

आयकर अपीलिय अधिकरण, मुंबई पीठ, मुंबई
INCOME TAX APPELLATE TRIBUNAL
MUMBAI BENCHES, MUMBAI

BENCH: I
BEFORE HON'BLE BEENA PILLAI, JUDICIAL MEMBER
AND HON'BLE ARUN KHODPIA, ACCOUNTANT MEMBER

ITA 4247 & 4275/MUM/2025		
निर्धारण वर्ष/Assmt. Year: 2004-05 & 2005-06)		
DCIT(IT)-4(2)(2) ROOM NO.627, KAUTILYA BHAWAN, BKC, BANDRA (E), MUMBAI-400051, MAHARASHTRA	Vs.	STANDARD CHARTERED BANK C 38 AND 39 G BLOCK CRESCENZO BLDG BANDRA KURLA COMPLEX, BANDRA(EAST) MUMBAI-400051, MAHARASHTRA
(अपीलार्थी Appellant)		(प्रत्यर्थी Respondent)
Permanent Account Number of Assessee:		AABCS4681D

ITA 4264 & 4265/MUM/2025		
निर्धारण वर्ष/Assmt. Year: 2004-05 & 2005-06)		
STANDARD CHARTERED BANK C 38 AND 39 G BLOCK CRESCENZO BLDG BANDRA KURLA COMPLEX, BANDRA(EAST) MUMBAI-400051, MAHARASHTRA	Vs.	DCIT(IT)-4(2)(2) ROOM NO.627, KAUTILYA BHAWAN, BKC, BANDRA (E), MUMBAI-400051, MAHARASHTRA
(अपीलार्थी Appellant)		(प्रत्यर्थी Respondent)
Permanent Account Number of Assessee:		AABCS4681D

निर्धारिती द्वारा/Assessee represented by:	Shri Porus Kaka, Ld. Senior Counsel & Manish Kanth, Counsel, instructed by Shri
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	Vijay Budhwani [authorised signatory of Standard Chartered Bank]
राजस्व द्वारा/Revenue represented by:	Shri Ajay Chandra (CIT-DR)

सुनवाई की तारीख / Date of conclusion of hearing:	28-Apr-2026
घोषणा की तारीख / Date of pronouncement:	16/07/2026

आदेश / ORDER

PER BEENA PILLAI, JUDICIAL MEMBER:

The present cross-appeals filed by the Revenue and the assessee for A.Y. 2004-05 & 2005-06 arise out of the separate orders dated 11/04/2025 passed by the Learned Commissioner of Income Tax (Appeals)-58, Mumbai (hereinafter referred to as "Ld.CIT(A)").

We first take up the cross-appeals for A.Y. 2004-05 for adjudication.

2. Brief facts of the case are as under:-

Assessee is a bank incorporated by Royal Charter under the laws of England and Wales. Assessee is a foreign body corporate registered in India under the provisions of the Companies Act, 1956. It carries on the business of banking, financial services and allied activities in India in accordance with the provisions of the Banking Regulation Act, 1949. For the year under consideration, the assessee filed its return of income on 29/10/2004.



Subsequently, the return was revised on 29/03/2006. The particulars of the revised return of income are as under:–

Particulars	Rs.
<i>Income from House Property</i>	80,558
<i>Profits & Gains of Business or Profession</i>	6,838,178,328
<i>Capital Gain</i>	28,654,514
Gross Total Income	6,866,913,400
<i>Less: Deduction u/s.80-G</i>	120,500
TOTAL INCOME	6,866,792,900

2.1. The assessee received notice issued under section 143(2) of the Act along with a questionnaire under section 142(1), calling for the requisite details and information in respect of the transactions reported in Form No. 3CEB. The issue relating to the reference made under section 92CA of the Act was also examined during the course of the proceedings. The Ld.TPO, after considering the details and explanations furnished by the assessee, accepted the value of the international transactions as reported in Form No. 3CEB, except with regard to the allocation of indirect costs.

2.2. The Ld.TPO observed that one of the international transactions pertained to costs directly attributable to the India Branch, which had been claimed as a deduction by the assessee in its computation of income. On being called upon to furnish the details, the assessee submitted that such costs were incurred by its Head Office, Singapore Branch and Hong Kong Branch exclusively for the benefit of the India Branch.

2.2.1. The assessee explained that the aggregate amount allocated and claimed towards such costs was Rs.85,18,87,800/-. It was submitted that the allocation of the aforesaid costs was based on



actual usage and was determined on an arm's length basis. In support of its claim, the assessee furnished the relevant details, allocation workings and supporting documents.

2.2.3. The assessee was thereafter called upon to explain the nature of benefits derived from such cost allocation and to demonstrate whether the benefits received were commensurate with the costs allocated. In response thereto, vide letter dated 28/08/2006, the assessee furnished, inter alia, the following documents/details:

- (a) Copy of the agreement entered into by the Branch in respect of the cost-sharing arrangement;*
- (b) Copies of invoices raised by the overseas entities towards allocation of such costs to the Indian Branch;*
- (c) Contemporaneous evidence demonstrating the services rendered and benefits received by the assessee during the relevant previous year under various heads for which charges were made; and*
- (d) Confirmation that the overseas entities rendering such services had not claimed any deduction in respect of such expenses in the event no corresponding charge was made to the assessee in its books of account.*

2.3.1. The Ld. TPO also raised specific queries in respect of the cost allocation transactions and the costs directly attributable thereto. In response, the assessee, vide letters dated 07/09/2006 and 18/09/2006, furnished its explanation. The assessee submitted that there were no formal agreements entered into with the co-branches for sharing of such costs. It was explained that no separate invoices were raised by the co-branches rendering the



services to the Indian Branch and that the expenses incurred were duly certified by the annual auditors by way of a specific certificate issued in this regard.

2.3.2. The assessee further submitted that certain contemporaneous documents evidencing the services rendered and benefits received had been furnished. It was also explained that, as a matter of historical practice, such allocated costs were not separately debited in the Branch accounts.

2.3.3. The assessee furnished certificates from the Hong Kong and Singapore co-branches confirming that the said expenses had not been claimed as a deduction by them in their respective income-tax assessments. In respect of services rendered by the London office, it was explained that since the assessee Bank was incorporated and tax resident in the UK, the deduction in respect of such expenses would ultimately be claimed by Standard Chartered Bank in the computation of its income under the India column, comprising the entire income and expenditure attributable to the India Branch.

2.3.4. The assessee also contended that the expenditure allocated by the Head Office/offshore co-branches would not fall within the scope of section 92 of the Act, in view of Article 10 of the Double Taxation Avoidance Agreement between India and UK.

2.3.5. The assessee explained that the costs under consideration were primarily in the nature of technology-related costs. It was submitted that, being an old banking institution operating in India, several of its systems and processes had become outdated over a period of time. Further, considering the evolving nature of the



financial services industry and the growth opportunities in the Indian market, there was a requirement to upgrade its systems and delivery processes.

2.3.6. It was submitted that a substantial part of the direct costs allocated to the India Branch represented technology expenditure incurred for upgrading the existing systems and migrating them to a common platform, with the objective of improving operational efficiency and enhancing competitiveness.

2.3.7. The assessee further contended that the upgraded technology and systems enabled improvement in business operations and overall efficiency. It was submitted that against the cost allocation of Rs.85.19 crores claimed by the assessee, the gross revenue earned by the India Branch during the relevant financial year was Rs.3,223 crores. Accordingly, the assessee contended that the allocated cost constituted only about 2.63% of the gross revenue and was reasonable and commensurate with the benefits derived.

2.4. The Ld.TPO thereafter called upon the assessee to furnish specific evidence in respect of the aforesaid cost items to substantiate that the expenditure pertained to the activities of the India Branch and that the assessee had derived commensurate benefits from such allocation. In response thereto, vide letter dated 18/09/2006, the assessee furnished details in respect of approximately 61% of the total costs, with a view to demonstrate the nature of services received and the benefits derived by the India Branch. The said details were examined and considered by the Ld. TPO in paragraphs 9 to 14 of the order.



2.5. Thereafter, the Ld. TPO accepted the cost allocation to the extent of Rs.51.95 crores out of the total allocation of Rs.85.19 crores claimed by the assessee. However, in respect of the balance amount of Rs.33.24 crores, the Ld. TPO determined the Arm's Length Price at Nil and proposed a transfer pricing adjustment of Rs.33.24 crores in the hands of the assessee.

2.6. Upon receipt of the order passed u/s 92CA of the Act, the Ld.AO issued the draft assessment order proposing, inter alia, the following additions/disallowances:-

1. Disallowance of salary paid to expatriates amounting to Rs.8,63,65,727/-.
2. Disallowance of interest expenditure incurred by the Head Office amounting to Rs.18,69,23,764/-.
3. Attribution of interest income received by the Head Office from the assessee as income in the hands of the assessee amounting to Rs.18,69,23,764/-.
4. Disallowance of expenditure attributable to exempt income amounting to Rs.31,16,33,936/-.
5. Disallowance of recoveries against securities loss amounting to Rs.4,62,27,884/-.
6. Disallowance of deduction claimed in respect of Head Office expenditure amounting to Rs.192,44,66,501/-.
7. Disallowance of interest on income-tax refund amounting to Rs.49,17,15,498/-.

2.6.1. Upon receipt of the draft assessment order, the assessee communicated its intention to prefer an appeal before the Ld.CIT(A). Thereafter, the final assessment order was passed on 30/11/2006, wherein the additions/disallowances, as discussed hereinabove, were made in the hands of the assessee.



Aggrieved by the order passed by Ld.AO, assessee preferred appeal before Ld.CIT(A).

3. The Ld.CIT(A), while disposing of the appeal, considered the submissions advanced by the assessee on the various issues involved. In respect of most of the issues, the Ld.CIT(A) either followed the orders passed by this *Tribunal* in the assessee's own case or relied on the decisions rendered by his predecessors in assessee's own case for preceding assessment years and allowed the claim of assessee.

3.1. Insofar as the issue relating to direct cost allocation is concerned, the submissions advanced by the assessee were duly considered. In support of its claim, the assessee placed reliance on the order passed by this *Tribunal* in *ITA No. 1683/Mum/2003* for *A.Y. 1994-95 dated 29/10/2007*.

3.2. Further, the issue relating to expenditure falling within the ambit of section 44C of the Act was examined with reference to the decisions of this *Tribunal* in the case of *British Bank of Middle East* in *ITA No. 2297/Mum/1999* and *ABN Amro Bank N V V/s JCIT* in *ITA No.692/Cal/2000(AY-1996-97) dated 30/03/2001*, as well as the decision of the *Hon'ble Bombay High Court* in the case of *American Bureau of Shipping v. ITO* reported in *(1986) 19 ITD 793 (Bom)*.

3.3. The Ld.CIT(A), thereafter observed and held as under:-

“5.4 Decision on Ground 1

5.4.1 *I have gone through the issue and the Appellant's submission. It is an undisputed fact that these expenses are incurred by the HO and offshore co-branches for the benefit of the India operations and therefore allocated to India.*



5.4.2 The Appellant had explained the transaction and submitted details under various heads for the total costs of INR 85.19 crs. However, the Appellant submitted evidences for 61 percent (i.e., INR 51.95 crs) of the total costs on a representative sample basis before the TPO for the above costs. The TPO post verification of these details accepted 61 percent of the total costs (i.e., INR 51.95 crs) to be at arm's length and determined the arm's length price for the balance costs (i.e., INR 33.24 crs) to be NIL. The only issue with regard to transfer pricing is the non-submission of the details for the entire (i.e., 100 percent) costs.

5.4.3 I have also perused the Hon'ble ITAT's Order for AY 2002-03 and AY 2003-04 in Appellant's own case. The Hon'ble ITAT, in its order dated 15 March 2024 for AY 2002-03 and AY 2003-04, while principally adjudicating the issue in favor of the Appellant by following the coordinate bench ruling in the case of Jabil Circuit India Private Limited Vs. Asst. CIT, Circle 3(2)(1) [TS-1274-ITAT-2018Mum-TP] against the adhoc transfer pricing adjustment, directed the AO to verify the Certified Public Accountant ('CPA') certificate, allocation keys, and relevant cost allocation to the Indian entity in relation to the Direct costs. Further, the Hon'ble ITAT had allowed the Appellant's ground under Section 37(1) of the Act and also deleted the disallowance under Section 40(a)(i) of the Act, by following the ruling of co-ordinate bench of the Hon'ble ITAT in Appellant's own case for AY 1999-00 and 2001-02 which relates to the same Direct costs. The relevant extract from the Hon'ble ITAT's order for AY 2002-03 and AY 2003-04 is reproduced below:

"56. It was held that the intra group services should have provided and such services must be at Arm's Length Price. As per OECD, allocation of cost based on approved allocation key and certified by the CPA certificate is relevant. The revenue cannot reject the CPA certificate since the same are specific and authenticated. As per Rule 10D(2)(A), the document must be supported by authentic documents, which includes authentication by the CPA. Therefore, the certification of allocation key and the same was authenticated by the CPA is proper documents as per Rule 10(2)(A) of the I.T. Rules. Respectfully following the above decision, we observe that in the given case also, the assessee has provided informations under Rule 10D(2)(A) and the cost allocation was also certified by the statutory auditors (CPA) of the Head Office and the service branches are submitted before tax authorities. However, this was not taken cognizance by the tax authorities. Therefore, we direct the Assessing Officer to verify the CPA certificate and verify the allocation key and relevant allocation of the cost to the Indian entity. Therefore, we rely on the above decision and findings of the Coordinate Bench in assessee's own case, we are inclined to allow the Ground No. 2 raised by the assessee with the above direction"

5.4.4 The Appellant thereafter filed a Miscellaneous Application ('MA') against the said remand with directions for verification. The Hon'ble ITAT vide its MA order dated 16 December 2024 rejected the Appellant's plea citing that the formation of a view that an issue should be remanded back to the file of the authorities below cannot constitute a mistake apparent on record in the facts and circumstances of the present case. However, the remand of the issue back to the file of the authorities below can, at best, constitute an error of judgment which may be subjected to judicial review in appellate proceedings under Section 260A of the Act. The relevant extract is reproduced below:

"In the facts of the present case, the remand of the issue back to the file of the authorities below can, at best, constitute error of judgment (and not mistake apparent on record as contended by the Assessee) which may be subjected to judicial review in appellate proceedings under Section 260A of the Act and the same does not fall within the ambit of powers vested in the Tribunal under Section 254(2) of the Act to rectify the mistake apparent on record."

5.4.5 In view of the above judgment, the Appellant had filed a written submission vide letter dated 24 March 2025 submitting that it has explained the entire transaction and submitted evidence on a representative sample basis for approx. 61 percent of the total



costs. Further, the Appellant submitted that it does not have any incremental documents to furnish in relation to the Direct Costs for the year under consideration. Given that the Appellant does not have any incremental document to submit, the issue is being decided based on the material available on record, the Hon'ble ITAT order for AY 2002-03 and AY 2003-04 in the Appellant's own case, and the coordinate bench ruling in case of *Jabil Circuit India Private Limited Vs. Asst. CIT, (Supra)*.

5.4.6 It is a well-settled position in law that the primary onus to substantiate the arm's length price of a transaction along with the prescribed / relevant documents is of the Assessee. In the present case, since no details have been submitted by the Appellant to substantiate the arm's length price for the balance costs, I affirm the findings of the TPO to determine the arm's length price for the balance costs of INR 33.24 crs to be NIL.

5.4.7 Further, as discussed above, I observe that the Hon'ble ITAT in past AYs in Appellant own case has allowed the deduction under Section 37(1) of the Act as the expenditure are incurred for the Appellant. The Hon'ble ITAT in AYs 2001-02, 2002-03, 2003-04 has held that the provision of Section 40(a)(i) of the Act is not applicable as the direct cost expenses represents transaction with self (as no one can make profit / income out of self) and also held that direct cost expenses are not in nature of royalty / FTS in the hands of HO and hence no disallowance can be made under Section 40(a)(i) of the Act. Further, in AY2000-01 the Hon'ble CIT(A) held that direct expenses are not in the nature of royalty, and no appeal was preferred by the Department before Hon'ble ITAT. Respectfully, following the Hon'ble ITAT orders in Appellant's own case, I direct the AO to allow the deduction of direct cost expense after necessary verification. **Accordingly, Ground no. 1 is allowed for statistical purpose."**

3.4. Accordingly, the Ld.CIT(A) confirmed the adjustment made by the Ld.AO/TPO in respect of the cost allocation transaction amounting to Rs.33.24 crores, observing that the assessee failed to substantiate the Arm's Length Price of the said international transaction.

Aggrieved by the order passed by the Ld.CIT(A), both the assessee as well as the Revenue are in appeal before this *Tribunal*.

4. The issue contested by the assessee before us relates to the partial disallowance of direct costs amounting to Rs.33.24 crores. And refurbishment expenses treated as capital in nature. On the other hand, the Revenue is aggrieved by the relief granted by the Ld. CIT(A) in respect of various additions/disallowances.

We shall first take up the appeal filed by the Revenue for adjudication.



5. Ground No. 1 raised by revenue has to be considered along with the appeal filed by assessee.

6. Ground No. 2: The Revenue is aggrieved by the relief granted by the Ld. CIT(A) in respect of deduction allowed towards salaries paid to expatriate employees amounting to Rs.8,63,65,727/-.

6.1. Brief facts, as submitted by the Ld.Sr.Counsel, are that during the year under consideration, the assessee claimed deduction of Rs.8,63,65,727/- towards salaries paid to expatriate employees working in India and deputed to the India Branch/SCB India. It was submitted that, the said expatriate employees were seconded by the Head Office to the assessee and were exclusively engaged in carrying out the activities of the India Branch.

6.2. It was further submitted that such expatriate employees were generally deputed to India for a period of two to three years, during which they worked exclusively for the India Branch of the assessee. The Ld.Sr.Counsel submitted that most of these expatriate employees were heading various functional divisions in India and were responsible for managing and supervising the business operations of the assessee in India.

6.2.1. The Ld.Sr.Counsel submitted that the expatriate employees received a part of their salary and allowances, including bonus, in their home country and that such overseas payments were made with the approval of the RBI. It was contended that both components of the salary, i.e., the portion paid outside India and the portion paid in India, were offered to tax in India by the respective expatriate employees in their returns of income, as the same accrued and arose in India.



6.2.2. It was submitted that the disallowance under consideration pertained only to the component of salary paid outside India by the Head Office. The Ld.Sr.Counsel submitted that the disallowance was made by the Ld.AO on the premise that such expenditure was in the nature of general administrative expenditure and, therefore, was covered within the scope of section 44C of the Act. The details of the expatriate employees are as under:—

Sr. No.	Name	India Designation	Foreign Currency	Amount	INR
1	Ajoy Kapoor	Head, Strategic Resourcing and Property Management	GBP	1,07,003	85,47,069
2	Allan Chris Low	Chief Executive Officer	GBP	2,30,045	1,82,86,525
3	Gramme Ardene	Head, Regional Service Centre	GBP	57,367	45,65,613
4	Mandeep Vohra	Credit Officer, Corporate and Institutional Banking	GBP	706	57,159
5	M. A Ravi Kumar	Head, Treasury	GBP	2,98,526	2,44,21,033
			USD	14,000	6,39,240
6	Robert Green	Head, Regional Service Centre	GBP	1,37,863	1,10,34,120
7	Vishu Ramachandran	Head, Consumer Banking	GBP	2,11,672	1,53,81,953
8	Tracey Gains	Head – Treasury	GBP	43,108	34,33,015
Total					Rs.8,63,65,727

6.3. At the outset, the Ld.Sr.Counsel submitted that the issue under consideration stands squarely covered in favour of the assessee by the orders passed by this *Tribunal* in the assessee's own case for the preceding assessment years. The details of the said decisions are as under:—



Sr. No.	Particulars
1	<i>Appellant's own Hon'ble ITAT order for AY 1994-95</i>
2	<i>Appellant's own Hon'ble ITAT order for AY 1995-96</i>
3	<i>Appellant's own Hon'ble ITAT order for AY 1997-98</i>
4	<i>Appellant's own Hon'ble ITAT order for AY 1998-99</i>
5	<i>Appellant's own Hon'ble ITAT order for AY 1999-00</i>
6	<i>Appellant's own Hon'ble ITAT order for AY 2000-01</i>
7	<i>Appellant's own Hon'ble ITAT order for AY 2001-02</i>
8	<i>Appellant's own Hon'ble ITAT order for AY 2002-03 and 2003-04</i>

6.4. The Ld.Sr.Counsel submitted that the facts and circumstances giving rise to the impugned addition during the year under consideration remained unchanged as compared to those prevailing in the preceding assessment years. It was submitted that the assessee had incurred the said expenditure wholly and exclusively for the purposes of its business by reimbursing to the Head Office the salary payments made by the Head Office to the expatriate employees in their respective home countries.

6.4.1. The Ld.Sr.Counsel contended that the expenditure represented salary costs of employees who were working exclusively for the India Branch and, therefore, the same was allowable as a business expenditure.

6.4.2. The Ld.Sr.Counsel further submitted that the expatriate salary payments were not in the nature of executive and general administrative expenses ("EGA") and, therefore, did not fall within the ambit of section 44C of the Act. In support of the said contention, the relevant extract of section 44C of the Act was reproduced as under:—

"Notwithstanding anything to the contrary contained in sections 28 to 43A, in the case of an assessee, being a non-resident, no allowance shall be made in



computing the income chargeable under the head "Profits and gains of business or profession", in respect of so much of the expenditure in the nature of head office expenditure as is in excess of the amount computed as hereunder, namely:—

- (a) an amount equal to five per cent of the adjusted total income; or*
- (b) where the adjusted total income of the assessee is a loss, an amount equal to five per cent of the average adjusted total income of the assessee; or*
- (c) the amount of so much of the expenditure in the nature of head office expenditure incurred by the assessee as is attributable to the business or profession of the assessee in India,*
whichever is the least.

Explanation.—For the purposes of this section,—

- (iv) "head office expenditure" means executive and general administration expenditure incurred by the assessee outside India, including expenditure incurred in respect of—*
 - (a) rent, rates, taxes, repairs or insurance of any premises outside India used for the purposes of the business or profession;*
 - (b) salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;*
 - (c) travelling by any employee or other person employed in, or managing the affairs of, any office outside India; and*
 - (d) such other matters connected with executive and general administration as may be prescribed.*

6.4.3. The Ld.Sr.Counsel submitted that the disallowance made by the Ld. AO by invoking the provisions of section 44C of the Act is unsustainable both on facts and in law. Referring to the definition of "head office expenditure" as contained in section 44C of the Act, it was submitted that the said provision applies only to executive and general administrative expenditure incurred by the assessee outside India in managing the affairs of an office outside India.

6.4.4. It was contended that the expatriate employees, in the present case, were seconded to India and were exclusively engaged in carrying out the activities of the Indian operations of the assessee. Since such employees were not involved in managing any office outside India, the salary paid to them could not be regarded as executive and general administrative expenditure falling within



the ambit of “head office expenditure” under section 44C. Accordingly, it was submitted that the restriction prescribed under section 44C had no application to the impugned expenditure.

6.4.5. The Ld.Sr.Counsel further submitted that section 44C was introduced to regulate claims in respect of common executive and general administrative expenditure incurred by foreign head offices and allocated to Indian operations. Referring to clause (c) of section 44C, it was argued that the expression “so much of the expenditure as is attributable to the business or profession of the assessee in India” indicates that the provision contemplates expenditure which is relatable to both Indian and overseas operations and requires apportionment between such activities.

6.4.6. It was submitted that, in the present case, the expatriate salary expenditure was incurred wholly and exclusively for the Indian business of the assessee and no part thereof was attributable to any business carried on outside India. Therefore, according to the Ld.Sr.Counsel, the said expenditure could not be subjected to the restriction prescribed under section 44C. In support of the aforesaid contention, reliance was placed on the decisions in *Rupenjuli Tea Co. Ltd. vs. CIT* reported in 186 ITR 301, *American Bureau of Shipping vs. ITO* reported in 19 ITD 793 and *IAC vs. Goodricke Group Ltd.* reported in 12 ITD 1.

6.4.7. The Ld.Sr.Counsel submitted that the expenditure incurred towards expatriate salaries had a direct nexus with the functions performed by such employees in India and was incurred wholly and exclusively for the purposes of the assessee’s Indian business. Since the expatriate employees were engaged in the Indian



operations of the assessee, the expenditure was allowable under section 37(1) of the Act.

6.4.8. Reliance was placed on the judgment of the *Hon'ble Bombay High Court* in *CIT vs. Emirates Commercial Bank Ltd.* reported in 262 ITR 55, wherein it was held that section 44C applies only to expenditure of a common nature incurred for various branches or for both the Head Office and the branch, and not to expenditure incurred exclusively for the Indian branch.

6.4.10. Reliance was also placed on the decision of the *Hon'ble Kolkata Bench of the Tribunal* in *ABN AMRO Bank NV vs. JCIT* in ITA No. 692/Cal/2000, wherein, following the aforesaid decision of *Hon'ble Bombay High Court*, it was held that remuneration paid outside India to expatriate employees rendering services in India was allowable as salary expenditure and could not be treated as head office expenditure under section 44C. It was held that salaries and bonuses paid to expatriate employees were incurred in India since the services were rendered in India and, therefore, did not fall within the definition of head office expenditure.

6.4.11. The Ld.Sr.Counsel further relied upon the decisions in *British Bank of Middle East vs. JCIT* reported in 4 SOT 122, *Bank of America NT&SA vs. DCIT* reported in 27 SOT 97, *American Bureau of Shipping vs. ITO* reported in 19 ITD 793, *DDIT vs. Chohung Bank* reported in 126 ITD 448, *Shinhan Bank vs. DDIT* reported in 23 taxmann.com 449 and *DDIT vs. Development Bank of Singapore* reported in 33 taxmann.com 300, wherein it was held that expenditure relating to expatriate employees working



exclusively for Indian operations could not be regarded as head office expenditure within the meaning of section 44C.

6.4.12. The Ld.Sr.Counsel also submitted that the expatriate salary expenditure had already been offered to tax in India by the respective expatriate employees in their individual returns of income. It was further submitted that the Ld.AO erred in disallowing the expenditure merely on the ground that the same had not been debited to the Profit and Loss Account of the Indian Branch.

6.4.12. It was contended that the Head Office and the Indian Branch constituted a single legal entity and, therefore, no separate debit entry was required to be passed in the books of the Indian Branch in respect of such expenditure. According to the Ld.Sr.Counsel, the allowability of expenditure is governed by the provisions of the Act and not by the accounting treatment adopted in the books of account. A lawful deduction could be claimed while computing taxable income irrespective of whether a corresponding entry was made in the books.

6.4.13. In support of this proposition, reliance was placed on the judgments on decisions of *Hon'ble Supreme Court* in case of *Kedarnath Jute Mfg. Co. Ltd. vs. CIT* reported in 82 ITR 363, *British Bank of Middle East vs. JCIT* reported in 4 SOT 122, *Bank of America NT&SA vs. DCIT (supra)*, *Sutlej Cotton Mills Ltd. vs. CIT* reported in 116 ITR 1, *ADIT vs. Mizuho Corporate Bank Ltd.* reported in 54 SOT 117 and *Ernst & Young Ltd. vs. ACIT* reported in 94 taxmann.com 227.



6.5. Without prejudice to the aforesaid submissions, the Ld.Sr.Counsel submitted that the expatriate salary expenditure was independently allowable under Article 7 of the India-UK Double Taxation Avoidance Agreement(DTAA). It was submitted that, in terms of section 90(2) of the Act, the assessee was entitled to avail the benefit of the provisions of the treaty to the extent the same were more beneficial than the provisions of the Act. Since the assessee was a resident of the United Kingdom, the provisions of the India-UK DTAA were applicable.

6.5.1. Referring to Article 7(5) of the Treaty, it was submitted that while computing the profits attributable to a Permanent Establishment, deduction is required to be allowed in respect of expenses incurred for the purposes of the Permanent Establishment, including executive and general administrative expenses, whether incurred in the State where the Permanent Establishment is situated or elsewhere. Accordingly, it was contended that the impugned expenditure was allowable under Article 7 of the Treaty and could not be restricted by invoking the provisions of section 44C of the Act.

6.5.2. The Ld.Sr.Counsel further distinguished the decision of the *Hon'ble Supreme Court* in case of *Centrica India Offshore (P.) Ltd. vs. CIT* reported in 44 *taxmann.com* 300, relied upon by the Revenue. It was submitted that, even in the earlier appellate proceedings for Assessment Years 2002-03 and 2003-04, it had been held that expatriate salaries were not covered within the ambit of section 44C of the Act.



6.5.3. It was argued that the facts in *Centrica India Offshore (P.) Ltd.*(supra) were distinguishable, inasmuch as the issue therein pertained to a transaction between two separate legal entities, namely, the foreign parent company and its Indian subsidiary. In the present case, however, the Head Office and the Indian Branch constituted the same legal entity and, therefore, there could be no question of income arising from a transaction undertaken with oneself.

6.5.4. It was submitted that since the expatriate employees of the Head Office/offshore branches were rendering services for the Indian Branch of the same entity, no separate income could be said to arise in the hands of the Head Office on account of such arrangement. Reliance in this regard was placed on the decisions in *Betts Hartley Huett & Co. Ltd. vs. CIT* reported in 116 ITR 425, decision of Hon'ble Mumbai Special bench in case of *Sumitomo Mitsui Banking Corporation vs. DDIT* reported in 136 ITD 66 (SB), *Dy. CIT (IT) vs. BNP Paribas S.A.* reported in 109 taxmann.com 391, decision of Hon'ble Supreme Court in case of *CIT vs. Sir Kikabhai Premchand* reported in 24 ITR 506 and *CIT vs. South India Viscose Ltd.* reported in 14 Taxman 259.

6.5.5. The Ld.Sr.Counsel further submitted that, in any event, the decision in *Centrica India Offshore (P.) Ltd.* (supra) was distinguishable on facts. Reliance was placed on the decision of the Hon'ble Pune Bench of the Tribunal in *Faurecia Automotive Holding vs. DCIT* in ITA No. 784/Pun/2015 dated 08/07/2019, wherein it was held that, seconded employees working under the supervision and control of the Indian entity would not give rise to fees for technical services merely on account of their expatriate status.



6.5.6. Reliance was also placed on the decision of *Hon'ble Bombay High Court* in *DIT vs. Marks and Spencer* reported in *TS-178-HC-2017*, wherein it was held that deputation of expatriate personnel does not by itself amount to rendering technical services and that mere provision of managerial or consultancy assistance, without transfer of technical knowledge, experience, skill, know-how or process, would not satisfy the “make available” condition under the India–UK DTAA.

6.5.7. It was emphasised that, in the present case, the salary income had already been offered to tax in India by the expatriate employees under the head “Salaries” and, therefore, there was no basis to treat the same amount as income attributable to the Head Office.

6.6. Without prejudice to the aforesaid submissions, the Ld.Sr.Counsel submitted that the provisions of section 195 of the Act were also not attracted in the facts of the present case. It was contended that the obligation to deduct tax under section 195 arises only at the time of payment or credit of any sum chargeable to tax in the hands of a non-resident. In the present case, there was neither any payment made nor any credit given in respect of the impugned expenditure to the account of the Head Office. Accordingly, it was submitted that the provisions of section 195 had no application.

6.6.1. The Ld.Sr.Counsel reiterated that the expatriate employees had already offered the entire salary income to tax in India and that this factual position had not been disputed by the Ld. AO. It was, therefore, submitted that the deduction claimed by the assessee



towards expatriate salary expenditure amounting to Rs.8,63,65,727/- ought to be allowed in full without invoking the provisions of section 44C of the Act and without making any disallowance on account of alleged non-deduction of tax at source.

6.6.2. The Ld.Sr.Counsel further brought to the notice of the Bench the decision of the *Hon'ble Delhi High Court* in the case of *Centrica India Offshore Pvt. Ltd. vs. CIT (supra)*, wherein it was held that tax deduction at source in respect of payments made under secondment arrangements would arise only where such payments partake the character of fees for technical services and the conditions prescribed under the Act are satisfied.

6.6.3. Referring to the aforesaid decision, the Ld.Sr.Counsel submitted that the services rendered by the expatriate employees in the present case could not be regarded as fees for technical services. It was submitted that the expatriate employees were engaged for the Indian operations and worked under the control, supervision and management of the Indian Branch. In support of the said contention, reliance was placed on the decision of the *Hon'ble Bangalore Bench of the Tribunal* in the case of *Goldman Sachs Services (P.) Ltd. vs. DCIT* reported in (2022) 138 *taxmann.com* 162 which has been approved by *Hon'ble Karnataka High Court* in *Pr.CIT (Intl.Tax) vs. Goldman Sachs Services (P.) Ltd.* reported in (2025) 179 *taxmann.com* 41.

6.6.4. The Ld.Sr.Counsel further submitted that the entire salary paid to the expatriate employees, including the component paid outside India by the Head Office, had been offered to tax in India by the concerned employees in their individual returns of income



under the head “Salaries”. It was, therefore, contended that there was no obligation to deduct tax at source on reimbursement of that portion of salary which had been paid by the Head Office to the family members or accounts of the expatriate employees in their respective home countries.

6.6.5. The Ld.Sr.Counsel further submitted that the issue relating to the applicability of section 28(iv) of the Act had been examined by the coordinate Bench of this *Tribunal* in the assessee’s own case for Assessment Years 2012-13 and 2013-14.

6.6.6. Reliance was further placed on the *decision of the coordinate Bench* in the case of *Shinhan Bank vs. DCIT* reported in 144 *taxmann.com* 182, wherein it was, inter alia, held that non-reimbursement of expenses incurred by the Head Office towards salary of employees deputed to the Indian Branch did not result in any taxable income in the hands of the Branch Office or the Head Office under section 28(iv) of the Act. It was submitted that, while rendering the said decision, the *Tribunal* had considered the relevant provisions of the India–Korea DTAA.

6.6.7. Based on the aforesaid decision, the Ld.Sr.Counsel contended that the same principle would apply with greater force in the present case, where the salary expenditure incurred by the Head Office had been reimbursed and the same had already suffered tax in India in the hands of the expatriate employees. It was, therefore, submitted that reimbursement of the salary component paid by the Head Office could not give rise to any taxable benefit under section 28(iv) of the Act, particularly when



the entire salary income had already been subjected to tax in India in the hands of the concerned expatriate employees.

6.6.8. On the contrary, the Ld.DR relied on the orders passed by the authorities below.

We have perused the submissions advanced by both sides in light of the records placed before this *Tribunal*.

7. We have considered the rival submissions and perused the material available on record. The issue before us relates to the allowability of expatriate salary expenditure claimed by the assessee and applicability of section 44C of the Act. The Ld.AO also took the view that the expenditure is not incurred for the purposes of business and therefore not eligible for deduction under section 37(1).

7.1. The Ld.AO proceeded on the basis that the expenditure incurred towards salaries paid by the Head Office to expatriate employees constituted “head office expenditure” and, therefore, was liable to be restricted under section 44C of the Act. In this regard, we note that section 44C is a specific provision which restricts deduction only in respect of executive and general administrative expenditure incurred by the assessee outside India in connection with the management of its affairs.

7.2. The applicability of section 44C depends upon the nature and character of the expenditure and not merely on the fact that the payment has been made from outside India. In the present case, the expatriate employees were deputed to India and were exclusively engaged in carrying out the business activities of the



India Branch. The expenditure represented salary costs in the hands of the assessee for services rendered in India and had direct nexus with the business operations carried on by the assessee in India.

7.3. The said expenditure was neither incurred for managing any office outside India nor was it in the nature of common executive and administrative overheads of the Head Office requiring allocation between Indian and overseas operations. The expenditure pertained exclusively to the Indian business of the assessee incurred by the assessee in India. Therefore, the same cannot be regarded as “head office expenditure” within the meaning of section 44C merely because the salary component was initially paid by the Head Office.

7.4. The objection of the Ld.AO is also that the expenditure was not incurred for the purposes of business of the assessee in India and, therefore, the same is not allowable under section 37(1) of the Act. However, we find that the allowability of an expenditure under section 37(1) has to be examined from the perspective of whether the expenditure has been incurred for the purposes of carrying on the business of the assessee and not merely on the basis of the entity from which the payment has originated.

7.5. In the present case, it is not disputed that the expatriate employees were rendering services in connection with the activities of the Indian branch and the expenditure was incurred in the course of carrying on the business of the assessee in India. The fact that such employees were employees of the overseas Head Office or that a part of the salary was initially borne by the Head Office



would not, by itself, disentitle the assessee from claiming the expenditure, if the same has been incurred for the business operations of the PE in India.

7.6. Further, the Ld.AO has not brought any material on record to establish that the expatriate employees did not perform any functions for the Indian branch or that the expenditure had no nexus with the business carried on by the assessee in India. In the absence of any such finding, the expenditure cannot be disallowed merely on a general observation that the liability was incurred outside India or was connected with the Head Office.

7.7. We further find that the assessee is entitled to rely upon the provisions of the India-UK Double Taxation Avoidance Agreement by virtue of section 90(2) of the Act. Article 7 of the India-UK DTAA provides that while determining the profits attributable to a Permanent Establishment, deduction shall be allowed for expenses incurred for the purposes of such Permanent Establishment, including executive and general administrative expenses, whether incurred in the State in which the Permanent Establishment is situated or elsewhere.

7.8. In the present case, the expatriate employees were rendering services exclusively for the India Branch, which constituted the Permanent Establishment of the assessee in India. The salary expenditure was incurred wholly for the purposes of such Permanent Establishment and was directly connected with the business carried on in India. Accordingly, the expenditure was allowable while computing the profits attributable to the Indian Permanent Establishment under Article 7 of the Treaty.



7.9. The treaty provision being more beneficial to the assessee, the same would prevail over the restrictive provisions of the Act in terms of section 90(2) of the Act. Therefore, even from the perspective of the India–UK DTAA, the impugned expenditure could not be disallowed or restricted by applying section 44C of the Act.

7.10. We note that identical issue has been examined by the coordinate Bench in the assessee’s own case for earlier assessment years, wherein it has been consistently held that expatriate salary expenditure incurred for the Indian Branch is allowable and cannot be treated as head office expenditure under section 44C. No distinguishing facts have been brought on record by the Revenue for the year under consideration.

7.11. We further note that entire salary income of the expatriate employees, including the portion paid in India as well as the portion initially paid by the Head Office in their respective home countries, was subjected to tax deduction at source in India. The assessee had deducted tax at source on 100% of the salary payable to such expatriate employees and the same had been offered to tax in India by the concerned employees in their individual returns of income under the head “Salaries”.

7.12. The portion of salary paid outside India by the Head Office was only a mode of payment and represented part of the overall salary cost attributable to the services rendered by the expatriate employees in India. The said amount was subsequently reimbursed by the Indian Permanent Establishment to the Head Office. Therefore, the reimbursement made by the India Branch cannot be regarded as a payment towards any independent service rendered



by the Head Office or as expenditure incurred for managing the affairs of an overseas office.

7.13. In substance, the expenditure represented salary cost of employees who were working exclusively for the Indian operations of the assessee. Since the entire salary income had already suffered tax in India and there was no dispute regarding the genuineness of the expenditure or the services rendered by the expatriate employees, the reimbursement of the salary component paid by the Head Office cannot be disallowed either by invoking section 44C or on the ground of non-deduction of tax at source.

7.14. The fact that a part of the salary was initially remitted by the Head Office does not change the character of the expenditure. What is relevant is the purpose for which the expenditure was incurred and the services for which the payment was made. In the present case, the expenditure was incurred wholly and exclusively for the business carried on by the Indian Permanent Establishment and is accordingly allowable.

7.15. In view of the above discussion and respectfully following the decisions of the Tribunal in the assessee's own case, we hold that the provisions of section 44C are not applicable to the expatriate salary expenditure claimed by the assessee. The expenditure is allowable under section 37(1) of the Act and also satisfies the conditions prescribed under Article 7 of the India-UK DTAA. We therefore do not find any infirmity in the view taken by the Ld.CIT(A) and the same is upheld.

Accordingly, Ground No.2 raised by the Revenue stands dismissed.



8. Ground Nos. 3 to 7 raised by the Revenue are in respect of the claim relating to interest income paid by the Head Office and overseas branches amounting to Rs.18,69,23,764/- to the assessee in India.

8.1. Brief facts giving rise to the present issue, as submitted by the Ld.Sr.Counsel, are that during the year under consideration, assessee paid interest on borrowings to Head Office /Overseas Branches ("HO/OB") amounting to Rs.18,89,23,764/- and claimed as deduction while computing taxable income of assessee. Also HO paid interest to assessee amounting to Rs.48,64,479/- which was offered to tax by assessee in its return of income at the applicable rate. Hence, the details of interest received by the HO from Standard Chartered Bank (SCB India) and paid by HO to assessee are as under:-

Particulars	Amount in INR
Interest paid by assessee to HO	18,89,23,764
Interest paid by HO to assessee	(48,64,479)

As the interest paid by assessee to HO/OB is not taxable in India, SCB India had not deducted tax at source while crediting/paying the interest to HO/OB.

8.2. The Ld.Sr.Counsel submitted that, without appreciating the fact that the said interest was not taxable in India, the Ld.AO proceeded to tax the interest in the hands of the Head Office in India. Consequently, the Ld.AO also disallowed the corresponding interest payment in the hands of the assessee by invoking the



provisions of section 40(a)(i) of the Act on the ground that tax had not been deducted at source u/s.195 of the Act.

8.3. The Ld.Sr.Counsel submitted that both the aforesaid issues are intrinsically linked and consequential to each other. It was, therefore, contended that common submissions would apply while adjudicating both the grounds under consideration.

8.4. The Ld.Sr.Counsel submitted that the interest paid by the SCB Indian to its HO/OB is not chargeable to tax in India and, consequently, no tax was deductible at source under section 195 of the Act. It was submitted that the Indian Branch constitutes a Permanent Establishment ("PE") of the assessee in India carrying on banking business and is merely a part and parcel of the same legal entity, namely the assessee-bank. The PE in India and the HO abroad are not independent persons and are not assessed separately in India. The taxable entity is only the assessee-bank and its business income is taxable in India only to the extent attributable to the PE. Therefore, the interest paid by the SCB Indian to the HO/OB is merely a payment to self.

8.5. The Ld.Sr.Counsel submitted that it is a settled proposition in law that no person can make profit out of himself. Since the source and the recipient are one and the same person, the payment of interest by the SCB Indian Branch to the HO/OB cannot give rise to any income chargeable to tax in India. Reliance in this regard was placed on *Betts Hartley & Co. Ltd. v. CIT* reported in [1979] 116 ITR 425 (Calcutta) wherein the Hon'ble Calcutta High Court held that there cannot be a valid transaction between the branch office and the head office of the same entity and that no



person can enter into a contract with himself. Reliance was also placed on *CIT v. Sir Kikabhai Premchand* reported in [1953] 24 ITR 506, wherein the *Hon'ble Supreme Court* reiterated the principle that no person can make profit out of himself.

8.6. The Ld.Sr.Counsel further submitted that this legal position was recognized by the legislature while introducing the amendment in section 9(1)(v) of the Act by the Finance Act, 2015. By the said amendment, a deeming fiction was created treating the PE of a foreign bank as a separate and independent person from the foreign bank for the purpose of taxing interest paid by a PE in India to its HO/OB. The amendment was made effective prospectively from AY 2016-17, i.e., from 01.04.2016. Thus, prior to the said amendment, the branch and the HO were admittedly not regarded as separate entities for this purpose. Accordingly, the interest paid by the SCB Indian Branch to the HO/OB could not be regarded as income chargeable to tax in India under the provisions of the Act.

8.7. Without prejudice to the provisions of the Act, the Ld.Sr.Counsel submitted that the assessee is a tax resident of the United Kingdom and, therefore, in terms of section 90(2) of the Act, is entitled to claim the benefit of the India-UK DTAA to the extent it is more beneficial. It was submitted that the learned AO has sought to tax the impugned interest under Article 12 of the India-UK DTAA. However, Article 12 inherently contemplates the existence of two separate entities, namely a payer and a recipient. In the present case, there exists only one legal entity, namely the assessee-bank. Consequently, the interest paid by the SCB Indian Branch to the HO/OB cannot be brought to tax under Article 12(2) of the DTAA.



8.8. The Ld.Sr.Counsel further submitted that under Article 12(6) read with Article 7 of the DTAA, where a resident of the UK carries on business in India through a PE and the debt claim in respect of which the interest is paid is effectively connected with such PE, Article 7 dealing with business profits would apply. However, reliance was placed on the decision of the *Hon'ble Mumbai Special Bench* of this *Tribunal* in case of *Sumitomo Mitsui Banking Corporation v. DDIT* reported in [2012] 136 ITD 66 (Mumbai) (SB), wherein it was held that the debt belongs to the HO, which is the economic owner thereof, and consequently the debt cannot be said to be effectively connected with the Indian PE. Therefore, Article 7 cannot be invoked to tax such interest. Reliance was also placed on the *OECD Commentary on the Model Tax Convention on Income and on Capital (Condensed Version, 2017)*, particularly paragraphs 24 and 25, in support of the proposition that the debt belongs to the HO and not to the PE.

8.9. The Ld. Sr.Counsel further submitted that the Ld.AO erred in extending the fiction contained in Article 7(2) of the DTAA to Article 12. It was contended that the deeming fiction under Article 7(2), whereby a Permanent Establishment is treated as a separate and independent enterprise for determining the profits attributable to such PE, is limited only to the computation of business profits under Article 7 and cannot be extended beyond the purpose for which it is created. The Ld. Senior Counsel submitted that the said fiction cannot be imported into Article 12 for the purpose of taxing interest paid by the Indian Branch to its Head Office/Overseas Branch. Reliance was placed on the decision of the *Hon'ble Special Bench* in the case of *Sumitomo Mitsui Banking Corporation v. DDIT*



(*supra*), wherein it was held that the fiction created under Article 7(2) is restricted to the determination of profits attributable to the PE and cannot be extended to other provisions of the DTAA. It was further submitted that legal fictions are created for a definite purpose and cannot be extended beyond their legitimate field, placing reliance on the decision of the *Hon'ble Supreme Court* in case of *CIT v. Mother India Refrigeration Industries Pvt. Ltd.* reported in (1985) 155 ITR 711. Reference was also made to Paragraph 28 of the OECD Commentary on Article 7 (2017). The Ld.Sr.Counsel further submitted that wherever the Contracting States intended to tax interest paid by a PE to its Head Office, specific provisions have been incorporated in the Treaty itself, as is evident from Article 14(3) of the India–USA DTAA, which specifically provides for taxation of interest paid by the Indian PE of a banking company to its Head Office in the USA. However, no such corresponding provision exists in the India–UK DTAA. Accordingly, in the absence of any specific provision treating the PE and the Head Office as separate persons for the purpose of Article 12, the interest paid by the Indian Branch to the HO/OB cannot be brought to tax in India in the hands of the Head Office.

8.10. The Ld.Sr.Counsel submitted that the provisions relating to "Interest" and "Business Profits" under the India-UK DTAA are *pari materia* with the corresponding provisions contained in the India-Japan DTAA and India-Netherlands DTAA. In this regard, reliance was placed on *ABN Amro Bank N.V. v. CIT* reported in [2012] 343 ITR 81 (Cal.), wherein the *Hon'ble Calcutta High Court*, while interpreting India-Netherlands DTAA, held that interest paid by an Indian branch to its HO is not taxable in the hands of the HO. It is



submitted that Special Leave Petition preferred by the Revenue against the said decision was dismissed by the *Hon'ble Supreme Court* in case of *CIT v. Mother India Refrigeration Industries Pvt. Ltd.*(*supra*)

8.11. The Ld.Sr.Counsel submitted that the issue is squarely covered in favour of the assessee by the decision of the Special Bench in *Sumitomo Mitsui Banking Corporation v. DDIT (supra)*, wherein it was held that interest paid by a branch to its HO is merely a payment to self and cannot be taxed either under the Act or under the applicable DTAA. *Hon'ble Special Bench* further held that since such interest is not chargeable to tax in India, no tax is deductible under section 195 of the Act and consequently no disallowance can be made under section 40(a)(i) of the Act.

8.12. The Ld.Sr.Counsel further relied on following decisions in support of the above proposition:

- a) *Deputy Director of Income-tax (IT)-4(1) v. Mizuho Corporate Bank Ltd.* reported in [2012] 24 taxmann.com 268 (Mum.);
- b) *BNP Paribas SA v. ADIT (IT)-3(2)* reported in [2016] 69 taxmann.com 6 (Mumbai - Trib.);
- c) *BNP Paribas SA v. DDIT (IT)-3(2)* reported in [2012] 23 taxmann.com 450 (Mumbai);
- d) *Credit Agricole Corporate & Investment Bank v. ACIT (IT)-1(2)* reported in [2015] 53 taxmann.com 426 (Mumbai - Trib.);
- e) *Deutsche Bank AG v. Assistant Director of Income-tax (International Taxation)-1(2)*, Mumbai reported in [2014] 47 taxmann.com 378 (Mumbai - Trib.);
- f) *JP Morgan Chase Bank NA v. Dy. Commissioner of Income-tax (IT), Circle-3(1)(1)*, Mumbai reported in ITA No.3747/Mum/2018 and ITA No. 363/Mum/2019;
- g) *Credit Suisse AG v. Deputy Commissioner of Income-tax (International Taxation)*, Mumbai reported in (2019) 104 taxmann.com 339.

8.13. Based on the aforesaid, the Ld.Sr.Counsel submitted that the interest paid by the assessee's Indian Branch to its HO/OB is not taxable in the hands of the HO and, therefore, no obligation to



deduct tax at source under section 195 arises. Since section 195 applies only where the payment is chargeable to tax in India, the disallowance made under section 40(a)(i) for non-deduction of tax at source is wholly unsustainable.

8.14. The Ld.Sr.Counsel further submitted that the Ld.AO erred in placing reliance upon CBDT Circular No. 740 dated 17.04.1996. It was submitted that the said Circular had already been considered and distinguished by *Hon'ble Mumbai Special Bench in Sumitomo Mitsui Banking Corporation v. DDIT(supra)*. It was argued that a Board Circular cannot create a charge to tax where none exists under the provisions of the Act. Once the impugned interest is not chargeable to tax under the Act, the same cannot be brought to tax merely on the basis of a Circular.

8.15. The Ld.Sr.Counsel assailed the reliance placed by Ld.AO on extracts from *Klaus Vogel's Commentary on Double Taxation Conventions*. It was submitted that the passages relied upon by the Ld.AO dealt with payments made by a PE situated in one Contracting State to an enterprise of the other Contracting State, i.e., payments to a third party enterprise. The said commentary does not deal with a payment by a PE to its own HO and is, therefore, wholly irrelevant to the issue under consideration.

8.16. In view of the aforesaid submissions, the Ld.Sr.Counsel submitted that the interest of Rs.18,89,23,764/- paid by the assessee's Indian Branch to its HO/OB be allowed as a deduction and that the corresponding addition made in the hands of the HO be deleted since the amount is not chargeable to tax in India. It was further submitted, without prejudice, that if the interest is



held to be taxable in the hands of the HO, the same should be taxed only on a net basis after allowing deduction of the interest paid by the HO to the Indian Branch, which had already been offered to tax by the Indian Branch in its return of income. The Ld.Sr.Counsel further submitted that disallowance of Rs.18,89,23,764/- in the assessment of the PE and simultaneous taxation of the same amount in the hands of the HO would amount to taxing the same income twice and is therefore unsustainable in law.

8.17. The Ld.Sr.Counsel also submitted that Ld.AO erred in not allowing assessee's claim under the proviso to section 40(a)(i) in respect of interest paid to the HO amounting to Rs.2,24,54,183/-, comprising Rs.32,44,183/- pertaining to AY 2001-02 and Rs.1,92,10,100/- pertaining to AY 1997-98. It was submitted that while the reassessment proceedings for AY 1997-98 have already been quashed by the *Tribunal*, the claim for deduction in respect thereof has been maintained on a protective basis in the event the Revenue prefers a further appeal against the order of the *Tribunal*.

8.18. *Per contra*, the Ld.DR relied on the orders passed by the authorities below and reiterated the submissions advanced before them.

We have perused the submissions advanced by both sides in light of the records placed before this *Tribunal*.

9. We have also carefully considered the orders passed by the authorities below. We find that the issue under consideration is no longer *res integra* in view of the decision of *Hon'ble Special Bench, Mumbai Tribunal* in *Sumitomo Mitsui Banking Corporation v. DDIT (Supra)*.



9.1. In the said decision, *Hon'ble Special Bench*, after elaborate consideration of the provisions of the Act, the applicable tax treaty provisions and various judicial precedents, held that interest paid by the Indian branch of a foreign bank to its Head Office and Overseas Branches is merely payment to self and, therefore, does not give rise to income chargeable to tax in India in the hands of the Head Office. *Hon'ble Special Bench* further held that since such interest is not chargeable to tax in India, there is no obligation to deduct tax at source under section 195 of the Act and, consequently, no disallowance can be made under section 40(a)(i) of the Act.

9.2. The aforesaid view has subsequently been followed in *ABN Amro Bank N.V. v. CIT* reported in [2012] 343 ITR 81 (Cal.), *Deputy Director of Income-tax (IT)-4(1) v. Mizuho Corporate Bank Ltd.* reported in [2012] 24 taxmann.com 268 (Mum.), *BNP Paribas SA v. ADIT (IT)-3(2)* reported in [2016] 69 taxmann.com 6 (Mumbai - Trib.), *Credit Agricole Corporate & Investment Bank v. ACIT (IT)-1(2)* reported in [2015] 53 taxmann.com 426 (Mumbai - Trib.), *Deutsche Bank AG v. Assistant Director of Income-tax (International Taxation)-1(2)*, Mumbai reported in [2014] 47 taxmann.com 378 (Mumbai - Trib.), *JP Morgan Chase Bank NA v. Dy. Commissioner of Income-tax (IT), Circle-3(1)(1)*, Mumbai reported in (2019) ITA No. 3747/Mum./2018 and ITA No. 363/Mum./2019, and *Credit Suisse AG v. Deputy Commissioner of Income-tax (International Taxation)*, Mumbai reported in (2019) 104 taxmann.com 339.

9.3. Respectfully following the ratio laid down by the *Hon'ble Special Bench* and the judicial precedents noted hereinabove, we hold that the interest paid by the assessee's Indian Branch to its



Head Office/Overseas Branches cannot be brought to tax in India in the hands of the Head Office. Consequently, no obligation to deduct tax at source under section 195 of the Act arises and the corresponding disallowance made under section 40(a)(i) of the Act is liable to be deleted.

Accordingly, these Ground Nos. 3 to 7 raised by revenue stands dismissed.

10. Ground Nos. 8 and 9 raised by the Revenue are in respect of the allowability of interest paid by the assessee to its Head Office amounting to Rs.18,89,23,764/-.

10.1. We note that this issue has become infructuous in view of our findings while adjudicating Ground Nos. 3 to 7 hereinabove, wherein we have upheld the order of the Ld. CIT(A) holding that the interest paid by the assessee's Indian Branch to its Head Office/Overseas Branches is not chargeable to tax in India and consequently no disallowance under section 40(a)(i) of the Act is warranted.

Accordingly, in view of the conclusions reached by us while deciding Ground Nos. 3 to 7, we find no infirmity in the order of the Ld. CIT(A) on this issue. The same is, therefore, upheld.

Accordingly, Ground Nos. 8 and 9 raised by the Revenue stand dismissed.

11. Ground No. 10 raised by the Revenue is in respect of the relief granted by the Ld.CIT(A) in relation to disallowance of expenditure amounting to Rs.31,16,33,936/- alleged to be attributable to



exempt income earned by the assessee during the year under consideration.

11.1. The facts leading to the present issue are that during the relevant previous year, the assessee earned interest income amounting to Rs.58,17,32,193/-, which was claimed as exempt under section 10(23G) of the Act. During the assessment proceedings, the assessee furnished all relevant documents and details in support of its claim and submitted before the Ld.AO that the provisions of section 14A of the Act were not applicable to the aforesaid exempt income for, inter alia, the following reasons:-

- “a) assessee has not incurred any expense attributable to exempt income;*
- b) Its own/free funds are in excess of the funds required for investment in the securities from which exempt income has been earned;*
- c) The funds of the assessee are fungible and it is engaged into indivisible business;*
- d) Cash profit for the FY under consideration was more than the incremental investments made during the FY under consideration;*
- e) The securities yield both tax-free income as well as taxable income. The tax free income arises in the form of interest on securities while the taxable income arises in their sale; and*
- f) The assessee relied on some judicial precedents supporting the above.”*

11.2. The Ld.AO, disallowed expenditure attributable to earning of exempt income. The Ld.AO held that the net interest post reducing the proportionate expenses was thereafter eligible to exempted u/s 10(23G) of the Act.

Aggrieved by the order of Ld.AO assessee preferred appeal before Ld.CIT(A).



11.3. Before the Ld. CIT(A), the assessee submitted that the issue was covered by various decisions of the Coordinate Benches of the Tribunal in assessee's own case for the preceding assessment years, wherein the disallowance under section 14A of the Act was restricted to 1% of the exempt income. It was submitted that, after considering the facts of the case and the submissions made by the assessee, the Ld.CIT(A) accepted the contention of the assessee that only a nominal disallowance was warranted and accordingly restricted the disallowance under section 14A of the Act at 1% of the exempt income for the year under consideration. It was further submitted that the said methodology adopted by the Ld.CIT(A) was accepted by the assessee and, therefore, no grievance survives from the assessee's perspective in respect of the said issue.

11.4. Per contra, the Ld.DR relied on the order passed by the Ld.AO.

We have perused the submissions advanced by both sides in light of the records placed before this *Tribunal*.

12. It is noted that the issue is recurring in the case of the assessee and has been considered by the *Tribunal* in the assessee's own case for the preceding assessment years. The Ld.Sr.Counsel submitted that the assessee had sufficient own funds and non-interest-bearing funds, which were substantially higher than the investments yielding exempt income, and therefore, no disallowance on account of interest expenditure was warranted. It was further submitted that no borrowed funds had been utilized for making the investments from which the exempt income was earned.



12.1. However, considering the consistent view taken by the *Coordinate Benches of the Tribunal* in the assessee's own case for the preceding assessment years, wherein the disallowance under section 14A of the Act was restricted to 1% of the exempt income, we find no reason to take a different view for the year under consideration. Accordingly, the disallowance sustained by the Ld. CIT(A) at 1% of the exempt income is upheld. We, therefore, do not find any infirmity in the order passed by the Ld. CIT(A) and the same is accordingly upheld.

Accordingly, Ground No.10 raised by the Revenue stands dismissed.

13. Ground No. 11 raised by the Revenue pertains to allowability of assessee's claim of recoveries against securities loss of Rs.4,62,27,884/-.

13.1. The assessee had incurred certain losses on securities transactions in Assessment Year 1993-94, out of which certain recoveries were made during the year under consideration. The Ld. Authorised Representative submitted that the aforesaid ground was originally raised since the allowability of such losses in Assessment Year 1993-94 was a matter of dispute.

13.2. It was submitted that the Coordinate Bench of the Tribunal, in assessee's own case for assessment year 1993-94, vide order dated 27/07/2023, allowed the said losses claimed by the assessee. Accordingly, in view of the aforesaid decision, the assessee did not press this ground before the Ld.CIT(A) for the year under consideration. However, the assessee requested the Ld.CIT(A) to issue a protective direction that, in the event the



Revenue succeeds before the Hon'ble High Court/Hon'ble Supreme Court in respect of assessment year 1993-94 and the said losses are ultimately held to be not allowable, the recoveries relating to such securities losses should not be brought to tax in the year under consideration.

13.3. The Ld.CIT(A) accordingly recorded following categorical finding:–

“10.2 Further, subsequent to receipt of ITAT order for AYs 1998-99, 2000-01 and AY 2001-02, the Appellant filed submission on 19 December 2023 highlighting the incremental issues emanating from the said ITAT orders (vis-à-vis ITAT order for AY 1999-2000). In respect of this ground, the Appellant submitted as under:

Gr. No.	Ground of Appeal in AY 2004-05	Incremental issue and the ITAT's finding on the same in the recent orders	Our comments / remarks for AY 2004-05
7	Recovery of securities losses	The Hon'ble ITAT held in AY2001-02 that recovery made on account of losses of earlier AY is taxable however, the same is subject to final conclusion by the higher / final appellate authorities on allowability of the said losses [Refer page 39 of AY 2001-02]	We request your Honour to kindly issue similar directions while disposing off the captioned appeal on this ground

10.3 Further, during the course of hearing on 27 February 2025, the Appellant submitted that losses under consideration are allowed by the Hon'ble ITAT in AY 1993-94 and accordingly, the Appellant does not want to press this ground. However, it sought direction that in case the Department succeed in its appeal before the Hon'ble High Court / Supreme Court in AY1993-94 that loss is not allowable in the said AY, then the Ld. AO be directed to not to tax the recoveries against the said securities losses in this AY i.e. AY2004-05. In this regard, the Appellant submitted that the Hon'ble ITAT in AY 2001-02, 2002-03 and 2003-04 has given the said direction.

10.4 Decision on Ground 7

I have considered the submission of the Appellant. The Appellant does not want to press this ground however, has sought a direction as stated above. I agree with the contention raised by the Appellant and I accordingly direct the AO that in case the Department succeed in its appeal before the Hon'ble High Court / Supreme Court in AY 1993-94 that



loss is not allowable in the AY 1993-94, then the recoveries made against the said securities losses should not be taxed in AY 2004-05."

We have perused the submissions advanced by both sides in light of records placed before us.

14. We have considered the rival submissions and perused the material available on record. We find that the direction issued by the Ld.CIT(A) merely safeguards the consequential treatment of the recoveries made during the year under consideration, depending upon the final outcome of the proceedings relating to Assessment Year 1993-94. Since the allowability of the securities losses for Assessment Year 1993-94 is pending adjudication before the higher judicial forums, we do not find any infirmity in the directions issued by the Ld.CIT(A). Accordingly, the same are upheld. The Ld.AO is directed to decide the issue in accordance with the final outcome of the appeals filed before the *Hon'ble High Court/Hon'ble Supreme Court* for Assessment Year 1993-94.

14.1. It is clarified that, in the event the order of the *Tribunal* for Assessment Year 1993-94 is upheld and the securities losses are ultimately held to be allowable in that year, the corresponding recoveries relating to such securities losses shall not be brought to tax in the year under consideration.

Accordingly, Ground No. 11 raised by the Revenue is treated as allowed partly allowed for statistical purposes.

15. Ground No. 12, raised by the revenue is against allowability of deduction claimed by assessee under the Head Office expenditure in entirety amounting to Rs.192,44,66,501/-.



Brief facts relating to this issue, as submitted by the Ld. Senior Counsel, are that during the year under consideration, the Head Office allocated expenditure amounting to ₹192,44,66,501/- to the assessee. In the return of income filed by the assessee, deduction towards Head Office expenditure amounting to ₹36,14,16,495/- was claimed, being 5% of the adjusted total income. The Ld.Sr.Counsel submitted that, after making various additions and adjustments to the total income, the Ld.AO restricted the deduction towards Head Office expenditure to ₹4,34,30,171/- under section 44C of the Act.

15.2. The Ld.Sr.Counsel submitted that, in terms of Article 26 of the India–UK DTAA, the assessee is entitled to claim deduction of the entire Head Office expenditure without being subjected to the restriction prescribed under section 44C of the Act. It was submitted that the Ld.AO, without appreciating the provisions of Article 26 of the Treaty, held that in terms of Article 7(5) of the DTAA, deduction towards Head Office expenditure was allowable only subject to the limitations prescribed under the domestic law, namely section 44C of the Act.

15.2.1. The Ld.Sr.Counsel submitted that section 44C places a restriction on the quantum of deduction available to a non-resident enterprise in respect of Head Office expenditure incurred for the purposes of its Permanent Establishment in India. Under the said provision, deduction towards Head Office expenditure while computing the taxable business income of the Permanent Establishment is restricted to the lower of (i) 5% of the adjusted total income, or (ii) the actual expenditure attributable to the Permanent Establishment.



15.3. It was contended that no similar restriction is applicable to a resident enterprise claiming expenditure incurred for the purposes of its business. Accordingly, the limitation prescribed under section 44C results in discriminatory treatment of a non-resident enterprise vis-à-vis a resident enterprise carrying on similar activities. The Ld.Sr.Counsel submitted that, in terms of Article 26 of the India–UK DTAA read with section 90(2) of the Act, where the provisions of the Treaty are more beneficial to the assessee, the same would prevail over the provisions of the Act. Therefore, the assessee is entitled to claim deduction of the entire Head Office expenditure without applying the restriction contained in section 44C of the Act.

15.4. The Ld.Sr.Counsel further submitted that a harmonious reading of Articles 7(5) and 26(2) of the India–UK DTAA would show that the limitations under the domestic law can be applied to a UK enterprise only if such limitations are equally applicable to resident enterprises. Since section 44C imposes a restriction exclusively upon non-resident enterprises, the same cannot be applied in the case of the assessee in view of the non-discrimination provision contained in Article 26(2).

15.4.1. The Ld.Sr.Counsel submitted that Article 26(2) of the India–UK DTAA does not carve out any exclusion in respect of Article 7(5), unlike certain other treaties such as the India–USA DTAA and India–Singapore DTAA, wherein specific exclusions have been provided in relation to the computation of profits of a PE. It was submitted that absence of such an exclusion in the India–UK DTAA indicates that, protection provided under Article 26(2) would apply while determining the tax treatment of the Permanent



Establishment under Article 7. Accordingly, he submitted that limitations imposed under the domestic law can be applied only if such limitations are equally applicable to resident and non-resident enterprises.

15.4.2. The Ld.Sr.Counsel submitted that, since section 44C imposes a restriction exclusively on non-resident enterprises, the same being discriminatory in nature, cannot be applied to the assessee in view of Article 26(2) of the India-UK DTAA. In support he placed reliance on the decision of the Co-ordinate Bench of the *Tribunal* in case of *Metchem Canada Inc. v/s. DCIT* reported in 284 *ITR (A.T.) 196*, wherein this *Tribunal* observed that:

(a) the limitation placed under the Act, violated the non-discrimination Article 24(2) of the India-Canada Treaty because the limitation did not apply to resident Indian companies and held that under Article 24 of the India-Canada Treaty, the provision of Section 44C of the Act has no application and the assessee is entitled to full deduction of HOE without applying the provisions of Section 44C the Act.

(b) In this case, it was also held that Special provisions i.e., Article 26(2) would take precedence over general provisions i.e., Article 7(5). It was also held that since the provisions of the treaty prevail over the provisions of the Act, the restrictions placed on the allowability of the head office expenditure by section 44C were to be ignored in the light of the provisions of article 24(2).

(c) It was also observed that when a tax treaty provision was identical to a provision in the OECD Commentary, unless it was specifically stipulated to the contrary in the tax treaty or by way of



a protocol to the tax treaty, it was reasonable to presume that the Contracting States were aware about the implications of that provision.

15.5. The Ld.Sr.Counsel further submitted that Article 26(2) of the India–UK DTAA is *pari materia* with Article 24(2) of the India–Canada DTAA. It was submitted that both provisions embody the principle of non-discrimination and provide that taxation of a Permanent Establishment of an enterprise of one Contracting State in the other Contracting State shall not be less favourably levied than the taxation applicable to enterprises of that other State carrying on the same activities under similar circumstances or conditions. For ready reference, the relevant extracts of the non-discrimination provisions under the India–UK DTAA and India–Canada DTAA are reproduced below:

Provision	India – UK Treaty	India – Canada Treaty
Non-discrimination	Article 26(2)	Article 24(2)
	“The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favorably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities in the same circumstances or under the same conditions.....”	“The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favorably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities.”

15.6. The Ld. Senior Counsel submitted that since the language and object of Article 26(2) of the India–UK DTAA are substantially similar to Article 24(2) of the India–Canada DTAA, the ratio laid down by the Coordinate Bench in the case of *Metchem Canada Inc.*



v. DCIT (supra) would squarely apply. It was submitted that in the said decision, the Tribunal held that the restriction imposed under section 44C of the Act, being applicable only to non-resident enterprises and not to resident enterprises, resulted in discriminatory treatment and therefore could not be enforced in view of the non-discrimination clause contained in the Treaty.

15.7. Reliance was also placed on the decision of *Hon'ble Delhi Bench of this Tribunal*, in the case of *Rolls Royce Industrial Power Ltd.* reported in 42 SOT 264, wherein it was held that, Article 26 of the India-UK DTAA negated the applicability of restrictive provisions contained in section 44D of the Act, as the said provision applied only to non-resident taxpayers. He submitted that *Hon'ble Tribunal* held that where a non-resident enterprise was subjected to a more burdensome taxation regime as compared to a domestic enterprise carrying on similar activities, the benefit of the non-discrimination provision under Article 26 of the DTAA had to be extended.

15.8. The Ld.Sr.Counsel, thus submitted that, the issue is covered by various decisions of Co-ordinate Bench of this *Tribunal* in assessee own case. The details of which are as under:-

A.Y.	ITA No.
1998-99	3377/Mum/2006
1999-00	803/Mum/2004
2000-01	3458/Mum/2009
2001-02	4867/Mum/2017
2002-03	1407/Mum/2019
2003-04	2936/Mum/2019

15.9. The Ld.DR submitted that the issue stands covered against the assessee by the decision of *Hon'ble Supreme Court* in the case



of *DIT (IT) v. American Express Bank Ltd.* reported in (2025) 181 *taxmann.com* 433. It was submitted that the *Hon'ble Supreme Court* upheld the applicability of section 44C in respect of Head Office expenditure claimed by a non-resident enterprise and held that, once the expenditure falls within the ambit of “Head Office expenditure” as defined under the Act, the deduction is subject to the restriction prescribed under section 44C.

15.10. It was submitted that section 44C is a specific provision enacted to determine the allowable quantum of Head Office expenditure attributable to the Indian Permanent Establishment and constitutes a part of the scheme for computation of income of a non-resident enterprise. Therefore, the restriction prescribed under section 44C cannot be regarded as discriminatory merely because a similar provision does not apply to resident enterprises. The Ld.DR submitted that the decision of *Hon'ble Supreme Court*, being the law of the land, overrides the earlier decisions relied upon by the assessee.

15.11. It was further submitted that Article 7(5) of the India-UK DTAA specifically provides that the determination of profits attributable to the Permanent Establishment shall be subject to the provisions of the domestic law of the State in which the PE is situated. Therefore, the limitation prescribed under section 44C has to be given effect while computing the profits attributable to the Indian PE.

We have perused the submissions advanced by both sides in light of records placed before us.



16. The controversy before us concerns the applicability of section 44C of the Income-tax Act, 1961 vis-à-vis Articles 7 and 26 of the India–UK DTAA. The Ld.Sr.Counsel submitted that since Article 26(2) mandates that, taxation of a PE of a UK enterprise shall not be less favourably levied than that of an Indian enterprise carrying on the same activities under the same conditions, the restriction contained in section 44C, being applicable only to non-resident enterprises, stands overridden by virtue of section 90(2) of the Act.

16.1 On the other hand, the Ld.DR placed reliance on the decision of the *Hon'ble Supreme Court* in case of *DIT (Intl. Tax) vs. American Express Bank Ltd.*(supra) and contended that section 44C is a special computation provision enacted to regulate the deduction of head office expenditure incurred by non-resident enterprises and, therefore, the statutory limitation has necessarily to be given effect.

16.2 We find no difficulty in accepting the proposition laid down by the *Hon'ble Supreme Court* in *American Express Bank Ltd.*(supra). The said decision authoritatively recognises section 44C as a special computation provision governing the deduction of head office expenditure of foreign enterprises. However, it is equally necessary to bear in mind that the said decision was rendered in the context of Article 7(3) of the India–USA DTAA, which expressly provides that the deduction of expenses attributable to the Permanent Establishment shall be allowed in accordance with and subject to the limitations of the taxation laws of the source State. The present appeal, however, is governed by the India–UK DTAA, whose provisions are materially different and, therefore, require independent examination.



16.3 Under the India–UK DTAA, Article 7 constitutes a self-contained code governing the attribution of profits to a Permanent Establishment. It is necessary to reproduce Article 7 of India UK DTAA as under:

Article 7 – Business Profits

- 1. The profits of an enterprise of a Contracting State shall be taxable only in that State unless the enterprise carries on business in the other Contracting State through a permanent establishment situated therein. If the enterprise carries on business as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is directly or indirectly attributable to that permanent establishment.*
- 2. Subject to the provisions of paragraph (3) of this Article, where an enterprise of a Contracting State carries on business in the other Contracting State through a permanent establishment situated therein, there shall in each Contracting State be attributed to that permanent establishment the profits which it might be expected to make if it were a distinct and separate enterprise engaged in the same or similar activities under the same or similar conditions and dealing wholly independently with the enterprise of which it is a permanent establishment.*
- 3. In the determination of the profits of a permanent establishment, there shall be allowed as deductions expenses which are incurred for the purposes of the permanent establishment, including executive and general administrative expenses so incurred, whether in the State in which the permanent establishment is situated or elsewhere, in accordance with the provisions of and subject to the limitations of the taxation laws of that State.*
- 4. In so far as it has been customary in a Contracting State to determine the profits to be attributed to a permanent establishment on the basis of an apportionment of the total profits of the enterprise to its various parts, nothing in paragraph (2) of this Article shall preclude that Contracting State from determining the profits to be taxed by such an apportionment as may be customary. The method of apportionment adopted shall, however, be such that the result shall be in accordance with the principles contained in this Article.*
- 5. No profits shall be attributed to a permanent establishment by reason of the mere purchase by that permanent establishment of goods or merchandise for the enterprise.*
- 6. For the purposes of the preceding paragraphs, the profits to be attributed to the permanent establishment shall be determined by the same method year by year unless there is good and sufficient reason to the contrary.*
- 7. Where profits include items of income which are dealt with separately in other Articles of this Convention, then the provisions of those Articles shall not be affected by the provisions of this Article.*



16.3.1. On a bare perusal of the above it can be noted that Article 7(2) embodies separate enterprise principle, Article 7(4) recognises that where it has been customary in a Contracting State to determine the profits attributable to a PE by apportioning the total profits of the enterprise to its various parts, such method may continue to be adopted, provided the result is in accordance with the principles contained in Article 7.

16.3.2. A harmonious reading of Article 7 of the India–UK DTAA shows that while paragraph (2) lays down the substantive principle for attributing profits to a PE by treating it as a distinct and separate enterprise, paragraph (4) expressly preserves the customary domestic mechanism for such attribution through apportionment, subject to the overriding requirement that the resultant attribution must conform to the principles embodied in Article 7.

16.3.3. A further aspect which merits consideration is the language employed in Article 7(5) provides that, in determining the profits of a Permanent Establishment, deductions in respect of expenses incurred for the purposes of the Permanent Establishment, including executive and general administrative expenses incurred either in the State where the Permanent Establishment is situated or elsewhere, shall be allowed *"in accordance with the provisions of and subject to the limitations of the taxation laws of that State."* Thus, while the Treaty recognises the deductibility of executive and general administrative expenditure incurred outside India, it simultaneously subjects such deduction to the provisions and limitations contained in the domestic law of the source State. Section 44C, being a special



computation provision regulate the allowability of head office expenditure incurred outside India, therefore constitutes one such domestic limitation contemplated by Article 7(5). This, read conjointly with Article 7(4), preserves the customary domestic method of attributing profits to a Permanent Establishment, indicates that the Treaty itself envisages the application of domestic computational rules in determining the profits attributable to a Permanent Establishment.

16.3.4. Thus, in our view, the Treaty itself expressly preserves the domestic attribution mechanism customarily followed by the Contracting State. The significance of Article 7(4) lies in recognising that the process of attributing profits to a PE is not divorced from domestic computational provisions, but rather permits the application of such domestic mechanisms, so long as the resultant attribution accords with the principles governing Article 7.

16.4 In the Income Tax Act, Section 44C forms part of domestic computation machinery. The provision is not a charging section but a special computation provision enacted to regulate the deduction of executive and general administrative expenditure incurred outside India by the Head Office of a non-resident enterprise. In order to understand the computation mechanism under section 44C, it is necessary to understand to what extent the provision is applicable. The relevant provision is thus reproduced as under:

Section 44C – Deduction of head office expenditure in the case of non-residents

44C. *Notwithstanding anything to the contrary contained in sections 28 to 43A, in the case of an assessee, being a non-resident, no allowance shall be made in computing the income chargeable under the head "Profits and gains of business or profession", in respect of so much of the*



expenditure in the nature of head office expenditure as is in excess of the lower of—

- (a) an amount equal to five per cent of the adjusted total income; or*
- (b) the amount of so much of the expenditure in the nature of head office expenditure incurred by the assessee as is attributable to the business or profession of the assessee in India.*

Explanation.— *For the purposes of this section,—*

(i) "adjusted total income" means the total income computed under this Act, without giving effect to the allowance referred to in this section or in section 32AB or section 33AB or the deduction referred to in Chapter VI-A or the deduction under section 35D, and as increased by the aggregate amount of the depreciation allowance, investment allowance, development rebate, development allowance, expenditure on scientific research and expenditure on family planning, to the extent deducted in computing the business income;

(ii) "head office expenditure" means executive and general administration expenditure incurred by the assessee outside India, including expenditure incurred in respect of—

(a) rent, rates, taxes, repairs or insurance of any premises outside India used for the purposes of the business or profession;

(b) salary, wages, annuity, pension, fees, bonus, commission, gratuity, perquisites or profits in lieu of or in addition to salary, whether paid or allowed to any employee or other person employed in, or managing the affairs of, any office outside India;

(c) travelling by any employee or other person employed in, or managing the affairs of, any office outside India; and

(d) such other matters connected with executive and general administration as may be prescribed.

16.4.1. A careful reading of section 44C would show that it is a special computation provision, introduced with a non obstante clause, overriding provisions of sections 28 to 43A of the Act. The legislative intent thus carves out distinct mechanism for determination of admissible deduction in respect of head office expenditure incurred by non-resident enterprises. It is important to also note that, the provision does not altogether disallow such expenditure, but merely places statutory ceiling on the quantum of deduction allowable. The restriction, however, is confined only to "head office expenditure", which has been specifically defined in the Explanation to mean executive and general administrative expenditure incurred by the assessee outside India. The definition



being inclusive in nature, as evident from the use of the expression "including", is of wide amplitude and encompasses not only common executive and administrative expenditure incurred by the foreign Head Office and allocated amongst its various PE, but also expenditure incurred outside India exclusively for the benefit of the Indian PE, provided such expenditure retains the character of executive and general administrative expenditure.

16.4.2. Thus, the legislative focus of section 44C is not on the place where the benefit of the expenditure is ultimately derived, but on the nature of the expenditure and the fact that it represents executive and general administrative expenditure incurred outside India by the Head Office of a non-resident enterprise.

16.5. Having regard to the very nature of the expenditure governed by section 44C, we are unable to accept the broad proposition advanced by the Ld.Sr.Counsel that, the provision is inherently discriminatory merely because it applies only to non-resident enterprises. The expenditure contemplated by section 44C represents executive and general administrative expenditure of a foreign Head Office situated outside India, which may either be commonly allocated amongst different PE or incurred outside India for the benefit of a particular PE. Such a category of expenditure is peculiar to enterprises having their Head Office outside India and ordinarily does not arise in the case of a resident Indian enterprise. The distinction drawn by Parliament is, therefore, founded upon the peculiar nature of the expenditure sought to be regulated and the attribution exercise contemplated under Article 7, and not merely upon the residential status of the assessee. To that extent, the legislative classification recognised by section 44C stands



reinforced by the attribution mechanism preserved under Article 7(4) of the India–UK DTAA and by the ratio laid down by the *Hon'ble Supreme Court* in *American Express Bank Ltd.*(supra)

16.6 At the same time, the above conclusion does not render Article 26(2) of the India–UK DTAA otiose. In order to understand the whether Article 26 of the India UK treaty would apply, the relevant portion is reproduced as under:

Article 26 – Non-discrimination

1. *The nationals of a Contracting State shall not be subjected in the other Contracting State to any taxation or any requirement connected therewith which is other or more burdensome than the taxation and connected requirements to which nationals of that other State in the same circumstances are or may be subjected.*

2. *The taxation on a permanent establishment which an enterprise of a Contracting State has in the other Contracting State shall not be less favourably levied in that other State than the taxation levied on enterprises of that other State carrying on the same activities in the same circumstances or under the same conditions. **This provision shall not be construed as preventing a Contracting State from charging the profits of a permanent establishment which an enterprise of the other Contracting State has in the first-mentioned State at a rate of tax which is higher than that imposed on the profits of a similar enterprise of the first-mentioned Contracting State, nor as being in conflict with the provisions of paragraph (4) of Article 7 of this Convention.***

.....

16.6.1. This language is unique to the India–UK DTAA and assumes great significance because it expressly recognizes that the non-discrimination clause is not intended to override the attribution mechanism preserved by Article 7(4). A harmonious reading of Articles 7 and 26 of the India–UK DTAA would indicate that the Convention itself preserves the customary domestic methodology for attributing profits to a PE. While Article 7(2) lays down the substantive principle of treating the PE as a distinct and separate enterprise, Article 7(4) expressly permits the Contracting



State to determine the profits attributable to the PE by applying its customary domestic method of apportionment, provided that the result accords with the principles contained in Article 7.

16.7. It is in this backdrop that section 44C, being a special domestic computation provision that governs attribution and allowability of head office expenditure incurred outside India, assumes relevance. Merely because the provision applies to non-resident enterprises, it cannot, by itself, be regarded as inherently discriminatory so as to offend Article 26(2) of the India–UK DTAA, particularly when Article 26(2) itself clarifies that the non-discrimination provision shall not be construed as being in conflict with paragraph (4) of Article 7. At the same time, this does not imply that Article 26(2) is rendered otiose.

16.7.1. Whether the application of section 44C, in a given case, results in less favorable taxation of a PE, vis-à-vis a similarly placed resident enterprise would necessarily depend upon the nature and character of the expenditure sought to be subjected to the statutory limitation and the factual application of the provision. The non-discrimination provision under Article 26, thus has to be read harmoniously with Article 7. The Treaty itself does not contemplate that every distinction arising in the attribution or computation of profits of a PE would amount to discrimination. On the contrary, Article 7(4) recognises the continued application of domestic attribution mechanisms, whereas Article 26(2) ensures that such mechanisms are not applied in a manner resulting in prohibited discriminatory taxation. Therefore, the applicability of Article 26(2) cannot be examined in the abstract but necessarily



depends on the nature of the expenditure subjected to the restriction and the factual matrix of each case.

16.8. We have also carefully considered the decisions relied upon by the Ld.Sr.Counsel, particularly the decisions of the co-ordinate Benches in *Metchem Canada Inc. v. DCIT (supra)* and *Rolls Royce Plc. v. DCIT(supra)*, wherein it was held that the restriction contained in section 44C could not be applied in view of the non-discrimination clause contained in the applicable DTAA. Those decisions undoubtedly recognize the overriding effect of treaty provisions where a domestic law provision results in prohibited discrimination. However, in our considered opinion, the said decisions cannot be construed as laying down an inflexible proposition that section 44C is rendered inapplicable in every case involving a PE of a non-resident enterprise. Neither of the decisions undertook examination of the scope and effect of Article 7(4) of the India-UK DTAA, which expressly preserves the customary domestic methodology for attribution of profits to a PE, nor did they analyse the significance of the concluding portion of Article 26(2), which specifically provides that the non-discrimination clause shall not be construed as being in conflict with paragraph (4) of Article 7. Further, the issue is now required to be appreciated in the light of the law subsequently declared by the *Hon'ble Supreme Court* in *American Express Bank Ltd.(supra)*, which recognizes section 44C as a special computation provision governing the deduction of head office expenditure. Accordingly, while respectfully agreeing with the principle that Article 26 may override a domestic provision where actual discriminatory taxation is established, we are of the considered view that the applicability of



Article 26(2) of India UK DTAA in relation to section 44C cannot be decided in the abstract, but must necessarily depend on the nature of the expenditure claimed and the factual application of the statutory provision in the light of the scheme of Articles 7 and 26 of the India–UK DTAA.

16.9. We are, therefore, of the considered opinion that section 44C cannot, as a proposition of law, be held to be discriminatory in every case merely because it applies only to non-resident enterprises. Equally, it cannot be held that Article 26(2) can never have any application to the operation of section 44C. If the expenditure represents common executive and general administrative overheads of the foreign Head Office forming part of the attribution mechanism recognised under Article 7, the application of section 44C would ordinarily be consistent with the scheme of the Treaty.

16.10. In the present case, however, we find that neither the assessment order nor the orders of the lower authorities identify the precise constituents of the expenditure claimed under section 44C. There is no finding as to whether the expenditure comprises common executive and general administrative overheads of the foreign Head Office, expenditure allocated amongst various PE, or expenditure incurred exclusively outside India for the benefit of the Indian PE. In the absence of such foundational facts, it is not possible to determine the precise scope of section 44C or to examine whether, in its application to the facts of the present case, any issue of less favourable taxation within the meaning of Article 26(2) of the India–UK DTAA actually arises.



16.11 In these circumstances, we consider it appropriate to set aside the impugned order on this issue and restore the matter to the file of the Ld.AO. The Ld.AO shall identify and classify the various items comprising the claim of head office expenditure with reference to the definition contained in the Explanation to section 44C and determine whether they constitute common executive and general administrative expenditure of the foreign Head Office, expenditure allocated amongst various PE, or expenditure incurred outside India exclusively for the benefit of the Indian PE. Upon such factual determination, the Ld.AO shall re-examine the allowability of the claim in accordance with the principles laid down by the *Hon'ble Supreme Court* in *American Express Bank Ltd.(supra)* and thereafter consider, wherever factually warranted, the assessee's contention regarding the applicability of Article 26(2) of the India-UK DTAA, after harmoniously construing Articles 7 and 26 in the light of the accepted principles of treaty interpretation. Needless to say that, the assessee shall be afforded adequate opportunity of being heard and of producing such material as may be considered necessary in support of its claim.

Accordingly, this ground raised by the revenue stands partly allowed for statistical purposes.

17. Ground No. 13-14, are in respect of taxability of interest on Income-tax refund of Rs. 49,17,15,498/-.

17.1. Brief background of this issue as submitted by the Ld.Sr.Counsel is that, the assessee received income-tax refund against order giving effect of appeals passed by the Ld.CIT(A) for A.Ys 1994-95, 1995-96, 1997-98 and 2001-02. The interest on



these refunds were included in the P&L Account for AY 2004-05 and the same was offered to tax @ 41%. The Ld.Sr.Counsel submitted that the said interest are subject matter of further revision based on further orders to be passed in the appeal pending before *Hon'ble High Court* and this *Tribunal*, details of which are as under:-

Sr. No.	Assessment Years	Interest Amount (in INR)	Pending at
1	AY 1994-95	13,18,59,323	No Appeal
2	AY 1995-96	96,097	Hon'ble Bombay HC
3	AY 1997-98 (withdrawn)	(3,75,41,847)	Hon'ble Bombay HC
4	AY 2001-02	39,73,01,925	Hon'ble Mumbai ITAT
	TOTAL	49,17,15,498	

17.2. It was submitted that the above fact was duly disclosed as a part of notes to retuned income filed by assessee. The Ld.Sr. Counsel thus submitted that the interest income ought to be excluded from the taxable income and should be taxed if only necessary, when the issue of income tax refund reaches finality.

17.3. He submitted that this issue was raised before Ld.CIT(A) for the first time by way of an additional ground and the Ld.CIT(A) decided the same by observing as under:-

“14.4 Decision of Additional Ground No. 2:

I have considered the submission of the Appellant. The issue is covered in the favor of the Appellant by Hon'ble ITAT order for past AYs in Appellant's own case. Respectfully, following the Hon'ble ITAT order in Appellant's own case, I direct the AO, after necessary verification, to tax the interest in current AY at the rate of 10 per cent as per Article 12 of India-UK Tax Treaty. Accordingly, this ground of appeal is allowed for statistical purpose.”

17.4. The Ld.Sr.Counsel submitted that, for the previous assessment year i.e., A.Y. 2003-04, the Ld.CIT(A) decided the issue



based on the decision of *Hon'ble Bombay High court* in case of *Credit Agricole Corporate & Investment Bank Indosuez* reported in [2015] 377 ITR 102 and the decision of *Hon'ble Special Bench of Delhi Tribunal* in case of *ACIT vs. Clough Engineering* reported in [2011] 11 taxmann.com 70. The Ld.Sr.Counsel submitted that for A.Y. 2003-04 the CIT(A) directed to tax the income tax refund @10% in accordance with the provisions of Article 12 of the treaty because the interest on income tax refund cannot be said to be effectively connected to the Indian Branch/PE of the assessee.

17.5. The Ld.Sr. Counsel thus, submitted that, the Ld.AO may be directed to tax the interest on income tax refund once it reaches finality and not in the year under consideration.

17.6. On the contrary the Ld.DR relied on the order passed by the Ld.AO.

We have perused the submissions advanced by both sides in light of the records placed before us.

18. It is noted that in respect of taxability of interest on refund at 10% under Article 12 of the Treaty has been accepted by the revenue as no further appeal has been filed on this aspect before the *Hon'ble High Court* in any of the preceding AYs.

18.1. Insofar as the taxability for the interest on refund during the year under consideration is concerned as the appeals against the order passed for preceding AYs are pending at various stages of *Hon'ble High Court* as well as this *Tribunal*, such amount has not attained finality. We, therefore, do not find any infirmity in the view



taken by the Ld.CIT(A). in the view taken hereinabove and the same is accordingly upheld.

Accordingly, Ground Nos. 13 & 14 raised by the revenue stands dismissed.

Now, we take up the Assessee's Appeal:

19. It is submitted that **Ground No. 1** raised by assessee is general in nature and, therefore, does not required any adjudication.

19.1. Ground No. 2 raised by assessee, is in respect of applicability of Transfer Pricing provisions to the transactions between and associate enterprise and its permanent establishment in India. At the outset, both sides submitted that the issue is now decided against assessee by an order of Hon'ble Special Bench of Ahmedabad Tribunal in case of *M/s TBEA Shenyang Transformed Group Company Limited vs. DCIT* reported in 169 taxmann.com 145. We, therefore, do not find any merit in the ground raised by assessee and the same is dismissed.

19.2. The Ld.Sr.Counsel submitted that **Ground No. 1 of the Revenue's appeal and Ground Nos. 3, 4 and 5 of the assessee's appeal** pertain to the expenditure in respect of which the Ld. TPO had partly accepted the ALP. He submitted that, notwithstanding the acceptance of the ALP by the Ld. TPO to that extent, the Ld. AO disallowed the said expenditure on the ground that the assessee had failed to furnish books of account, agreements, vouchers, invoices and other supporting documents. Accordingly, the assessee has challenged the disallowance made by the Ld. AO in



respect of the expenditure which had already been accepted by the Ld. TPO to be at arm's length. The assessee has also raised grounds challenging the determination of the ALP at Nil by the Ld. TPO in respect of the balance expenditure. On the other hand, the Revenue is in appeal against the relief granted by the Ld. CIT(A) in respect of that portion of the expenditure which had been accepted by the Ld. TPO as being at arm's length.

19.2.1. The brief facts leading to the present issue are that the assessee, in its return of income, claimed deduction of direct expenses amounting to Rs.85,18,87,800/-. During the course of assessment proceedings, a reference under section 92CA of the Act was made to the Ld.TPO for determination of the ALP of the international transactions relating to the said expenditure. During the transfer pricing proceedings, the Ld.TPO called upon the assessee to furnish details regarding the nature of the expenditure, the benefits derived therefrom, and supporting evidence under the various heads under which the costs had been allocated. In response, the assessee, vide letter dated 07/09/2006, furnished details regarding the nature of the costs incurred and the benefits derived therefrom. The assessee also produced documentary evidence demonstrating the receipt of benefits in respect of the majority of the costs allocated, aggregating to Rs.51.95 crore, under various heads. After examining the material placed on record, the Ld. TPO, vide order passed under section 92CA(3) of the Act dated 13.10.2006, accepted the ALP in respect of expenditure amounting to Rs.51.95 crore. However, in respect of the balance expenditure of Rs.33.24 crore, the Ld.TPO determined the ALP at



Nil, observing that the assessee had failed to discharge the onus of substantiating the arm's length nature of the said expenditure.

19.2.2. Upon receipt of the order passed by the Ld.TPO under section 92CA(3) of the Act, the Ld.AO, notwithstanding the acceptance of the ALP by the Ld.TPO in respect of expenditure amounting to Rs.51.95 crore, disallowed the said expenditure under section 37 of the Act on the ground that the assessee had failed to substantiate the claim by furnishing the books of account of the Head Office, details regarding the place where such expenditure was incurred, vouchers, invoices and other supporting documents. While making the aforesaid disallowance, the Ld.AO placed reliance upon the decision of the *Co-ordinate Bench of the Tribunal* in *Micoperi S.P.A. Milano v. DCIT*, reported in 82 ITD 369.

19.2.3. In so far as the balance direct expenditure amounting to Rs.33.24 crore was concerned, the Ld.AO accepted the findings recorded by the Ld.TPO in the order passed under section 92CA(3) of the Act and, accordingly, held that the ALP of the said expenditure was Nil.

19.3. On an appeal before Ld.CIT(A), the Ld.CIT(A) observed and held as under:-

“5.4 Decision on Ground 1

5.4.1 I have gone through the issue and the Appellant’s submission. It is an undisputed fact that these expenses are incurred by the HO and offshore co-branches for the benefit of the India operations and therefore allocated to India.

5.4.2 The Appellant had explained the transaction and submitted details under various heads for the total costs of INR 85.19 crs. However, the Appellant submitted evidences for 61 percent (i.e., INR 51.95 crs) of the total costs on a representative sample basis before the TPO for the above costs. The TPO post verification of these details accepted 61 percent of the



total costs (i.e., INR 51.95 crs) to be at arm's length and determined the arm's length price for the balance costs (i.e., INR 33.24 crs) to be NIL. The only issue with regard to transfer pricing is the non-submission of the details for the entire (i.e., 100 percent) costs.

5.4.3 I have also perused the Hon'ble ITAT's Order for AY 2002-03 and AY 2003-04 in Appellant's own case. The Hon'ble ITAT, in its order dated 15 March 2024 for AY 2002-03 and AY 2003-04, while principally adjudicating the issue in favor of the Appellant by following the coordinate bench ruling in the case of Jabil Circuit India Private Limited Vs. Asst. CIT, Circle 3(2)(1) [TS-1274-ITAT-2018Mum-TP] against the adhoc transfer pricing adjustment, directed the AO to verify the Certified Public Accountant ('CPA') certificate, allocation keys, and relevant cost allocation to the Indian entity in relation to the Direct costs. Further, the Hon'ble ITAT had allowed the Appellant's ground under Section 37(1) of the Act and also deleted the disallowance under Section 40(a)(i) of the Act, by following the ruling of co-ordinate bench of the Hon'ble ITAT in Appellant's own case for AY 1999-00 and 2001-02 which relates to the same Direct costs. The relevant extract from the Hon'ble ITAT's order for AY 2002-03 and AY 2003-04 is reproduced below:

"56. It was held that the intra group services should have provided and such services must be at Arm's Length Price. As per OECD, allocation of cost based on approved allocation key and certified by the CPA certificate is relevant. The revenue cannot reject the CPA certificate since the same are specific and authenticated. As per Rule 10D(2)(A), the document must be supported by authentic documents, which includes authentication by the CPA. Therefore, the certification of allocation key and the same was authenticated by the CPA is proper documents as per Rule 10(2)(A) of the I.T. Rules. Respectfully following the above decision, we observe that in the given case also, the assessee has provided informations under Rule 10D(2)(A) and the cost allocation was also certified by the statutory auditors (CPA) of the Head Office and the service branches are submitted before tax authorities. However, this was not taken cognizance by the tax authorities. Therefore, we direct the Assessing Officer to verify the CPA certificate and verify the allocation key and relevant allocation of the cost to the Indian entity. Therefore, we rely on the above decision and findings of the Coordinate Bench in assessee's own case, we are inclined to allow the Ground No. 2 raised by the assessee with the above direction"

5.4.4 The Appellant thereafter filed a Miscellaneous Application ('MA') against the said remand with directions for verification. The Hon'ble ITAT vide its MA order dated 16 December 2024 rejected the Appellant's plea citing that the formation of a view that an issue should be remanded back to the file of the authorities below cannot constitute a mistake apparent on record in the facts and circumstances of the present case. However, the remand of the issue back to the file of the authorities below can, at best, constitute an error of judgment which may be subjected to judicial



review in appellate proceedings under Section 260A of the Act. The relevant extract is reproduced below:

“In the facts of the present case, the remand of the issue back to the file of the authorities below can, at best, constitute error of judgment (and not mistake apparent on record as contended by the Assessee) which may be subjected to judicial review in appellate proceedings under Section 260A of the Act and the same does not fall within the ambit of powers vested in the Tribunal under Section 254(2) of the Act to rectify the mistake apparent on record.”

5.4.5 In view of the above judgment, the Appellant had filed a written submission vide letter dated 24 March 2025 submitting that it has explained the entire transaction and submitted evidence on a representative sample basis for approx. 61 percent of the total costs. Further, the Appellant submitted that it does not have any incremental documents to furnish in relation to the Direct Costs for the year under consideration. Given that the Appellant does not have any incremental document to submit, the issue is being decided based on the material available on record, the Hon'ble ITAT order for AY 2002-03 and AY 2003-04 in the Appellant's own case, and the coordinate bench ruling in case of Jabil Circuit India Private Limited Vs. Asst. CIT, (Supra).

5.4.6 It is a well-settled position in law that the primary onus to substantiate the arm's length price of a transaction along with the prescribed / relevant documents is of the Assessee. In the present case, since no details have been submitted by the Appellant to substantiate the arm's length price for the balance costs, I affirm the findings of the TPO to determine the arm's length price for the balance costs of INR 33.24 crs to be NIL.

5.4.7 Further, as discussed above, I observe that the Hon'ble ITAT in past AYs in Appellant own case has allowed the deduction under Section 37(1) of the Act as the expenditure are incurred for the Appellant. The Hon'ble ITAT in AYs 2001-02, 2002-03, 2003-04 has held that the provision of Section 40(a)(i) of the Act is not applicable as the direct cost expenses represents transaction with self (as no one can make profit / income out of self) and also held that direct expenses are not in nature of royalty / FTS in the hands of HO and hence no disallowance can be made under Section 40(a)(i) of the Act. Further, in AY2000-01 the Hon'ble CIT(A) held that direct expenses are not in the nature of royalty, and no appeal was preferred by the Department before Hon'ble ITAT. Respectfully, following the Hon'ble ITAT orders in Appellant's own case, I direct the AO to allow the deduction of direct cost expense after necessary verification. Accordingly, Ground no. 1 is allowed for statistical purpose.”

Aggrieved by the order of Ld.CIT(A), both revenue as well as assessee are in appeal before this Tribunal.



20. At the outset, the Ld.Sr.Counsel submitted that the challenge raised by the Revenue pertains to direct expenses amounting to Rs.114,91,20,000/-. He submitted that the assessee had, in fact, claimed deduction of only Rs. 85.19 crore in its return of income, whereas the balance amount of Rs.29.72 crore was never claimed as a deduction nor was it the subject matter of appeal before the Ld.CIT(A). The Ld.Sr.Counsel further submitted that the said amount of Rs.29.72 crore had been disallowed by the Ld.AO under section 40(a)(i) of the Act on the ground that the assessee had failed to deduct tax at source under section 195, treating the payment as royalty. While making the said disallowance, the Ld.AO placed reliance on the following decisions:—

Gleeson vs. Demee, 1975 (RPC 471);
E.P. W. Da Costa vs. Union of India (1980) (121 ITR 751) (Del);
CIT vs. Travel Corporation of India Ltd (209 ITR 555) (Bom);
Dampass Industries P. Ltd (2004) (268 ITR 1) (AAR)

20.1. The Ld.Sr.Counsel further submitted that, insofar as the verification of the direct costs under section 37 of the Act is concerned, the same has become academic in view of the order of the Ld.CIT(A), who has allowed the deduction to the extent the ALP of the expenditure has been accepted by the Ld.TPO. He, therefore, submitted that the issues arising for consideration before this Tribunal, as raised by both the assessee and the Revenue, may be bifurcated in the following manner:—

Amount of direct expenses (INR)	Actions of the learned TPO	Actions of the learned AO
51.95 Cr	Accepted the ALP to the extent of INR 51.95 Cr.	i) Disallowed the expenses stating that the Appellant has not furnished books of accounts of the HO, original voucher supporting such expenses etc. ii) Treated direct expense as royalty and consequently disallowed the same due to non-deduction of tax at source.



Amount of direct expenses (INR)	Actions of the learned TPO	Actions of the learned AO
33.24 Cr	<i>ALP is treated as "NIL" in respect of expense of INR 33.24 Cr on citing non-submission of the details</i>	<i>i) Learned AO accepted the finding of learned TPO. ii) Treated direct expense as royalty and consequently disallowed the same due to non-deduction of tax at source.</i>

20.2. The Ld.Sr.Counsel submitted that the adjustment made by the Ld. TPO to the extent of Rs. 33.24 crore ignores the fact that the assessee had furnished an independent auditor's certificate in support of the allocation of the said expenditure, along with various documents evidencing the receipt of services and the benefits derived therefrom, thereby substantiating the arm's length nature of the direct costs. He submitted that the Ld.TPO erred in determining the ALP of the said expenditure at Nil, as the expenses were specifically attributable to the assessee's operations in India and had been allocated on a reasonable and scientific basis. It was further submitted that India is of strategic importance to the Group, being an emerging market where the financial services industry is undergoing significant transformation. According to the Ld.Sr.Counsel, enhanced system capabilities are essential to enable the Indian Permanent Establishment to augment its income streams in the face of increasing competition and substantial investments made by competitors in advanced banking technology. The Ld.Sr.Counsel further submitted that, against the direct costs of Rs.85.18 crore claimed by the assessee, the gross revenue earned by the assessee during the relevant assessment year amounted to Rs.3,223 crore, and, therefore, the direct costs constituted only 2.63% of the gross revenue. He also furnished the following broad break-up of the direct costs incurred by the assessee in India.



Particulars	Amount
Reallocation Details	
1. Hongkong IS & T	173,120
2. Singapore India Metros / IS & T	436,460
Total IS & T costs (1+2)	609,581
3. Global Technology costs	156,602
4. Corporate & Institutional Banking (Global Account Managers)	64,877
5. Group Taxation	20,828
TOTAL	851,888

20.3. The Ld.Sr.Counsel submitted that the assessee had substantiated the impugned expenditure by furnishing contemporaneous documentation establishing the need for the services and the benefits derived therefrom. However, in respect of certain portions of the expenditure under the aforesaid heads, for which complete supporting details could not be furnished, the Ld.TPO determined the ALP at Nil. It was submitted that the assessee had furnished documentary evidence in respect of approximately 61% of the total costs to demonstrate the benefits derived by its Indian operations under the various heads of expenditure. The Ld.Sr.Counsel placed reliance on the independent auditor's certificate dated 31/12/2003, which has not been disputed by the Revenue authorities, certifying that the allocation keys adopted were in accordance with the allocation policy consistently followed by the Bank in the preceding years. He also relied upon the order of the *Co-ordinate Bench of this Tribunal for Assessment Year 2002-03 in ITA Nos. 1407 & 2936/Mum/2019, vide order dated 15.03.2024*. The Ld.Sr.Counsel emphasized that the expenditure, which had been partly accepted by the Ld.TPO, primarily represented technology costs incurred for the Indian operations of the assessee and did not partake the character of



Head Office expenditure. He, therefore, submitted that the provisions of section 44C of the Act were inapplicable, as the primary condition for invoking the said provision, namely that the expenditure should have been incurred outside India by the Head Office, was not satisfied. Accordingly, it was contended that the balance expenditure, allocated to the Indian operations on the basis of certified and consistently applied allocation keys, could not be disallowed merely on the basis of conjectures and surmises.

20.4. The Ld.Sr.Counsel submitted that the portion of the expenditure accepted by the Ld.TPO had nevertheless been disallowed by the Ld.AO on two distinct grounds, namely, under section 37(1) of the Act and under section 40(a)(i) of the Act for alleged non-deduction of tax at source under section 195. He submitted that, insofar as the disallowance made under section 37(1) is concerned, the same has already been deleted by the Ld.CIT(A), who held that the expenditure constituted direct business expenditure incurred wholly and exclusively for the purposes of the assessee's business. In support of the said contention, the Ld.Sr.Counsel placed reliance upon various *orders of Co-ordinate Benches of this Tribunal rendered in the assessee's own case for the preceding assessment years*, wherein the said expenditure has consistently been held to be allowable under section 37(1) of the Act. He further submitted that the impugned payments did not involve the make available of any technical knowledge, experience, skill, know-how or processes to the assessee and, therefore, could not be characterised as fees for technical services. Consequently, it was contended that the provisions of section 40(a)(i) of the Act were not attracted. In



support of this proposition, reliance was placed on the *order of the Co-ordinate Bench of this Tribunal in the assessee's own case for Assessment Year 2000-01 in ITA No. 3458/Mum/2009, vide order dated 13.11.2023.*

20.5. On the contrary, the Ld.DR relied on the orders passed by the authorities below.

We have perused the submissions advanced by both sides in light of the records placed before us.

21. It is noted that the expenditure claimed by the assessee, amounting to Rs. 85.19 crore, represents direct costs allocated to the Indian operations based on scientifically determined and consistently applied allocation keys. The expenditure comprises, inter alia, consumer and corporate banking information system and technology costs, group technology costs, global account managers' costs and group taxation costs. It is further evident from the material placed on record that these expenditures were incurred wholly and exclusively for the purposes of the assessee's business and that the assessee derived tangible business benefits therefrom.

21.1. As regards the applicability of Article 13 of the India-UK DTAA, we find that expenditure such as global account managers' costs and group taxation costs pertains to the day-to-day business operations of the assessee and represents routine managerial and administrative support. By no stretch of imagination can such payments be characterised as fees for technical services. Insofar as the expenditure towards Hong Kong/Singapore information system and technology costs and group technology costs is concerned,



there is nothing on record to suggest that any copyright, process, patent or other rights contemplated under section 9(1)(vi) read with Explanation 2 thereto were transferred to the assessee. Likewise, the Revenue has failed to establish that any technical knowledge, experience, skill, know-how or processes were made available to the assessee so as to attract Article 13 of the India–UK DTAA. In the absence of satisfaction of the "make available" condition, the impugned payments cannot be brought within the ambit of fees for technical services under the Treaty. Our aforesaid view is fortified by the decisions of the *Hon'ble Supreme Court* in *Engineering Analysis Centre of Excellence (P.) Ltd . vs. CIT* reported in (2021) and decision of *Hon'ble Karnataka High Court* in case of *CIT v. De Beers India Minerals Pvt. Ltd.* reported in (2012) 21 taxmann.com 214.

21.2. In view of the foregoing discussion, we hold that the impugned expenditure constitutes allowable business expenditure incurred wholly and exclusively for the purposes of the assessee's business. We further hold that the payments are neither in the nature of royalty nor fees for technical services either under the provisions of the Act or under Article 13 of the India–UK DTAA. Consequently, no disallowance under section 40(a)(i) of the Act is warranted. Likewise, we find no justification for determining the Arm's Length Price of the impugned expenditure at Nil, particularly when the expenditure stands supported by documentary evidence, certified allocation keys and demonstrable business benefits. Accordingly, the additions/disallowances made by the Ld. AO/TPO under the domestic provisions as well as the transfer pricing provisions of the Act are directed to be deleted.



Accordingly Ground No. 1 raised by revenue stands dismissed and ground no. 3, 4 & 5 raised by assessee stands allowed.

22. Ground No.6 raised by assessee is in respect of the refurbishment expenses of Rs. 2,50,28,427/- treated as capital in nature.

The brief facts, as submitted by the Ld. Sr. Counsel, are that the assessee incurred expenditure amounting to Rs. 2,50,28,427/- towards renovation of its various leasehold premises. It was submitted that the expenditure was incurred mainly on interior works, electrical works, cabling and wiring, ducting, carpets, access control systems, travelling expenses, architects' fees and other allied items. According to the Ld. Sr. Counsel, these expenses were incurred solely for the purpose of making the leased premises suitable for carrying on the assessee's business operations.

22.1. The Ld. Sr. Counsel submitted that the Ld.AO disallowed the aforesaid expenditure by treating it as capital in nature on the ground that it resulted in the creation of assets of an enduring nature. It was submitted that similar expenditure had been incurred by the assessee in the preceding assessment years. In those years, the Ld.CIT(A) allowed 75% of the expenditure as revenue in nature, while directing that the remaining 25% be treated as capital expenditure, on which depreciation was allowed.

22.2. The Ld.Sr.Counsel further submitted that the assessee carried the matter in appeal before the *Co-ordinate Bench of this Tribunal*, which allowed the assessee's claim by holding that the improvements made to the leasehold premises did not result in the creation of any capital asset belonging to the assessee, since the



assessee was merely a lessee of the premises. He submitted that this *Tribunal*, while deciding identical issue in earlier assessment years, took note of the fact that no enduring advantage accrued to the assessee in the capital field by incurring the said expenditure and that the expenditure had been incurred wholly and exclusively for the purpose of making the leased premises suitable for carrying on its business and for providing an appropriate working environment to its employees. In support of the aforesaid contention, reliance was placed on the *order of the Co-ordinate Bench of this Tribunal in the assessee's own case for Assessment Year 2002-03 in ITA Nos. 1407 & 2936/Mum/2019, vide order dated 15/03/2024*, wherein the Tribunal followed its earlier *order for Assessment Year 2001-02 in ITA No. 4867/Mum/2017, dated 13/11/2023*.

22.3. On the contrary the Ld.DR relied on the orders passed by authorities below.

We have perused the submissions advanced by both sides in light of the record placed before us.

24. It is noted that this Tribunal *Tribunal in the assessee's own case for Assessment Year 2002-03(supra)* observed and held as under:

“23. Considered the submissions and material placed on record, we observe from the record that identical issue is decided in favour of the assessee for the A.Y. 2001-02. While deciding the issue, the Coordinate Bench ITA.No. 4867/Mum/2017 dated 13.11.2023 held as under: -

“Ground No. 4: Expenditure on refurbishment of premises

4.1 Ground



4.1 The learned CIT (A) erred in law and on facts to disallow 25% of the expenditure incurred on refurbishment of leasehold premises as capital in nature.

4.2 The learned CIT (A) ought to have allowed the said expenditure as revenue in nature and accordingly disallowance should be deleted.

.....

The Appellant submits that this issue is covered in favor of the Appellant by the decision of the Co-ordinate bench of the Tribunal in the Appellant's own case for the assessment year 1999-2000, wherein the Tribunal following the decision of Hon'ble Supreme Court in the case of Madras Auto Service Pvt. Ltd. [233 ITR 468] (Copy of decision is enclosed in the Bank's legal paper book at page 336) allowed the deduction for the entire refurbishment expenses (Copy of A.Y. 1999-00 ITAT order is enclosed in the Bank's legal paper book -refer page 157, para 13 and 14) which reads as under:

"13. Considered the rival submissions and material placed on record, we observed that Hon'ble Supreme Court in the case of Madras Auto Services Pvt. Ltd., (supra) on similar issue adjudicated in favour of the assessee. While holding so Hon'ble Supreme Court held as under: -

'The assessee is a limited company carrying on the business of sale of motor parts. Its head-office is at Madras. It has a branch at Bangalore. Under an agreement of lease dated 1st of February, 1966, the assessee obtained from M/s. Hajira Comer and Mrs. Rabia Bai Razack a lease of premises Nos. 64 and 64/1 situated at Sri Narasimharaja Road, Bangalore for a period of 39 years commencing from 1st of January, 1966. Under the terms and conditions of the lease, the lessee (that is to say the assessee), had the right to demolish at its own expense the existing premises and appropriate to itself all the material thereof without paying to the lessors any compensation and construct a new building thereon to suit the purpose of their business as per the plan approved by the lessors. Under Clause 2 of the lease deed, the lessee was required to pay a rent of Rs. 1000/- per month for the first fifteen years, Rs. 1500/- per month for the next ten years, Rs. 1650/- per month for the next ten years and Rs. 2000/- per month for the remaining years. The lease deed further provided that the new construction shall, right from the commencement of the work, be the property of the lessors; and upon completion of the work of construction the lessee will have only the right to be a tenant for a period of 39 years under the existing lease subject to the payment of rent and observation of other terms and conditions of the lease. The lessee shall not be entitled under any circumstances for any compensation whatsoever on account of its putting up the new construction in the place of the old.



Acting under the lease agreement the assessee invested a sum of Rs. 1, 62, 835/- in the previous year relevant to the assessment year 1968/69 and Rs. 50, 937/- during the succeeding year in constructing a new building on the said land. The assessee claimed before the Income-tax Officer the expenditure of the said sums of Rs. 1, 62,835/- and Rs. 50, 937/- in the relevant assessment year as capital loss. In the alternative, the assessee claimed depreciation on capital investment; in the alternative, the assessee claimed deduction of the payments as business expenditure or as extra rent for the lease. Ultimately, the Income-tax Tribunal has held that the expenditure of the said two amounts for the construction of a new building is in the nature of business expenditure for proper carrying on of the business of the assessee. The Tribunal has, therefore, treated these amounts as revenue expenditure and allowed a deduction in that regard to the assessee. The claim of the department that the expenditure was capital expenditure and was, therefore, not deductible was negated by the Tribunal.

On the application of the department the Tribunal referred the following question to the High Court for its determination under Section 256(1) of the Income-tax Act, 1961:

‘Whether on the fact and in the circumstances of the case the Appellate Tribunal was right in holding that the building expenses of Rs. 1,62,835/- are not liable to be taken into account as deductible expenditure in arriving at the real income of the assessee for the assessment year 1968-69?’

For the next assessment year, a similar question was raised in regard to the second sum of Rs. 50,937/-. The High Court has, by the impugned judgment, upheld the view of the Tribunal and has held that the two amounts constitute revenue expenditure for the concerned assessment years and are deductible in order to arrive at the income of the assessee for the said assessment years. The present appeals are filed by the department from the impugned judgment of the High Court.

The assessee in the present case has spent the amounts in question in order to construct a new building after demolishing the old building. The new building, however, from inception was to belong to the lessor and not to the assessee. The assessee, however, had the benefit of the existing lease in respect of the new building at the agreed rent for a period of 39 years. The Tribunal has found, as a fact, that the rent as stipulated in the lease was extremely low. If rental rate for the area in which the building was situated was much higher and would be not less than Rs. 12,000/- as against which the maximum rent the assessee would be paying was only Rs. 2,000/-. This concessional rent was on account of the fact that the new building was constructed by the assessee at its own cost.



In order to decide whether this expenditure is revenue expenditure or capital expenditure, one has to look at the expenditure from a commercial point of view. What advantage did the assessee get by constructing a building which belonged to somebody else and spending money for such construction? The assessee got a long lease of a newly constructed building suitable to its own business at a very concessional rent. The expenditure, therefore, was made in order to secure a long lease of new and more suitable business premises at a lower rent. In other words, the assessee made substantial savings in monthly rent for a period of 39 years by expending these amounts. The saving in expenditure was saving in revenue expenditure in the form of rent. Whatever, substitutes for revenue expenditure, should normally be considered as revenue expenditure. Moreover, assessee in the present case did not get any capital asset by spending the said amounts. The assessee, therefore, could not have claimed any depreciation. Looking to the nature of the advantage which the assessee obtained in a commercial sense, expenditure appears to be revenue expenditure.

The test for distinguishing between capital expenditure and revenue expenditure in our country was laid down by this Court in Assam Bengal Cement Co. Ltd. v. Commissioner of Income-tax, West Bengal (27 ITR 34). In that case, the appellant-company had acquired from the Government of Assam lease of certain lime-stone quarries for a period of 20 years for the purpose of manufacture of cement. The lessee had, inter alia, agreed to pay an annual sum during the whole period of the lease as a protection fee and in consideration of that payment, the lessor undertook not to grant to any person any lease, permit or prospecting license for limestone. This Court examined tests laid down in various cases for distinguishing between capital expenditure and revenue expenditure. One of the standard tests now in use was laid down in the case of Atherton v. British Insulated and Helsby Cables Ltd. ([1925] 10 Tax Cases 155). It said: "When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital." Whether by spending the money any advantage of an enduring nature has been obtained or not will depend upon the facts of each case. Moreover, as the above passage itself provides, this test would not apply if there are special circumstances pointing to the contrary. This Court in the above case summarised the tests as follows : (p. 44):

Outlay is deemed to be capital when it is made for the initiation of a business, for extension of a business, or for a substantial replacement of equipment.



Expenditure may be treated as properly attributable to capital when it is made not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade.....If what is got rid of by a lump sum payment is an annual business expense chargeable against revenue, the lump sum payment should equally be regarded as a business expense, but if the lump sum payment brings in a capital asset, then that puts the business on another footing altogether.

Whether for the purpose of the expenditure, any capital was withdrawn, or, in other words, whether the object of incurring the expenditure was to employ what was taken in as capital of the business. Again, it is to be seen whether the expenditure incurred was part of the fixed capital of the business or part of its circulating capital. (Underlining ours)

Relying upon the second test enumerated above, learned counsel for the appellant has submitted that the assessee got enduring benefit of a capital nature by spending the amount because the assessee obtained a new building for a period of 39 years. The difficulty, however, in the present case, arises from the fact that this building was never to belong to the assessee. Right from inception, the building was of the ownership of the lessor. Therefore, by spending this money, the assessee did not acquire any capital asset. The only advantage which the assessee derived by spending the money was that it got the lease of a new building at a low rent. From the business point of view, therefore, the assessee got the benefit of reduced rent. The High Court has, therefore, rightly considered this as obtaining a business advantage. The expenditure is, therefore, to be treated as revenue expenditure.

*Although there are a number of cases dealing with this question, we will limit ourselves to examining a few cases where the assessee, by expending money, created an asset of an enduring nature. However, the asset so created did not belong to the assessee. In such a situation the courts have held that the expenditure was for better carrying on of the business of the assessee and could be allowed as revenue expenditure, looking to the circumstances of each of those cases. Thus in *Lakshmi Sugar Mills Co. P. Ltd. v. Commissioner of Income-tax, New Delhi* (82 ITR 376) the assessee company was carrying on the business of manufacture and sale of sugar. It paid to the Cane Development Council certain amounts by way of contribution for the construction and development of roads between various sugarcane-producing centers and the sugar factories of the assessee. The roads remained the property of the Government. This Court held that the expenditure was not of a capital nature and had to be allowed as an admissible deduction in computing the profits of the assessee's business. The expenditure was incurred for the purpose of*



facilitating the running of the assessee's motor vehicles and other means employed for transportation of sugarcane to its factories.

In the case of L.H. Sugar Factory and Oils Mills (P) Ltd. v. Commissioner of Income-tax, U.P. (125 ITR 293), the assessee was carrying on the business of manufacture and sale of sugar. It has factory in U.P. The assessee paid a contribution towards meeting the cost of construction of roads in the area around its factory under a sugarcane development scheme. The question was whether this amount was deductible in computing the assessee's profits. The Court held that it was. Because although the advantage secured was of long duration, it was not an advantage in the capital field because no tangible or intangible asset was acquired by the assessee; nor was there any addition to or expansion of the profit making apparatus of the assessee. The amount was contributed for the purpose of facilitating the business of the assessee and making it more efficient and profitable. It was, therefore, revenue expenditure.

In the case of Commissioner of Income-tax, Bombay City-I v. Associated Cement Companies Ltd. (172 ITR 257) the respondent-company entered into an agreement to supply water to the municipality and to provide water pipelines as also supply electricity for street lighting and put up a transmission line for that purpose. The assessee also agreed to concrete the main road from the factory to the railway station. The amounts expended for these purposes were held to be revenue expenditure since the installations and accessories were the assets of the municipality and not of the assessee. The expenditure, therefore, did not result in creating any capital asset for the company. The advantage secured by the respondent was immunity from liability to pay municipal rates and taxes for a period of 15 years. This Court said that had these liabilities been paid, the payments would have been on revenue account. Therefore, the advantage secured was in the field of revenue and not capital.

In the case of Commissioner of Income-tax v. Bombay Dyeing and Manufacturing Co. Ltd. (219 ITF 521) the company contributed to the State Housing Board certain amounts for construction of tenements for its workers. The tenements remained the property of the Housing Board. It was held that the expenditure was incurred wholly and exclusively on the welfare of the employees and, therefore, constituted legitimate business expenditure. As the assessee company acquired no ownership rights in the tenements, this Court said that the expenditure was incurred merely with a view to carry on the business of the company more efficiently by having a contented labour force.

All these cases have looked upon expenditure which did bring about some kind of an enduring benefit to the company as revenue expenditure when the expenditure did not bring into existence any



capital asset for the company. The asset which was created belonged to somebody else and the company derived an enduring business advantage by expending the amount. In all these cases, the expense has been looked upon as having been made for the purpose of conducting the business of the assessee more profitably or more successfully. In the present case also, since the asset created by spending the said amounts did not belong to the assessee but the assessee got the business advantage of using modern premises at a low rent, thus saving considerable revenue expenditure for the next 39 years, both the Tribunal as well as the High Court have rightly come to the conclusion that the expenditure should be looked upon as revenue expenditure.

In the premises, the appeals are dismissed with costs.'

14. respectfully following the above said decision, we allow ground No.2 raised by the assessee”.

In view of the above, the Appellant submits before us to follow its own case vide ITAT order for A.Y. 1999-00 dated 27 September 2022 and allow deduction for the entire amount incurred on refurbishment of premises. Revenue is not able to produce any argument to controvert the facts of the ground raised by the assessee and also not able to controvert the stand taken by the coordinate bench in assessee's own case. Hence, in the given situation respectfully following the decision of coordinate bench in assessee's own case for A.Y. 1999-00, dated 17 October 2022, ground raised by the assessee is allowed.”

24. Respectfully following the above decision and following the principle of consistency, the view taken by the Tribunal in A.Y. 2001-02 is respectfully followed, accordingly, ground raised by the revenue is dismissed.”

24.1. Revenue has not been able to produce any argument to controvert the facts of the ground raised by the assessee and also not able to controvert the stand taken by the coordinate bench in assessee's own case. Respectfully following the consistent approach followed by this *Tribunal*, this addition made by Ld.AO deserves to be deleted.

Accordingly, Ground No. 6 raised by assessee stands allowed.

Assessment Year 2005-06.



25. It was submitted by both the assessee and the Revenue that most of the grounds raised in the cross appeals for Assessment Year 2005–06 are *mutatis mutandis* identical to the issues already adjudicated by us while deciding the cross appeals for Assessment Year 2004–05. It was contended that, except for variation in the quantum of the additions/disallowances, the nature of the disputes, the rival submissions advanced by the parties, and the issues arising for consideration remain substantially the same as those dealt with by us in the preceding paragraphs while adjudicating the appeals for Assessment Year 2004–05. For the sake of convenience and to avoid repetition, the corresponding grounds raised by the assessee as well as the Revenue for Assessment Year 2005–06 are tabulated issue-wise as under:

Department appeal Ground No. A.Y. 2004–05	Department appeal Ground No. A.Y. 2005–06	Issue
1	1	Disallowance of Direct Cost
2	2	Salaries paid to expatriates taxable under section 28(iv) of the Act
3 to 7	3 to 7	Taxability of interest income in the hands of Head Office
8 and 9	8 and 9	Disallowance of interest paid to Head Office
10	10	Expenditure attributed to exempt income
11	NA	Recoveries against securities losses
12	11	Deduction of Head Office expenditure in entirety (Article 26 of India–UK Tax Treaty – Non-discrimination)



Assessee's appeal Ground No. A.Y. 2004-05	Assessee's appeal Ground No. A.Y. 2005-06	Issue
1	1	General Ground
2	2	Transfer Pricing provisions are not applicable- Not an associated Enterprise under Article 10 of India - UK DTAA
3	3	Transfer pricing adjustment is unsustainable and bad in law
4	4	Transfer pricing adjustment in respect of direct cost

25.1. Accordingly, for the sake of convenience and to avoid repetition, the corresponding grounds raised by the assessee as well as the Revenue for Assessment Year 2005-06 have been tabulated hereinabove issue-wise with reference to the corresponding grounds adjudicated for Assessment Year 2004-05. Since the facts and issues involved are identical, our findings and conclusions recorded while deciding the respective grounds for Assessment Year 2004-05 shall apply *mutatis mutandis* to the corresponding grounds raised by both the assessee and the Revenue for Assessment Year 2005-06.

Revenue's Appeal

26. The only additional issue arising in the Revenue's appeal for Assessment Year 2005-06, which requires independent adjudication and did not arise for consideration while deciding the cross appeals for Assessment Year 2004-05, pertains to Ground Nos. 12 to 14, relating to the allowability of loss arising on the year-end revaluation/mark-to-market valuation of outstanding foreign exchange forward contracts. Since no corresponding ground was



involved in the appeals for the immediately preceding assessment year, the said issue is required to be examined independently on its own facts and in accordance with law. We, therefore, proceed to adjudicate Ground Nos. 12 to 14 of the Revenue's appeal for Assessment Year 2005–06 separately, as under:

27. Ground Nos. 12-14 raised by the revenue relates to the disallowance on revaluation of Forward Foreign Exchange Contract.

The assessee-bank, in the ordinary course of its banking business, enters into foreign exchange forward contracts with its customers on a day-to-day basis. In certain cases, the maturity of such forward contracts extends beyond the end of the relevant accounting year. In accordance with the accounting guidelines prescribed by the Reserve Bank of India (RBI) and the rates notified by the Foreign Exchange Dealers Association of India (FEDAI), the assessee consistently revalues all outstanding foreign exchange forward contracts as on the balance sheet date and recognizes the resultant profit or loss in its books of account. During the relevant previous year, the assessee debited a sum of Rs.7,13,49,112/- to its Profit and Loss Account towards loss arising on the year-end revaluation of unmatured foreign exchange forward contracts outstanding as on 31.03.2005 and claimed the same as a deduction while computing its taxable income.

27.1. During the course of the assessment proceedings, the Ld.AO disallowed the aforesaid claim by holding that the loss represented merely a mark-to-market loss on forward contracts that were yet to mature and, therefore, was not an ascertained liability. According to the Ld.AO, the actual profit or loss on such



contracts could be determined only upon their maturity or settlement in a subsequent assessment year and not as on the balance sheet date. Although the assessee, vide its letter dated 18.03.2008, relied upon various judicial precedents in support of its claim that the mark-to-market loss was allowable as a deduction in the relevant assessment year, the Ld. AO rejected the contention. In doing so, the Ld.AO placed reliance upon the decision of the *Hon'ble Madras High Court* in case of *Indian Overseas Bank v. CIT* reported in 183 ITR 200, wherein it was held that the profit or loss on foreign exchange forward contracts can be ascertained only upon settlement of the contracts and that any loss recognized prior thereto is merely notional and, therefore, not allowable as a deduction.

Aggrieved by the aforesaid disallowance, the assessee preferred an appeal before the Ld.CIT(A).

28. The Ld.CIT(A), following the judicial precedents governing the issue, deleted the disallowance by observing that the assessee-bank had consistently followed the accounting methodology prescribed under the RBI/FEDAI guidelines, which require year-end revaluation of outstanding foreign exchange forward contracts. The Ld.CIT(A) further held that the resultant loss represented a recognized trading loss and was, therefore, allowable as a deduction.

Aggrieved by the relief so granted, the Revenue is in appeal before us.

29. The Ld.DR placed reliance on the assessment order and submitted that the loss claimed by the assessee on the year-end



revaluation of outstanding foreign exchange forward contracts was merely notional and contingent in nature and did not represent an ascertained liability. It was contended that, unless the forward contracts actually matured or were settled, no real profit or loss could be said to have crystallized. Accordingly, the mark-to-market loss claimed by the assessee was not allowable as a deduction under the provisions of the Act.

29.1. On the contrary, the Ld.Sr.Counsel relied on the decision by *coordinate bench of this Tribunal in assessee's own case for AY 1996-97 (read with confirmatory order dated 22/01/2026)* and decision of *Hon'ble Supreme Court* in case of *Woodward Governor India (P.) Ltd.* reported in *312 ITR 254*, wherein deduction of loss arising on revaluation of forward foreign has been allowed.

The Ld.Sr.Counsel relied on following decisions of coordinate bench of this *Tribunal*, where identical issue has been addressed.

Mashreq Bank PSC [2007] (18 SOT 233) (Mum ITAT)

- *Deutsche Bank v. DCIT [2003] (86 ITD 431) (Mum ITAT)*

29.1. The Ld.Sr.Counsel also relied on following decisions by *Hon'ble Supreme Court* and *Hon'ble Bombay High Court* where mark-to-market losses were held to be allowable:

- *Chainrup Sampatram v. CIT [1953] (24 ITR 481)*
- *CIT v. Bank of India [1996] (218 ITR 371)*

We have perused the submissions advanced by both sides in light of records placed before us.

30. The undisputed facts reveal that the assessee, being a banking company, enters into foreign exchange forward contracts with its



customers in the ordinary course of its banking business. It is also an admitted position that the assessee has consistently followed the accounting policy prescribed by the Reserve Bank of India (RBI) read with the guidelines issued by the Foreign Exchange Dealers Association of India (FEDAI), whereby all outstanding foreign exchange forward contracts are revalued at the prevailing exchange rates as on the balance sheet date and the resultant gain or loss is recognized in the Profit and Loss Account. The Revenue neither disputed the method of accounting consistently followed by the assessee, nor demonstrated that the same does not reflect the true and correct profits of the business.

30.1. The sole basis for the disallowance made by the Ld.AO is that the forward contracts had not matured as on the close of the relevant previous year and, therefore, the loss was merely notional and contingent in nature. We are unable to subscribe to the aforesaid view. It is a settled proposition of law that where the liability has accrued on the balance sheet date and is capable of being reasonably determined in accordance with a recognized method of accounting, the same cannot be regarded as a contingent liability merely because its actual discharge would take place at a future date. The valuation of revenue assets and liabilities at the year-end is an accepted principle of commercial accounting intended to determine the true profits of the business. Consequently, the loss arising on the year-end revaluation of outstanding foreign exchange forward contracts, computed in accordance with the RBI/FEDAI guidelines, represents an accrued business loss and not a hypothetical or contingent loss.



30.2. We find that the issue is no longer *res integra*. The *Hon'ble Supreme Court* in *CIT v. Woodward Governor India (P.) Ltd.(supra)* has categorically held that the loss arising on account of fluctuation in the foreign exchange rate as on the balance sheet date is an item of expenditure under section 37(1) of the Act and is allowable as a deduction if it is computed in accordance with the regularly employed method of accounting. The principle that stock-in-trade and other revenue items are required to be valued at the close of the accounting year so as to ascertain the true profits of the business also stands recognized by the *Hon'ble Supreme Court* in *Chainrup Sampatram v. CIT(supra)*. Similar principles have been applied by *Hon'ble Bombay High Court* in *CIT v. Bank of India(supra)* while considering the valuation of foreign exchange contracts by banking companies.

30.2. We also note that an identical issue has arisen in the assessee's own case for the earlier assessment years. The *Co-ordinate Bench* of this *Tribunal*, while deciding the appeals for Assessment Year 1996-97 (read with the confirmatory order dated 22.01.2026), has accepted the assessee's claim. Similar views have also been expressed by the *Co-ordinate Bench* in the cases of *Mashreq Bank PSC v. DCIT(supra)* and *Deutsche Bank v. DCIT (supra)*. The Revenue has not brought on record any distinguishing feature in the facts of the present assessment year warranting a departure from the consistent view taken in the assessee's own case.

30.3. In view of the aforesaid discussion, we hold that the loss arising on the year-end revaluation of outstanding foreign exchange forward contracts, computed in accordance with the



RBI/FEDAI guidelines and the consistently followed method of accounting, represents an accrued trading loss and is allowable as a deduction under the provisions of the Act. The Ld. AO was, therefore, not justified in treating the same as a notional or contingent loss merely because the forward contracts had not matured as on the balance sheet date. We, accordingly, do not find any infirmity in the view taken by the Ld. CIT(A) and the same is upheld.

Accordingly, Grounds 12-14 raised by the revenue stands dismissed.

Assessee's Appeal

31. The only issue arising in the assessee's appeal for Assessment Year 2005-06 is **Ground No.5**, which requires independent adjudication.

It is noted that the issue raised in this Ground relate to the disallowance of direct costs amounting to Rs. 39,04,89,028/- made by the Ld.AO under section 37 of the Act. According to the Ld.Sr.Counsel, the said expenditure had already been subjected to transfer pricing adjustment by the Ld.TPO, who determined the ALP of the corresponding international transaction at Nil. It was, therefore, contended that the Ld.AO was not justified in once again disallowing the very same expenditure, resulting in a duplication of the disallowance.

31.1. The Ld.Sr.Counsel submitted that the direct expenses amounting to Rs.39,04,89,028/- were incurred wholly and exclusively for the purposes of the business carried on by the Indian Permanent Establishment and were, therefore, allowable as



a deduction in computing its taxable income in accordance with the provisions of the Act as well as the India-UK DTAA. He submitted that the Ld.AO had disallowed the said expenditure solely on the ground that the Ld.TPO had determined the ALP of the corresponding international transaction at Nil. It was contended that the determination of the ALP at Nil was itself unsustainable in law and on facts for the reasons advanced while addressing the transfer pricing grounds. Accordingly, once the transfer pricing adjustment is held to be unsustainable, the consequential disallowance of the direct expenditure amounting to Rs.39.05 crore is also liable to be deleted and the assessee is entitled to deduction of the said expenditure while computing its taxable income.

31.2. On the contrary, the Ld.DR relied on the orders passed by the authorities below.

We have perused the submissions advanced by both sides in light of records placed before us.

32. The short controversy before us is whether the direct expenditure amounting to Rs.39,04,89,028/- is allowable as deduction. It is an undisputed position that the impugned expenditure was incurred in connection with and for the purposes of the assessee's banking business in India. The Revenue has not disputed either the nature of the expenditure or the business purpose for which the same was incurred. In fact, the Ld.TPO himself, on examination of the documentary evidence furnished by the assessee, accepted the Arm's Length Price of substantial portion of the direct costs after being satisfied regarding the receipt



of services and the benefits derived therefrom. Thus, the very exercise undertaken by the Ld.TPO proceeds on the premise that the expenditure was incurred for business purposes and that the only issue was the extent to which the arm's length nature thereof stood substantiated.

32.1. In our considered opinion, once it is accepted that the expenditure has been incurred wholly and exclusively for the purposes of the assessee's business, the same cannot be disallowed merely because the assessee could not furnish similar documentary evidence in respect of the balance expenditure before the Ld.TPO. The allowability of an expenditure under the Act is governed by its nature and nexus with the business, and not merely by the quantum of evidence accepted by the Ld.TPO while determining the ALP. The Ld.TPO himself accepted the arm's length nature of the expenditure to the extent supported by evidence. Therefore, in the facts of the present case, in the absence of any finding that the balance expenditure was not incurred for the purposes of business, or that it was sham, fictitious or personal in nature, there was no justification for denying the deduction merely because additional evidences were not furnished.

32.3. Accordingly, considering that the business purpose of the expenditure remains undisputed and that a substantial portion of the expenditure stood accepted by the Ld.TPO upon verification of the evidences produced by the assessee, we find no justification for sustaining the disallowance. The Ld.AO is, therefore, directed to allow the deduction of the impugned expenditure. The ground raised by the assessee is accordingly allowed.



Accordingly, Ground No. 5 of the assessee's appeal for A.Y. 2005-06 stands allowed.

In the result the appeals filed by the assessee and revenue for assessment years 2004-05 and 2005-06 stands partly allowed.

Order pronounced in the open court on 16/07/2026.

Sd/-
ARUN KHODPIA
ACCOUNTANT MEMBER

Sd/-
BEENA PILLAI
JUDICIAL MEMBER

Mumbai
Dated: 16/07/2026
SC. Sr. P.S.

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