the Indian resident and therefore, sub-clause (a) and (b) of Section 9(1)(v) are not applicable. As far as sub-clause (c) is concerned, two tests need to be satisfied. Firstly, the payer needs to be a non-resident and secondly, the interest is payable in respect of money used for the purposes of business or profession in India. It was submitted that in the instant case, all the lending transactions were entered into with non-residents and all the payers of interest are therefore non-resident. It was further submitted that the borrower banks used these funds for lending to third parties that are usually multinational entities and it is not possible to establish an exact correlation with any usage of funds by such third parties in Indian operations and the question of using the money for operations in India does not arise. It was accordingly submitted that though the payment is received by the assessee from non-resident, the second test relating to usage of money for the purposes of business or profession in India is not satisfied and therefore, the interest income received by the assessee is not covered within the ambit of Section 9(1)(v)(c) of the Act.

62. The submissions so filed by the assessee were considered but not found acceptable to the ld. CIT(A).The ld CIT(A), referring to his findings in context of transactions between the assessee and its head office/overseas branches, held that the funds have been transferred

overseas to these non-resident banks after seeking permission of the RBI and therefore, it is a case where the funds were lent in India and repayment of loan and interest would also have to be made in India and in such a situation, even though the actual user of the money was abroad, such interest income had accrued or arisen in India and have to be included in taxable total income of the assessee's bank in India. Against the said findings, the assessee is in appeal before us.

63. During the course of hearing, the ld. AR reiterated the submissions made before the lower authorities. It was submitted that the assessee has earned interest from overseas branches of BayerischeLandes Bank (Rs 45,553) and from overseas branches of Midland Bank (Rs 1,53,908). It was submitted that it is an undisputed fact that the interest was paid on money lying abroad which was lent to these non-resident banks and therefore, the act of lending and source of interest income happens outside of India. Further, our reference was drawn to the provisions of Section 9(1)(v)(c) of the Act, wherein income by way of interest payable by a person who is a non-resident will be taxable in India, where the interest is payable in respect of any debt incurred or money borrowed and used for the purposes of business or profession carried on by such person in India. It was submitted that in the instant case, it is not in dispute that the interest is payable by the non-resident banks to the assessee. Further, the funds have been lent overseas to non-resident banks who use these funds for lending to third parties who are usually multinational entitiesand therefore, it is clear that the money has been lent and used by such non-resident banks for the purposes of business or profession outside of India and therefore, the question of utilizing the funds for operations in India does not arise for consideration and in support, reliance was placed on the decision of Coordinate Calcutta Benches in case of *Assam Frontier Tea Co. Ltd. vs. ITO [1994] 49 ITD 412 (Cal).*

64. The ld. DR has been heard, who has relied on the order passed by the lower authorities.

65. We have heard the rival contentions and perused the material available on record. Firstly, for the interest income to accrue or arise in India, it is essential to determine the source of the interest income. The interest income will originate from the act of lending by the assessee bank and therefore, the place where the assessee has actually lent the funds will help determine the place of accrual of the interest income. As per ld CIT(A), the funds have been transferred overseas only after seeking permission of the RBI and therefore, it is a case where the funds were lent in India. However, as per the assessee, the assessee money was already lying abroad which was then lent to the overseas branches of the non-resident banks and therefore, the act of lending and source of interest income happens outside of India. We therefore find contrary factual assertions by both sides and in absence of requisite material available on record to support the stand taken by either sides, we are unable to decide the matter in so far as accrual of interest income u/s 5 of the Act is concerned and deem it appropriate to set-aside the matter to the file of the AO to thrash out the relevant facts and decide the matter a fresh as per law.

66. Now coming to the deemed accrual of interest income u/s 9(1)(v) of the Act, our reference was drawn to the decision of the Coordinate Calcutta Benches in the case of Assam Frontier Tea Co. Ltd. (supra). In the said case, the assessee, a non-resident company, derived income from the manufacture and sale of tea in India. The Assessing Officer observed that the assessee had not included the interest income earned on deposit placed with a bank in the U.K. and the same was brought to tax invoking provisions of Section 9(1)(*v*) for the reason that interest was earned on funds which flowed from India to the assessee's headquarters in England. The ld. Commissioner (Appeals) took the view that the

deposit should have come out of the unremitted sale proceeds of tea in England or out of a fund set apart from such unremitted funds, and so, in either case, the deposits were relatable to the assessee's business connection in India, attracting the provisions of Section 9(1)(*i*) and not Section 9(1)(*v*). Thereafter, the matter was carried in appeal before the Coordinate Bench. The Coordinate Bench held that the ld. CIT(A) was not correct in holding that the provisions of Section 9(1)(*i*) are applicable and not Section 9(1)(*v*). It was held that even the Legislature has recognized the fact that interest income for the purposes of the deeming provision of Section 9 would be dealt with as a separate category of income and accordingly, the provisions of Section 9(1)(*v*)were enacted with effect from 01.06.1976 effective from the assessment year 1977-78. It was held that it is no longer possible to treat the interest income as falling within the provisions of section 9(1)(i) on the ground that it arises out of a business connection in India. It was held that when a specific provision has been made in respect of a particular category of income, that provision has to be applied in preference to the general provisions. It was held that it is not possible to postulate that notwithstanding a specified treatment meted out to the interest income, the general provisions of section 9(1)(i) would continue to apply even after 01.06.1976 as a same will lead to the anomalous situation where two statutory provisions would simultaneously govern the same type of income, a result which is inconceivable and therefore, it was held that the interest income should be dealt with in accordance with section 9(1)(v) of the Act.

67. Further, referring to the provisions of Section 9(1)(*v*) in particular sub clause (c) thereof, the Coordinate Bench held that the same provides that any interest payable by a non-resident to another non-resident would be taxable in the hands of the recipient non-resident, if the interest is payable in respect of any debt incurred or money borrowed and used for the purpose of the business of the non-resident,

who pays the interest. It was further held that the reference in the provision to "such person" is only to the non-resident who is liable to pay the interest and cannot refer to the person who is in receipt of the interest and the interpretation so suggested on behalf of the Revenue was dismissed holding that the same is against the plain literal construction of the sub-clause, which is also against the "source rule" enacted by the Legislature. It was also held that the under the source rule, the income shall be deemed to arise or accrue in India, if the source from which it is derived has any business operations in India. It is not at all necessary that the non-resident who is in receipt of the interest income should have any business operations in India. It is the source which provides the income that is relevant and not the ultimate destination of the income. Accordingly, in that case, it was held by the Coordinate Bench that it is the U.K. Bank which paid the interest to the assessee and it is nobody's case that the bank has paid the interest in respect of any debt incurred or money borrowed and used by it for the purpose of its banking operations in India and it was accordingly held that such interest income will not be liable to tax in India.We fully subscribe to the view so taken by the Coordinate Bench.

68. In the instant case, the assessee bank, which qualifies as non-resident, has lent funds to overseas branches of two non-resident banks and both happen to be carrying on their respective banking operations. There is no dispute regarding the non-resident status of the borrower entities and factum of interest payable in respect of debt incurred or money borrowed by such borrower entities. The limited dispute as we could see from the findings of the Assessing officer is restricted to interpretation of the satisfaction of condition as to whether interest is payable in respect of debt incurred or money borrowed and used for the purposes of business carried on by such person in India and how the term “such person” should be interpreted. As we have noted supra, as so held by the Coordinate Bench, the term “such person” has to be read

and understood to mean the non- resident who is liable to pay the interest and not to the assessee who is in receipt of such interest income as so wrongly construed and understood by the Assessing officer. Further, it has been submitted by the assessee that the money has been lent and used by such non-resident banks for the purposes of its business operations outside of India. In any case, it is not the case of the Revenue that money so borrowed has been used by such non-residents bank for their banking operations in India. In light of the same, we find that the interest income on funds lend to the overseas branches of the non-resident banks cannot be held to be deemed to accrue or arise in India in terms of section 9(1)(v) of the Act and the contention so raised by the ld AR in this regard are accepted.

69. In the result, ground no. 04 of the assessee's appeal for A.Y 2000-2001 and ground no. 05 for A.Y 2001-02 are partly allowed for statistical purposes.

70. In its appeal for A.Y 2000-2001, the assessee has challenged the action of ld. CIT(A) in sustaining the action of the Assessing Officer, whereby he has disallowed the interest of Rs. 1,03,00,131/- paid to the Reserve Bank of India for default in maintaining Statutory Liquidity Ratio.

71. Briefly, the facts of the case are that during the year under consideration, the assessee paid an amount of Rs. 1,03,00,131/- to Reserve Bank of India towards interest for default in maintaining the SLR and which was claimed as an allowable deduction while filing its return of income. The AO however held that the interest paid by the assessee to RBI for shortfall in maintenance of SLR was penal in nature being paid for infraction of law and therefore, not an allowable expenditure.

72. Against the aforesaid finding, the assessee carried the matter in appeal before the ld. CIT(A) and it was submitted that Section 37 of the Act provides 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 was submitted that it is a well settled principle of law that interest paid, which is in the nature of compensatory interest and not infraction of law, is an allowable deduction under section 37 of the Act in computing the chargeable profits of the business carried on by an assessee. It wasfurther submitted that Section 24(2A) of the Banking Regulation Act, 1949 ('BR Act') requires every banking company to maintain in India in cash, gold or unencumbered securities an amount which shall not at the close of business on any day be less than 25 percent or such other percentage not exceeding 40 percent as the RBI may by notification in the official gazette specify, of the total of its net demand and time liabilities in India as on the last Friday of the second preceding fortnight. It was submitted that Section 24(4) of the BR Act provides for payment of penal interest by a banking company on account of default in maintenance of SLR. It was submitted that the assessee, being a bank, as required by the Banking Regulation Act, is required to maintain a prescribed amount of SLR balance in the form of cash, gold or unencumbered approved securities. Where the above requirement is not met with, the bank is required to pay interest at prescribed rates. The levy of interest under section 24 of the BR Act is purely compensatory in nature and is therefore fully deductible under the Act. Further, reliance was placed on the decisions in case of *Dhanalakshmi Bank Ltd (76 TTJ 439) (ITAT, Cochin); Corporation Bank (ITA No 448 & 449/Bang/1985, dated September 18, 1986) (ITAT, Bangalore) and Syndicate Bank (ITA No 750/Bang/1985, dated March 15, 1988).*

73. The submissions so filed by the assessee were considered but not found acceptable to the ld CIT(A). The ld. CIT(A) in his finding stated that it is true that section 37 of the Act provides 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 business shall be allowed in computing the income chargeable under the head 'Profits and Gains of Business of Profession'. The ld CIT(A) referred to the decision in the case of *Prakash Cotton Mills vs. CIT (201 ITR 684)*, wherein the Hon'ble Supreme Court has ruled that whenever any statutory impost is paid by an assessee by way of damages or penalty or interest, the assessing authority is required to examine the scheme of the provisions of the relevant statute providing for payment of such impost, notwithstanding the nomenclature of the impost as given by the statute, to determine whether it is compensatory or penal in nature. Further, ld. CIT(A) relied on the decision of Hon'ble Kerala High Court in the case of *Pachi Philip & Co. (212 ITR 75)*, where the Hon'ble Kerala High Court held that the important test to determine whether the levy is compensatory or penal in nature is whether for the non-compliance of the provisions, any criminal liability or prosecution is provided. If any criminal liability or prosecution is provided under the law, it is surely penal in nature.

74. It was held by the ld CIT(A) that in the instant case, the relevant provisions under the RBI Act as well as the Banking Regulation Act provide for charging of penal interest on the amount of shortage in maintenance of SLR for its first default. However, for a continuous succeeding default, these enactments not only provide for a higher rate of penal interest but also provide that every director, manager, or secretary of the Banking Company who is knowingly and willfully a party to the default shall be punishable with fine. Thus, it becomes

evident that if the payment of interest is made in respect of first default in complying with the SLR requirement, it cannot be treated as a penal provision, however, if the payment relates to second default or subsequent default, such payment has to be treated as penalty for infraction of law, because the RBI Act and the Banking Regulation Act provide for sanction in the form of punishing the director, manager or secretary of the bank with fine and also for prosecution of said officers besides prohibition in receiving any fresh deposits. Therefore, in the backdrop of these provisions, the appellant was asked to furnish details of various defaults for which the amount as large as Rs. 1,03,00,131/- had to be paid by the appellant to Reserve Bank of India for default in maintaining SLR and to show that such payment was only in respect of first default and not any subsequent default/s. However, despite giving repeated opportunities to the appellant to comply with the aforesaid requirement, no details were furnished in appellate proceedings. The ld. CIT(A) held that the ld. AR expressed his inability to produce any further detail in the matter and admitted that there was major default by the appellant bank and therefore, in these circumstances, it can be presumed that the impugned payment of interest by the assessee is for continuing defaults in maintenance of SLR and such payment of interest to RBI will have to be treated as penal in nature and not allowable as a deduction under section 37 of theAct, in view of the legal position and the ld. CIT(A) accordingly dismissed the ground of appeal raised by the assessee. Against the said findings, the assessee is in appeal before us.

75. During the course of hearing, the ld. AR submitted that the assessee has paid a sum of Rs. 1,03,00,131/- to RBI by way of interest for shortfall in maintenance of statutory liquidity ratio (SLR) and the same, being compensatory in nature, was claimed as deduction while filing its return of income. Referring to the provisions of Section 24(4) of the Banking Regulation Act, 1949, it was submitted that there was no

distinction of character between interest paid u/s. 24(4)(a) or 24(4)(b) of the Banking Regulation Act, 1949. It was submitted that the only difference between the two clauses was the rate, while under clause (a), the rate was 3% with respect to the first default and under clause (b), the rate was increased to 5% which is further born out from the fact that the percentage charged under clause (b) is referred to as "increased" to 5% from 3% as per clause (a). It was submitted that such an increase in percentage of rate of interest cannot tantamount to change in character from compensatory to penal. It was further submitted that where the assessee continues with the default after the levy of 5% u/s. 24(4)(b), the Banking Regulations Act u/s. 24(7) provides for a levy of "fine" as a punishment for every director or manager or secretary of the baking company (and not on the assessee). It was submitted that it is this amount in the scheme of Section 24, that was penal in nature, being different in character from the interest recovered u/s. 24(4), as Section 24 itself draws a distinction between the character of the interest payable u/s. 24(4) and amount payable u/s. 24(7). It was accordingly submitted that the artificial distinction of character so drawn by the ld. CIT(A), therefore, deserves to be set aside.

76. Further, reliance was placed on the Coordinate Benches decisions in case of *Dhanalakshmi Bank Ltd (76 TT) 439) (ITAT, Cochin), Bank of America [2014] 41 taxmann.com 9 (Mumbai Trib.)* and the Hon'ble Jurisdictional High Court in case of *CIT vs. Bank of Baroda (in ITA No. 4169 of 2009, dated 15.02.2011).* It was submitted that the Jurisdictional Bombay High Court in case of *Bank of Baroda (supra)*have approved the decision passed by the Cochin Bench of the Tribunal in case of *Dhanalakshmi Bank Ltd (supra),* wherein it was held that the interest paid u/s. 24(a) and 24(b), both are compensatory in nature and allowable as deduction. It was fairly submitted that although the view of the ld. CIT(A) is supported by the decision of Kerala High Court in case of *Catholic Syrian Bank Ltd. (2003) 130 taxmann.com*

*447 (Ker.), h*owever, in view of the decision of the Jurisdictional High Court in case of *Bank of Baroda (supra),* the decision of the Jurisdictional High Court will have a binding force on the matter under consideration.

77. The ld DR has been heard who has relied on the findings of the AO and the ld CIT(A).

78. We have heard the rival contentions and perused the material available on record. There is no dispute in the legal proposition so canvassed by the ld. CIT(A) that whenever any statutory impost is paid by the assessee by way of damages or penalty or interest and which is claimed as an allowable expenditure u/s. 37(1) of the Act, the Assessing Officer is required to examine the scheme of the provisions of the relevant statute providing for payment of such impost notwithstanding the nomenclature of the impost as given by the statute to find out whether it is compensatory or penal in nature. The Assessing Officer has to allow deduction u/s. 37(1), wherever such examination reveals the concerned impost to be purely compensatory in nature. However, where such impost is found to be a composite in nature, the Assessing Officer is obliged to bifurcate and give deduction for the component which is compensatory in nature. It has been further held by the Courts, as rightly highlighted by the ld CIT(A),that one of the important tests to determine whether the levy is compensatory or penal in nature is whether for non-compliance of the provisions, any criminal liability or prosecution is provided and where such a criminal liability or prosecution is provided, the levy is clearly penal in nature. We find that these are settled legal propositions and no dispute as such has been raised by either of the parties during the course of hearing in terms of following the same in the instant case.

79. The relevant provisions under which the penalty has been levied are contained in Section 24 of the Banking Regulation Act, 1949 and we refer to the relevant provisions to understand the nature of levy so paid by the assessee. Sub-section (2A) of Section 24 provides that a scheduled bank, (in addition to average daily balance which is required to be maintained u/s. 42 of the Reserve Bank of India Act, 1934) and every other banking company, (in addition to the cash reserve which is required to be maintained u/s. 18), shall maintain in India, in cash, gold, or in unencumbered approved securities, the value of which shall not be less than 25% or such other percentage not exceeding 40% of the total of its demand and time liabilities in India, as on the last Friday of the second preceding fortnight as the Reserve Bank specify from time to time. It has been further provided that for the purposes of ensuring compliance, every banking company shall furnish to the RBI, a monthly return in such form and manner as may be specified. In Clause (a) of sub-section (4) to Section 24, it has been provided that where on any alternate Friday, the amount maintained by a banking company at the close of the business on that day falls below the minimum prescribed threshold, such banking company shall be liable to pay to the Reserve Bank in respect of that day's default, penal interest for that day at the rate of 3% per annum above the bank rate on the amount by which the amount actually maintained falls short of the prescribed minimum on that day. In sub-clause (b) to sub-section (4) to Section 24, it has been further provided that where the default occurs again on the next succeeding alternate Friday, and continues on succeeding alternate Fridays, the rate of penal interest shall be increased to a rate of 5% per annum, above the bank rate on each such shortfall in respect of that alternate Friday and each succeeding alternate Friday in which the default continues. Sub-section (6) to Section 24 provides that the penalty payable under sub-section (4) shall be paid within a period of 14 days from the day on which a notice issued by the RBI demanding payment is served on the banking company, and in the event of failure

of the banking company to pay the same within such period, the penalty may be levied by a direction of the Principal Civil Court having jurisdiction in the area, where an office of the defaulting banking company is situated and such a direction is to be made upon an application made by the Reserve Bank of India to the Civil Court. It has been provided that where the Civil Court makes the direction, it shall issue a certificate specifying the sum payable by the banking company and every such certificate shall be enforceable in the same manner, as if it were a decree made by the Court in a suit. In sub-section (7) to Section 24, it has been further provided that where under clause (b) of sub-section (4), penal interest at the increased rate of 5%, above the bank rate has become payable by a banking company and thereafter, the amount required to be maintained on the next succeeding alternate Friday is still below the prescribed minimum, every director, manager or secretary of the banking company who is knowingly and willfully a party to the default shall be punishable with fine which may extend to 500 rupees and with a further fine which may extend to 500 rupees for each subsequent alternate Friday on which the default continues. Sub-section (8) further provides that where on application, the RBI is satisfied that the banking company had sufficient cause for its failure to comply with the provisions, it shall not demand the payment of the penal interest.

80. We therefore find that the non-compliance of the provisions relating to maintenance of minimum asset threshold in terms of SLR is provided under the Banking Regulation Act by way of levy of interest at the rate of 3% in case of initial default and thereafter at the increased rate of 5% in case of subsequent default/defaults and in case of non-payment within prescribed threshold and to ensure compliance, the Reserve Bank of India can move an application before the Principal Civil Court seeking necessary direction for payment of the interest. We therefore, find that the liability is primarily of a civil nature by way of levy of

interest arising out of non-compliance and lack of adherence of the obligation under the Banking Regulation Act, 1949 and there is no mention of any criminal liability or prosecution in respect of non-compliance which can be initiated against the banking company. Even in terms of sub-section (7) to Section 24, it provides that where interest at the rate of 5% has become payable and thereafter, the amount required to be maintained is still below the prescribed minimum threshold, every director, manager or secretary shall be punishable with fine which may extend to 500 rupees and with a further fine of 500 rupees for each subsequent alternate Friday on which the default continues and therefore, even in respect of the liability of the directors, etc. of the banking company, we find that the liability continues to be a civil liability by way of levy of fine. There is no mention of any prosecution to be initiated and that too, any criminal prosecution against the directors, etc of the banking company. In light of the same, the payment of interest either at the rate of 3% or at the increased rate of 5% for non-compliance with the requirement to maintain the minimum prescribed SLR is compensatory in nature and cannot be termed as penal in nature.

81. In the instant case, the ld CIT(A) in absence of sufficient information on record and inability shown by the ld AR to furnish the requisite information and concession on part of the ld AR on behalf of the assessee that there was major default, the ld CIT(A) has arrived at the conclusion that it was a case of continued default in maintenance of SLR and held the payment of interest to be penal in nature. However, as we have held above, whether the payment of interest is at the rate of 3% for the initial default or at the increased rate of 5% for continued non-compliance with the requirement to maintain the minimum prescribed SLR, the interest payment continues to remain as compensatory in nature and cannot be termed as penal in nature

82. Further, we find that in case of *Dhanalakshmi Bank Ltd (supra),* the Coordinate Cochin Benches has recorded a similar finding and held thatthough *mens rea* is not relevant as far as the penalty for infraction of law is concerned, still if the assessee has, without any action from its side, crossed the border of permissible limit, such action cannot be treated as a criminal action liable to penalty, or, for that matter, infraction of law. It was held by the Coordinate Bench that in banking parlance, it is an additional interest, termed as 'penal interest' and given that the assessee failed to maintain the ratio of cash reserve and statutory liquidity described by the Banking Regulation Act, 1949, such default leads to payments towards the penal interest.It has been further held by the Coordinate Bench that the RBI, being the controlling body, it has to keep a check on the assessee and to guard the interest of the depositor, it prescribes certain limits with regard to cash reserve and statutory liquidity ratio and penal interest is automatic in nature and without any further action on the part of the assessee, the consequences follows and merely use of the word "penalty" in sub-section (6)(a) of Section 24 of the Banking Regulation Act, 1949 would not lead to the conclusion that interest paid by the assessee is not interest but penalty for infraction of law. It was held that for imposing any penalty, the assessee by action or inaction has to contribute something, that falling short of the percentage of assets by cash or reserve may be unintentional and by levy of penalty interest, the assessee is checked from falling into the trap and Section 24(4)(a) and 24(4)(b) of the Banking Regulation Act, 1949 uses the word "rate of penal interest" which is interest only and nothing else.

83. We further find that the decision in case of *Dhanalakshmi Bank Ltd (supra)* has been taken into consideration and concurred by the Hon'ble Bombay High Court in case of *CIT vs. Bank of Baroda (supra)* and appeal filed by the Revenue was dismissed and the relevant findings of the Hon'ble Bombay High Court read as under:

"The only question raised by the revenue in this appeal is, whether the interest paid by the assessee for non maintainance of the cash reserve ratio / statutory liquidity ratio as per Section 24 of the Banking Regulation Act, 1949 and Section 42 of the Reserve Bank of India Act, 1934 constitute penalty so as to disallow the interest claim. The Tribunal following the decision in the case of DCIT V/s. Dhanalakshmi Bank Ltd. (Cochin) reported in 76 TTJ 439 held that the interest paid to the RBI was not penalty and accordingly the interest expenditure is allowable. SLP filed by the revenue against similar decision of the Tribunal in the case of Dhanalakshmi Bank Ltd. (supra) has been dismissed by the Apex Court as reported in [2005] 277 I.T.R. (ST) 3. In this view of the matter, we find no merit in the appeal and the same is dismissed with no order as to costs."

84. Following the decision of Hon'ble Bombay High Court in case of *Bank of Baroda (supra)*, the Coordinate Mumbai Benches in case of *Bank of America (supra)* has again decided the matter in favour of the assessee holding that the amount paid by the assessee for shortfall in maintenance of CRR and SLR cannot be held as payment for infraction of any law.

85. In light of aforesaid discussions and in the entirety of facts and circumstances of the case and respectfully following the decision of the Hon'ble Bombay High Court in case of *Bank of Baroda (supra)*, we set-aside the findings of ld. CIT(A) and the Assessing Officer is hereby directed to allow the interest of Rs. 1,03,00,131/- paid by the assessee to the Reserve Bank of India for default in maintaining Statutory Liquidity Ratio as being compensatory in nature.

86. In the result, ground no. 05 of the assessee's appeal for A.Y 2000-2001 is allowed.

87. In assessee's appeal for A.Y. 2001-02, the assessee has challenged the action of ld. CIT(A) in not admitting an additional ground of appeal raised by the assessee during the course of appellate proceedings whereby the assessee has claimed deduction for expatriate salary expenses amounting to Rs. 1,45,96,718/- borne by its head office in

respect of services rendered by the expatriates in connection with operations of the Indian branch office.

88. During the course of hearing, the ld. AR submitted that this ground was raised before the ld. CIT(A), however, the same has not been adjudicated by the ld. CIT(A) and therefore, the matter may be remanded back to the file of ld. CIT(A) to decide the same.

89. The ld. DR has been heard, who has relied on the order passed by the ld. CIT(A).

90. We have heard the rival contentions and perused the material available on record. It is a matter of fact that the assessee raised the aforesaid additional ground before the ld. CIT(A) in the course of appellate proceedings. However, the same was not admitted and consequently, there is no adjudication thereof by the ld. CIT(A). The ld. CIT(A) in its findings at para 3.3 of its order stated that during the course of appellate proceedings, the ld. AR was asked as to whether this claim was raised before the Assessing Officer and in response, it was submitted that the expatriate salary expense amounting to Rs. 1,45,96,718/- borne by the head office was neither considered in computing the total income at a time of filing the return of income nor was it claimed as a deduction as business expenditure under section 37(1) during the course of assessment proceedings and the Assessing Officer therefore, never examined this issue. The ld. CIT(A) accordingly held that when the ground of appeal is not arising out of the assessment order, which is the subject matter of appeal, the same cannot be raised for adjudication before him and in support, reliance was placed on the decision of Hon'ble Supreme Court in case of *Addl. Commissioner of Income-tax vs. Gurjargravures (P.) Ltd. [1978] 111 ITR 1 (SC)[08-11-1977],*wherein the Hon'ble Supreme Court held that a claim for deduction not made before the Assessing Officer cannot be

entertained by the ld. CIT(A), where the relevant material to sustain the claim is not on record. Accordingly, the additional ground so raised by the assessee was not admitted. Therefore, as against the contention raised by the ld AR during the course of hearing that the ground was not adjudicated by the ld. CIT(A), on examination of the findings of the ld. CIT(A), we find that the ground was not admitted at first place and therefore, it was not adjudicated by the ld. CIT(A).

91. Further, we find merit in the findings of the ld. CIT(A), wherein he said that where the relevant material to sustain the claim is not on record, the additional ground and the claims so raised by the assessee cannot be admitted during the appellate proceedings. It is therefore not a case where the assessee seeks to raise a legal claim where the relevant material to dispose off the same is already available on record and doesn't require any fact findings and therefore, on the admitted set of facts, a legal claim was sought to be raised for the first time. It is a case where the relevant facts have to be brought on record in terms of incurrence of expenditure on the expatriate employees by the Head office at the first place and secondly, examination of whether the expatriates have rendered services in India in connection of assessee's operations and thereafter, once the said facts are thrashed out and brought on record, the matter relating to allowability thereof u/s 37 of the Act. Therefore, it is a case of mixed question of facts and law and where the ld CIT(A) has denied admitting the said claim following the legal proposition so laid down by the Hon'ble Supreme Court referred supra, we see no justifiable reason to interfere with the findings of the ld CIT(A) and the findings are hereby confirmed. In light of the same, the ground no. 6 so raised by the assessee is hereby dismissed.

92. In the result, the assessee's appeal in ITA No. 3159/Mum/2004 for A.Y 1999-2000 is allowed and appeal in ITA No. 7158/Mum/2004 for A.Y 2000-01 and appeal in ITA No. 2285/Mum/2005for A.Y 2001-02

are partly allowed for statistical purposes. The Revenue's appeal in ITA No. 3488/Mum/2004 for A.Y 1999-2000, appeal in ITA No. 7217/Mum/2004 for A.Y 2000-01, and appeal in ITA No. 2286/Mum/2004 for A.Y 2001-02 are dismissed. The Revenue's cross-objections in ITA No. 174/Mum/2013for A.Y 1999-2000, ITA No. 175/Mum/2013for A.Y 2000-01 and ITA No.176/Mum/2013 for A.Y 2001-02 are dismissed.

Order pronounced in the open court on 25-06-2026.

Sd/-	Sd/-
(JUSTICE (RETD.) C.V. BHADANG)	(VIKRAM SINGH YADAV)
PRESIDENT	ACCOUNTANT MEMBER

Mumbai,
Dated: 25-06-2026
Karishma J. Pawar, SR. PS

Copy to :

1) The Appellant
2) The Respondent
3) The CIT concerned
4) The D.R, ITAT, Mumbai
5) Guard file

By Order

Dy./Asst. Registrar
I.T.A.T, Mumbai