

A DEPUTY COMMISSIONER, INCOME TAX, BARODA
v.
GUJARAT ALKALIES & CHEMICALS LTD.
(Civil Appeal Nos. 3957-3958 of 2002)

B FEBRUARY 8, 2008

[S.H. KAPADIA AND B. SUDERSHAN REDDY, JJ.]

Income Tax Act, 1961:

C s. 36 (1)(iii) and 37 – ‘Commitment charges’ on borrowed capital from a bank – Refinanced by foreign bank – Claim of, as deduction under s. 36 (1)(iii) – Held: Allowed as deduction u/s 37 and not u/s 36 (1)(iii) of the Act.

D s. 36 (1)(iii) – ‘Finance charges’ on borrowed capital – Nature of – Held: Is similar to payment of interest – Equated with commitment charges and treated as revenue expenditure – Hence, deductible u/s 37 of the Act.

Words and Phrases:

E ‘Commitment charges’ – Meaning of.

F The questions which arose for consideration in these appeals were as to whether ‘commitment charges’ payable by the assessee to a foreign company which had refinanced foreign currency loan obtained by assessee for its business activities from IDBI bank, could be allowed as deduction under section 36(1)(iii) of the Income-tax Act, 1961; and as to whether ‘charges’ paid to foreign company was similar to payment of interest under section 36(1)(iii) of the Act and, therefore, was to be allowed as deduction.

G Dismissing the appeals, the Court

HELD: 1.1 The ‘commitment charges’ was upfront payment. The Tribunal allowed the claim under section 37 and not under section 36(1)(iii), hence there is no

infirmity therein. [Para 3] [656-D, F]

Addl. Commr. Of Income-tax v. Akkamamba Textiels Ltd. 1997 (227) ITR 464; Commr. Of Income-tax v. Sivakami Mills Ltd. 1997 (227) ITR 465 – relied on.

1.2 On facts and circumstances of the instant case, once the Department equated the charges payable to the foreign company with interest, the judgment of this Court in *Dy Commr. of Income Tax, Ahmedabad v M/s. Core Health Care Ltd. comes in and the second issue is answered as claimed by assessee that the finance charges payable to foreign company was similar to payment of interest. [Para 4] [657-C, D]

**Dy Commr. of Income Tax, Ahmedabad v M/s. Core Health Care Ltd. decided by Supreme Court in Civil Appeal No, 3952-55 of 2002 – relied on.*

1.3 The finance charges paid by the assessee to the foreign company have also been equated by the Department with commitment charges which are held to be revenue expenditure and deductible under Section 37 of the Income-tax Act, 1961. [Para 5] [657-D, E]

CIVIL APPELLATE JURISDICTION : Civil Appeal Nos.3957-3958 of 2002.

From the Judgment and Order dated 25.04.2001 of the High Court of Gujarat at Ahmedabad in Tax Appeals Nos. 39-40 of 2001.

P. Vishwanatha Shetty, Gaurav Agrawal and B.V. Balaram Das for the Appellant.

J.P. Shah, Manish J. Shah, Jatin Zaveri and Harish J. Jhaveri for the Respondent.

The Judgment of the Court was delivered by

KAPADIA, J. 1. These civil appeals are filed by the Department against decision dated 25.4.01 in Tax Appeal

A Nos.39 and 40 of 2001 delivered by Gujarat High Court.

2. Two questions of law arise for determination in these civil appeals which are as follow:

B (1) Whether "commitment charges" can be allowed as deduction under Section 36(1)(iii) of the Income-tax Act, 1961?

C (2) Whether "charges" paid to COFACE is similar to payment of interest under Section 36(1)(iii) of the Income-tax Act, 1961 and, therefore, has to be allowed as deduction?

D 3. Regarding question No.(1), we may state that assessee had borrowed Rs.30 crores (approximately) from IDBI which in turn was refinanced by COFACE which foreign company had charged interest, commitment charges and insurance charges payable by the assessee. The said "commitment charges" was upfront payment. We have also examined the contract between IDBI and the assessee. In the case of **Addl. Commr. of Income-tax v. Akkamamba Textiles Ltd. – (1997) 227 ITR 464**, this Court has held that commission paid by the assessee to the banker and the insurance company was admissible deduction under Section 37 of the Income-tax Act, 1961. To the same effect is the judgment of this Court in the case **Commr. of Income-tax v. Sivakami Mills Ltd. – (1997) 227 ITR 465**. For the aforesaid reasons, we answer question No.(1) in favour of the assessee and against the Department. We may clarify that both the above judgments allows deductions under Section 37 of the 1961 Act and not under Section 36(1)(iii) of the 1961 Act. In this case, the Tribunal has allowed the claim under Section 37 and not under Section 36(1)(iii), hence there is no infirmity therein.

H 4. As regards question No.(2) is concerned it may be stated that the assessee established phosphoric Acid Project as an extension to its present business activities and for that purpose obtained foreign currency loan from IDBI which in turn

was refinanced by COFACE subject to the assessee paying finance charges to COFACE which according to the assessee was similar to payment of interest. The Department disallowed the said item on the ground that finance charges paid to COFACE on foreign currency loan was in the nature of interest and commitment charges and since the charges have been paid in relation to the project of manufacturing phosphoric acid which did not commence production during the assessment year under consideration, the expenses incurred were capital in nature. The Department also placed reliance in this connection on Explanation 8 to Section 43(1) of the Income-tax Act, 1961. On facts and circumstances of this case, once the Department equated the charges payable to COFACE with interest, our judgment in the case of **Dy. Commr. of Income Tax, Ahmedabad v. M/s. Core Health Care Ltd.** in Civil Appeal Nos.3952-55 of 2002 comes in. Accordingly, the said question No.(2) is also answered in favour of the assessee and against the Department.

5. Before concluding, we may also mention that in this case the finance charges paid by the assessee to COFACE have also been equated by the Department with commitment charges which, as stated above, are held to be revenue expenditure and deductible under Section 37 of the Income-tax Act, 1961 [See: **Akkamamba Textiles Ltd. (supra)** and **Sivakami Mills Ltd. (supra)**]. Therefore, on either counts the above question No.(2) is answered in favour of the assessee and against the Department.

6. For the aforestated reasons, the Department's civil appeals are accordingly dismissed with no order as to costs.

N.J.

Appeals dismissed.