IN THE INCOME TAX APPELLATE TRIBUNAL
HYDERABAD BENCHES "B", HYDERABAD

BEFORE
SHRI RAMA KANTA PANDA, ACCOUNTANT MEMBER
&
SHRI K.NARASIMHA CHARY, JUDICIAL MEMBER

ITA No. 202/Hyd/2020
(Assessment Year: 2016-17)

NACL Industries Limited, Hyderabad [PAN No. AAACN6932H]	Vs.	Assistant Commissioner of Income Tax, Circle-16(1), Hyderabad
Appellant		Respondent

Assessee by:	Shri C.S.Subrahmanyam, AR
Revenue by:	Shri Rohit Mujumdar, DR

Date of hearing:	02-06-2022
Pronouncement on:	23-06-2022

ORDER

PER K. NARASIMHA CHARY, JM:

Aggrieved by the order dated 02-12-2019, passed by the Learned Commissioner of Income Tax (Appeals)-4, Hyderabad ("Ld. CIT(A)") in the case of M/s.NACL Industries Limited ("the assessee") for the AY.2016-17, assessee preferred this appeal.

2. Briefly stated facts relevant for the disposal of this appeal are that the assessee is a company engaged in the business of manufacture and trading of Agro chemicals and pesticides with the manufacturing plants in Srikakulam and Ethakota areas. They have filed their return of income for the assessment year 2016-17 on 16-10-2016 declaring an income of ₹ 10, 59,83,375/-before set off of brought forward losses and book profit under section 115 JB of the Income Tax Act, 1961 (for short "the Act") at ₹ 10,85, 79,910/-. By order dated 27-12-2018, passed under section 143(3) of the Act, learned Assessing Officer made an addition of ₹ 1,09,14,682/- because of disallowance under section 35(2AB) of the Act, ₹ 84,28,163/- by disallowing the social welfare expenses and ₹ 9,99,631/- under section 14A of the Act read with Rule 8D of the Income Tax Rules1962 ("the Rules").

3. Aggrieved by such an action of the learned Assessing Officer, assessee preferred an appeal before the Ld. CIT(A) challenging the disallowance of the social welfare expenditure and disallowance under section 14A of the Act read with Rule 8D of the Rules. According to the learned Assessing Officer the social welfare expenses incurred by the assessee were in the nature of "corporate social responsibility" (CSR), only such expenses which were incurred wholly and exclusively for the purpose of business could be allowed as a direction but not the expenses in the nature of CSR. According to the learned Assessing Officer the expenditure incurred by the assessee is only application of income and has nothing to do with the business of the assessee.

4. By way of impugned order, Ld. CIT(A) allowed relief to the assessee in respect of the addition made on account of disallowance under section 14A of the Act read with Rule 8D of the Rules, but confirmed the addition

of ₹ 84,28,163/- made on account of disallowance of social welfare expenditure. Hence the assessee is before us in this appeal to delete the disallowance of social welfare expenses.

5. It is the submission of the Ld. AR that in as much as the assessee is running the chemical plants near the villages and dependent upon the participation of the villagers in the activities by engaging them to work in their factories in various capacities it is necessary for them to win the goodwill of the people so as to how the seamless supply of labour everyday and also for smooth functioning of the chemical plants. According to the Ld. AR is not necessary that every expense that could be allowed as a direction should be such as a hard-nosed and perhaps devoid of sense of compassion, businessman alone would incur in furtherance of his business pursuits, as was held by various fora on this aspect. He placed reliance on the addition of a Coordinate Bench of Raipur Tribunal in ACIT Vs. Jindal Power Ltd (2016) 70 taxmann.com 389 (Raipur Trib.).

6. Per contra, while justifying the findings of the authorities below, Ld. DR, placed reliance on the decisions of the Hon'ble Andhra Pradesh High Court in the case of CIT Vs. Singareni Collieries Co (1997) 90 Taxman 185 (AP), Hon'ble Madras High Court in the case of Ismail and Sethuraman (1977) 107 ITR 470 (Mad), Bangalore Bench of ITAT in the case of Kanhaiyalal Dudheria (2017) 82 taxmann.com 134 and Jaipur Bench of ITAT in the case of DCIT Vs. Rajasthan State Mines & Minerals Ltd. (2012) 25 taxmann.com 11 (JP) to submit that where the assessee fails to prove that the expense is wholly and exclusively for the purpose of business, no deduction under section 37(1) of the Act is allowable.

7. In reply, Ld. AR submitted that the decisions relied upon by the Revenue have no application to the facts of the case, inasmuch as in the case of Singareni Collieries Co. (supra) it was not clear whether the assessee was prompted by a business motive in adopting the orphans, because it was done at the appeal of the State Government; in the case of Ismail and Sethuraman (supra) the expense was the donation paid to a political party; in the case of Kanhaiyalal Dudheria (supra) the expenditure was incurred on construction of houses to be handed over to the people affected by the floods; and lastly in the case of Rajasthan State Mines & Minerals Ltd. (supra) the expense was incurred on cultural events which have no nexus with the business. Ld. AR submitted that facts of none of the cases is comparable to the case of the assessee, whereas the facts of the case of assessee are similar to the facts covered by the decision in the case of Jindal Power Ltd (supra).

8. We have gone through the record in the light of the submissions made on either side. It could be seen from the record that, it was pleaded by the assessee before the learned Assessing Officer and also before the Ld. CIT(A) that the expenditure incurred by it is in the nature of social welfare activities but not CSR activities. Assessee pleaded that they have incurred the expenses in the form of supply of water to nearby villages, operation and maintenance expenses of RO plants of nearby villages, borewells maintenance expenses, contribution to vidya volunteer scheme, donation of schoolbags and uniforms to local schoolchildren, stipends to students, financial assistance to nearby villages for various welfare activities in the villages etc., and it is necessary for them to incur such expenditure to secure the cooperation of the villages for smooth running

of the manufacturing plants it was further submitted that such an expenditure was necessary because the assessee engages the villagers to work and then factory in various capacities and therefore, winning the goodwill is equally important for their business.

9. On a perusal of the decisions relied upon by the Revenue, we are inclined to accept the explanation offered by the assessee for the nonapplication of the ratio of these decisions to the facts of the case on hand because the facts of none of the cases is comparable to the facts of the case on hand. In Singareni Collieries Co. (supra) at the request of the State Government, the assessee incurred the expenditure for rehabilitation of the orphan children and the Hon'ble High Court observed that it was not clear as to whether the assessee was prompted by a business motive in adopting the orphans. The case of Ismail and Sethuraman (supra), it could be seen, is a case where the assessee claimed deduction of certain amounts paid by it to a political party is a donation. In the case of Kanhaiyalal Dudheria (supra) the expenditure incurred by the assessee was on the construction of houses to be handed over to the people affected by the floods. So also in the case of Rajasthan State Mines & Minerals Ltd. (supra) the expenditure was for conducting certain cultural events like Umang Utsav, amounts paid to Rose Society for sponsorship of Rose show, payment to the parishad for sponsorship of 46 Maha Rana Kumbha Sangeet Samaroh etc. It is, therefore, clear that none of the assessee is comparable to the case on hand inasmuch as there is not an iota of contention on behalf of the assessee is therein that the expenditure had any nexus to the business of the assessees.

10. Now coming to the case on hand, absolutely there is no dispute that the assessee incurred the expenditure in dispute. There is also no dispute that the assessee incurred expenditure in the form of supply of water to nearby villages, operation and maintenance expenses of RO plants of nearby villages, burbles maintenance expenses, contribution to media volunteer scheme, donation of schoolbags and uniforms to local schoolchildren, stipends to students, financial assistance to nearby villages for various welfare activities in the religious etc. As pointed out by the Ld. AR, in the case of Jindal Power Ltd. (supra), the assessee incurred the expenses on construction of school building, Devasthanam/temple, drainage, barbed wire fencing, educational schemes and distribution of cloths etc., voluntarily in the vicinity of the business place.

11. It was contended in that case also that the incurring of the expenditure was voluntary, not mandatory and not for the purpose of business. It was further contended that such a voluntary expenditure, which is not mandated by any enactment and which the assessee was not statutorily bound to incur, is not admissible for deduction in computation of business income.

12. The Tribunal, however, turned down such a contention advanced on behalf of the assessee and dealt with the issue in detail more particularly in the light of explanation 2 to section 37(1) of the Act with effect from 01-04-2015. The reasoning of the Tribunal to reach the conclusion that the assessee is entitled to claim the deduction of such an expenditure is strikingly applicable to the facts of this case and we deem it just and necessary, for the sake of completeness, to extract the relevant observations of the Tribunal which are self-explanatory:

16. We have noted that fundamental objection of the Assessing Officer is that the expenses is voluntary, not mandatory and not for business purposes. As for the contention that the expenses being in the nature of voluntary expenses, which are not mandatory, and which the assessee was not statutorily required to incur, are not admissible deduction in computation of business income, we are of the considered view that as long as expenses are incurred wholly and exclusively for the purposes of earning the income from business or profession, merely because some of these expenses are incurred voluntarily, i.e. without there being any legal or contractual obligation to incur the same, those expenses do not cease to be deductible in nature. In other words, it is not necessary that every expense that could be allowed as a deduction should be such as a hardnosed and perhaps devoid of senses of compassion, businessman alone would incur in furtherance of his business pursuits. We find guidance from a passage from the judgment of House of Lords in the case of Atherton v. British Insulated & Helsbey Cables Ltd. [1925] 10 Tax Cases 155 (HL), referred to with approval by the Hon'ble Supreme Court in the case of CIT v. Chandulal Keshavlal & Co. [1960] 38 ITR 601, which reads as follows: "It was made clear in the above cited cases of Usher's Wilshire Brewery v. Bruce (supra) and Smith v. Incorporated Council of Law Reporting [1914] 6 Tax Cases 477 that a sum of money expended not with a necessity and with a view to direct immediate benefit to the trade, but voluntarily and on the grounds of commercial expediency and in order to indirectly facilitate, carrying on of business may yet be expended wholly and exclusively for the purpose of the trade; and it appears to me that the findings of the CIT in the present case, bring the payment in question within that description. They found (in words which I have already quoted) that payment was made for the sound commercial purpose of enabling the company to retain the existing and future members of staff and for increasing the efficiency of the staff; and after referring to the contention of the Crown that the sum of Sterling Pound 31,784 was not money wholly and exclusively laid out for the purpose of the trade under the rule above referred to, they found deduction was admissible thus in effect, though not in terms, negativing the Crowns contentions. I think that there was ample material to support the findings of the CIT, and accordingly hold that this prohibition does not apply." It will, therefore, be clear that even if an expense is incurred voluntarily, it may still be construed as 'wholly and exclusively'. Explaining this principle, Hon'ble Supreme Court has, in the case of Sassoon J David & Co. (P) Ltd. v. CIT [1979] 118 ITR 261/1 Taxman 485inter alia

observed that : "It has to be observed here that the expression "wholly and exclusively" used in s. 10(2)(xv) of the Act does not mean "necessarily". Ordinarily, it is for the assessee to decide whether any expenditure should be incurred in the course of his or its business. Such expenditure may be incurred voluntarily and without any necessity and if it is incurred for promoting the business and to earn profits, the assessee can claim deduction under s. 10(2)(xv) of the Act even though there was no compelling necessity to incur such expenditure. It is relevant to refer at this stage to the legislative history of s. 37 of the IT Act, 1961, which corresponds to s. 10(2)(xv) of the Act. An attempt was made in the IT Bill of 1961 to lay down the "necessity" of the expenditure as a condition for claiming deduction under s. 37. Sec. 37(1) in the Bill read "any expenditure, laid out or expended wholly, necessarily and exclusively for the purposes of the business or profession shall be allowed." The introduction of the word "necessarily" in the above section resulted in public protest. Consequently, when s. 37 was finally enacted into law, the word "necessarily" came to be dropped. The fact that somebody other than the assessee is also benefited by the expenditure should not come in the way of an expenditure being allowed by way of deduction under s. 10(2)(xv) of the Act if it satisfies otherwise the tests laid down by law."

17. The next issue is whether it is for the purposes of business or not. We may, in this regard, usefully refer to the observations of a coordinate bench of this Tribunal, speaking through one of us (i.e. the Accountant Member) and in the case of Hindustan Petroleum Corporation Ltd v Dy. CIT [2005] 96 ITD 186/[2004] 141 Taxman 33 (Mum.) (Mag.), as follows:

"7. We find that as held by Hon'ble Karnataka High Court in the case of Mysore Kirloskar Ltd. v. CIT [1987] 166 ITR 836, while 'the basic requirements for invoking sections 37(1) and 80G are quite different', 'but nonetheless the two sections are not mutually exclusive'. Thus, there are overlapping areas between the donations given by the assessee and the business expenditure incurred by the assessee. In other words, there can be certain amounts, though in the nature of donations, and nonetheless, these amounts may be deductible under section 37(1) as well. Therefore, merely because an expenditure is in the nature of donation, or, to use the words of the CIT(A), 'promoted by altruistic motives', it does not cease to be an expenditure deductible under section 37(1). In Mysore Kirloskar Ltd.'s case (supra), Their Lordships have observed that even if the contributions by the assessee is in the forms of donations, but if it

could be termed as expenditure of the category falling in section 37(1), then the right of the assessee to claim the whole of it as a deduction under section 37(1) cannot be declined. What is material in this context is whether or not the expenditure in question was necessitated by business considerations or not. Once it is found that the expenditure was dictated by commercial expediencies, the deduction under section 37(1) cannot be declined. As to what should be relevant for examining this aspect of the matter, we may only refer to the observations of Hon'ble Supreme Court in the case of Sri Venkata Satyanarayna Rice Mill Contractors Co. v. CIT [1997] 223 ITR 1012:

**. . . any contribution made by an assessee to a public welfare fund which is directly connected or related with the carrying on of the assessee's business or which results in the benefit to the assessee's business has to be regarded as an allowable deduction under section 37(1) of the Act. Such a donation, whether voluntary or at the instance of the authorities concerned, when made to a Chief Minister's Drought Relief Fund or a District Welfare Fund established by the District Collector or any other fund for the benefit of the public and with a view to secure benefit to the assessee's business, cannot be regarded as payment opposed to public policy. It is not as if the payment in the present case had been made as an illegal gratification. There is no law which prohibits the making of such a donation. The mere fact that making of a donation for charitable or public cause or in public interest results in the Government giving patronage or benefit can be no ground to deny the assessee a deduction of that amount under section 37(1) of the Act when such payment had been made for the purpose of assessee's business.*

8. In the case of CIT v. Madras Refineries Ltd. [2004] 266 ITR 170 1, Hon'ble Madras High Court has upheld deductibility of the amount spent by the assessee even on bringing drinking water to locality and in aiding local school. While doing so, Their Lordships observed as follows:

The concept of business is not static. It has evolved over a period of time to include within its fold the concrete expression of care and concern for the society at large and the locality in which business is located in particular. Being a good corporate citizen brings goodwill of the local community as also with the regulatory agencies and society at large, thereby creating an atmosphere in which the business can succeed in a greater measure with the aid of such goodwill . . . .

9. Let us now take a look at the undisputed facts of this case. The assessee is a company owned by the Government of India and working under the control and directions of the Government of India. As the statement of facts clearly sets out, the expenditure on 20-Point Programmes was incurred in view of specific directions of the Government of India. This factual aspect is not even disputed or challenged by the Revenue at any stage. It cannot but be in the business interest of the assessee-company to abide by the directions of the Government of India which also owns the assessee-company. In any event, as observed by the Hon'ble Madras High Court in Madras Refineries Ltd.'s case (supra), monies spent by the assessee as a good corporate citizen and to earn the goodwill of the society help creating an atmosphere in which the business can succeed in a greater measure with the help of such goodwill. The monies so spent therefore are required to be treated as business expenditure eligible for deduction under section 37(1) of the Act. What is the expenditure for the implementation of 20-point plant after all? It is solely for the welfare of the oppressed classes of society, for which even the Constitution of India sanctions positive discrimination, and for contribution to all around development of villages, which has always been the central theme of Government's development initiatives. An expenditure of such a nature cannot but be, to use the words employed by the Hon'ble Madras High Court in Madras Refineries Ltd.'s case (supra), 'a concrete expression of care and concern for the society at large' and an expenditure to discharge the responsibilities of a 'good corporate citizen which brings goodwill of with the regulatory agencies and society at large, thereby creating an atmosphere in which the business can succeed in a greater measure with the aid of such goodwill."

18. We have also take note of the fact that in view of insertion of Explanation 2 to Section 37(1), with effect from 1st April 2015, which provides that "for the removal of doubts, it is hereby declared that for the purposes of sub-section (1), any expenditure incurred by an assessee on the activities relating to corporate social responsibility referred to in section 135 of the Companies Act, 2013 (18 of 2013) shall not be deemed to be an expenditure incurred by the assessee for the purposes of the business or profession", the expenses incurred in discharging corporate social responsibility are not deductible in computation of business income. Learned Departmental Representative submits that this amendment should be treated as clarificatory in nature, as it is stated to be in so many words, and we should, therefore, hold that the expenses in

discharging corporate social responsibility were outside the ambit of expenses deductible under section 37(1).

19. We are unable to see legally sustainable merits in this plea either. The amendment in the scheme of Section 37(1), which has been introduced with effect from 1st April 2015, cannot be construed as to disadvantage to the assessee in the period prior to this amendment. This disabling provision, as set out in Explanation 2 to Section 37(1), refers only to such corporate social responsibility expenses as under Section 135 of the Companies Act, 2013, and, as such, it cannot have any application for the period not covered by this statutory provision which itself came into existence in 2013. Explanation 2 to Section 37(1) is, therefore, inherently incapable of retrospective application any further. In any event, as held by Hon'ble Supreme Court's five judge constitutional bench's landmark judgment, in the case of CIT v. Vatika Townships Pvt Ltd (2014) 367 ITR 466/227 Taxman 121/49 taxmann.com 249 (SC), the legal position in this regard has been very succinctly summed up by observing that "Of the various rules guiding how legislation has to be interpreted, one established rule is that unless a contrary intention appears, legislation is presumed not to be intended to have a retrospective operation. The idea behind the rule is that a current law should govern current activities. Law passed today cannot apply to the events of the past. If we do something today, we do it keeping in view the law of today and in force and not tomorrow's backward adjustment of it. Our belief in the nature of the law is founded on the bedrock that every human being is entitled to arrange his affairs by relying on the existing law and should not find that his plans have been retrospectively upset. This principle of law is known as lex prospicit non respicit: law looks forward not backward. As was observed in Phillips v. Eyre [, a retrospective legislation is contrary to the general principle that legislation by which the conduct of mankind is to be regulated when introduced for the first time to deal with future acts ought not to change the character of past transactions carried on upon the faith of the then existing law." It may appear to be some kind of a dichotomy in the tax legislation but the well settled legal position is that when a legislation confers a benefit on the taxpayer by relaxing the rigour of pre-amendment law, and when such a benefit appears to have been the objective pursued by the legislature, it would be a purposive interpretation giving it a retrospective effect but when a tax legislation imposes a liability or a burden, the effect of such a legislative provision can only be prospective. We have also noted that the amendment in the scheme of Section 37(1) is not specifically stated to be retrospective

> *and the said Explanation is inserted only with effect from 1st April 2015. In this view of the matter also, there is no reason to hold this provision to be retrospective in application. As a matter of fact, the amendment in law, which was accompanied by the statutory requirement with regard to discharging the corporate social responsibility, is a disabling provision which puts an additional tax burden on the assessee in the sense that the expenses that the assessee is required to incur under a statutory obligation in the course of his business are not allowed deduction in the computation of income. This disallowance is restricted to the expenses incurred by the assessee under a statutory obligation under section 135 of Companies Act 2013, and there is thus now a line of demarcation between the expenses incurred by the assessee on discharging corporate social responsibility under such a statutory obligation and under a voluntary assumption of responsibility. As for the former, the disallowance under Explanation 2 to Section 37(1) comes into play, but, as for latter, there is no such disabling provision as long as the expenses, even in discharge of corporate social responsibility on voluntary basis, can be said to be "wholly and exclusively for the purposes of business". There is no dispute that the expenses in question are not incurred under the aforesaid statutory obligation. For this reason also, as also for the basic reason that the Explanation 2 to Section 37(1) comes into play with effect from 1st April 2015, we hold that the disabling provision of Explanation 2 to Section 37(1) does not apply on the facts of this case.*

13. It is not the case of the Revenue that there is some other purpose for the assessee to incur these expenses nearby their chemical plants other than to win the goodwill of the people in order to secure their cooperation in smooth running of the chemical plants and also to secure their participation by engaging them in their work in different capacities. Such a purpose would definitely be congenial to the working atmosphere of the assessee and cannot be said that it is something foreign to the business purposes of the assessee. It cannot be said that such incurring of the expenditure by the assessee is the application of income and not the expenditure incurred for the purpose of business. As long as expenses are incurred for the purpose of earning the income from business, merely

because some of these expenses are incurred voluntarily without there being any legal or contractual obligation to incur the same, such expenses do not cease to be deductible in nature.

14. In the set of circumstances, we are of the considered opinion that the expenditure incurred by the assessee is not merely philanthropic, but also has a business angle, which we cannot ignore. For these reasons, we are of the considered opinion that the social welfare expenses incurred by the assessee at their workplace and nearby villages is an allowable deduction under section 37(1) of the act. With this view of the matter, we allow the grounds of appeal, and direct the learned Assessing Officer to addition of ₹ 84,28,163/-made under section 37(1) of the Act.

15. In the result, appeal of the assessee is allowed.

Order pronounced in the open court on this 23rd day of June, 2022

Sd/-	Sd/-
(RAMA KANTA PANDA)	**(K. NARASIMHA CHARY)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

TNMM

Hyderabad,
Dated: 23-06-2022

Copy forwarded to:

1. NACL Industries Limited, Plot No.12A, C-Block, Lakshmi Towers, Nagarjuna Hills, Panjagutta, Hyderabad.
2. Assistant Commissioner of Income Tax, Circle-16(1), Hyderabad.
3. The CIT(Appeals)-4, Hyderabad.
4. The Pr.CIT-4, Hyderabad.
5. DR, ITAT, Hyderabad.
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