

**IN THE HIGH COURT OF JUDICATURE AT BOMBAY
ORDINARY ORIGINAL CIVIL JURISDICTION**

WRIT PETITION (LODGING) NO. 770 OF 2013

HDFC Bank Limited

...Petitioner

vs.

The Assistant Commissioner of Income-tax 2(3) & Ors. ...Respondents

Mr.Jehangir D. Mistry, Senior Advocate with Mr.R. Murlidhar and Mr.Atul K. Jasani for Petitioner.

Mr.Suresh Kumar for Respondents.

**CORAM : DR.D.Y. CHANDRACHUD &
A.A. SAYED, JJ.**

APRIL 4, 2013

ORAL JUDGMENT (PER DR.D.Y. CHANDRACHUD, J.) :-

1 Rule; with the consent of Counsel for the parties returnable forthwith. With the consent of Counsel and at their request the Petition is taken up for hearing and final disposal.

2 The Petitioner is in challenge to an order of the Assistant Commissioner of Income Tax - 2(3), Mumbai dated 18 March 2013. By the impugned order, while disposing of an application for a stay of demand in the amount of Rs.1719.65 crores arising out of an order dated 31 January 2013 passed under Section 143(3) of the Income Tax Act, 1961, for Assessment Year

2010-11, the assessee has been called upon to deposit an amount of Rs.377.65 crores. This is apart from an adjustment which has been effected by the department in respect of two refunds respectively in the amount of Rs.49.56 crores payable to the assessee for Assessment Year 2008-09 pursuant to an order under Section 156 dated 28 February 2013 and an amount of Rs.518.30 crores payable for Assessment Year 2009-10 in pursuance of an order under Section 156 dated 4 March 2013.

3 An order of assessment has been passed for Assessment Year 2010-11 on 31 January 2013. The assessee has summarised the consequences of the order of assessment in paragraph 2 of the petition. The assessing officer has essentially made five disallowances, among others, which are as follows ;

- (i) Disallowance of broken period interest;
- (ii) Disallowance of amortisation of premium on Held-To-Maturity securities;
- (iii) Disallowance of exemption on dividend income from mutual fund units;
- (iv) Disallowance of interest under Section 36(1)(viia); and
- (v) Disallowance under Section 14(A).

4 The quantum of the disallowance and the tax and interest thereon are reflected in the following table which is extracted from the writ petition. The last column of the table contains the submissions of the Petitioner in respect of each item of disallowance.

Particulars	Amount of Disallowance (Rs.)	Tax and Interest thereon (Rs.)	Remarks
Disallowance of Broken period Interest	2649,26,00,000	1175,44,37,699	Covered by the Tribunal's judgement for A.Y. 2001-02 & 2002-03. Issue not even raised by the AO from A.Y. 2003-04 to 2008-09. In A.Y. 2009-10 CIT(A) has allowed the Petitioner's appeal.
Disallowance of Amortisation of premium on Held-To-Maturity securities	440,76,00,000	195,55,97,397	Covered by the Tribunal's judgement for A.Y. 2001-02 to 2007-08. In A.Y. 2008-09 & 2009-10 CIT(A) has allowed the Petitioner's appeal.
Disallowance of exemption on dividend income from mutual fund units	426,33,31,752	189,15,87,367	The Petitioner has now produced letters from all mutual funds that dividend distribution tax has been paid by them on dividends paid to the Petitioner. Accordingly, the reason given for denial of

			the exemption now has no basis.
Disallowance of Interest u/s 36(1)(viia)	351,06,96,982	155,76,52,664	No opportunity was given to the Petitioner to explain why the said branches are "rural branches". However, even assuming that some branches are not "rural" as alleged, a deduction of 7.5% of the total income has still to be granted u/s 36(1)(viia)
Disallowance u/s 14A	8,39,96,049	3,72,68,004	The Tribunal's judgement for the earlier (pre Rule 8D) years that no disallowance of interest can be made still holds good. Also, the law that s. 14A and Rule 8D do not apply to securities held as stock-in-trade means that no disallowance can be made.
TOTAL	3875,82,24,783	1719,6543,130	

The total disallowance on these five heads is Rs.3875.82 crores. The tax and interest payable thereon is Rs.1719.65 crores.

5 The contention of the assessee in respect of the disallowance for

the broken period interest is that the issue is covered in its favour for Assessment Years 2001-02 and 2002-03 by the decision of the Tribunal. Moreover, it has been submitted that the issue has not been raised by Assessing Officer for Assessment Years 2003-04 to 2008-09. In Assessment Year 2009-10, the Commissioner of Income Tax (Appeals) had allowed the appeal of the assessee.

6 In respect of the disallowance of amortization of premium, the assessee has stated that it is covered by the Tribunal's judgment for Assessment Years 2001-02 to 2007-08 and, for Assessment Years 2008-09 and 2009-10, the Commissioner of Income Tax (Appeals) had allowed its appeal.

7 On the aforesaid two items, the Assistant Commissioner of Income-tax in his impugned order dated 18 March 2013 held as follows :-

“ It is found that the issue of 'Broken period interest' and 'amortization of premium' are decided in assessee's favour by CIT(A) for AY 2009-10. The addition on these issues are made for AY 2010-11 as the department has not accepted the decision of the learned CIT(A) and is in appeal before the Hon'ble ITAT. Accordingly, the assessee will not be treated as assessee in default in respect the demand arising out of the said issues. However all refunds [both existing or arising subsequently] would be adjusted

against the demand arising out of these issues.”

8 The impugned order declining to grant a stay of recovery proceeds on the basis that, both on the issue of broken period interest and amortization of premium, there is a decision of the CIT (Appeals) in favour of the assessee for Assessment Year 2009-10. Yet what the department has done is to make an adjustment of the demand on these two grounds against the refunds which have been allowed to the assessee (both existing and subsequent). The impugned order suggests that in view of the fact that the issue is covered in favour of the assessee, it shall not be treated as an assessee in default in respect of the demand arising out of the two issues. An adjustment has been made only on the ground that the department is in appeal before the Tribunal for Assessment Year 2009-10. For Assessment Year 2008-2009, a refund of Rs.49.56 crores has been sanctioned to the assessee by an order dated 28 February 2013 under Section 156 (Exhibit - Q). Similarly for Assessment Year 2009-10, there is a refund of Rs.518.30 crores in favour of the assessee in pursuance of a notice under Section 156 dated 4 March 2013 (Exhibit – R). These refunds have been adjusted against the demand for Assessment Year 2010-11 even though the impugned order concedes that the issue is covered by a decision of the CIT (Appeals) in favour of the assessee.

9 The third item of disallowance is in respect of the exemption which was claimed by the assessee under Section 10(35A) from dividend income received from mutual fund units. The assessing officer made a disallowance on the ground that in order to avail of the exemption, the mutual fund must be registered with SEBI and the dividend which is distributed should suffer dividend distribution tax under Section 115R. A disallowance was made only on the ground that the assessee had not produced material to establish that dividend distribution tax had been paid by the mutual funds in question. On this aspect, the assessee has by its letter dated 15 March 2013 pointed out that Section 10(35D) does not require an assessee to establish that the mutual fund has paid dividend distribution tax. However, the assessee in this case has stated that it has obtained confirmation from the mutual funds to the effect that dividend distribution tax had been paid. The assessee stated that in a similar case in Assessment Year 2010-2011, where it had obtained confirmation letters, the assessing officer allowed the claim. Certificates issued by the mutual funds have been forwarded to the assessing officer on 18 March 2013 (Exhibit N).

10 The fourth item of disallowance is of interest under Section 36(1) (viiia). On this aspect, the total disallowance is Rs.351.06 crores on the ground

that the assessee had not established that the branches in question were 'rural branches'. The fifth and final disallowance is under Section 14A in the amount of Rs.8.39 crores.

11 There is merit in the submission which has been urged on behalf of the assessee by Learned Senior Counsel that the manner in which and the ground on which an adjustment of the refund was made is arbitrary and contrary to law. The impugned order dated 18 March 2013 accepts the position that both on the disallowance of broken period interest and the disallowance of amortisation of premium, there is a decision of the CIT (Appeals) in favour of the assessee. The impugned order, therefore, states that the assessee would not be treated as an assessee in default. Yet the department has proceeded to adjust the refund due and payable to the assessee of Rs.49.56 crores for Assessment Year 2008-09 and of Rs.518.30 crores for Assessment Year 2009-10 merely on the ground that the department has filed an appeal before the Tribunal against the decision of the CIT (Appeals). The adjustment of a refund is a mode of effecting recovery. Once an issue has been covered in favour of the assessee in respect of another assessment year on the same point, it was wholly arbitrary on the part of the department to proceed to make an adjustment of the refund. If the adjustment was not made, there can be no manner of doubt that the assessee

would have been entitled to a stay on the recovery of the demand. The demand cannot be adjusted by the department in this manner merely because it is in possession of the funds belonging to the assessee to which the assessee is legitimately entitled to and has been granted a refund for Assessment Years 2008-09 and 2009-10. The making of an adjustment in these facts is totally arbitrary and contrary to law. As a matter of fact, the assessee has contended that it was also governed by the order of the Tribunal on both the issues. Even this aspect has not been considered by the assessing officer.

12 Similarly, on the disallowance of the exemption on dividend income, the assessee under cover of its letters dated 15 and 18 March 2013 has produced certificates of confirmation from the mutual funds to the effect that dividend distribution tax has been paid. The assessing officer was apprised of the fact that in a similar situation for Assessment Year 2011-12, the claim of the assessee was allowed upon the production of confirmations from the mutual funds. Prima facie there was sufficient material before the assessing officer to indicate that the mutual funds which are registered with SEBI fall within the purview of Section 10(23D) and the assessee was entitled to an exemption under Section 10(35A).

13 Consequently, the assessee has made out a strong prima facie case for a stay of the recovery of the demand in respect of the aforesaid three items viz.; (i) Disallowance of broken period interest; (ii) Disallowance of amortization of premium, and (iii) Disallowance of exemption on dividend income from the mutual fund units. The recovery of the demand on these three heads has to be stayed in view of a strong prima facie case being made out. The balance due and payable by the assessee would work out to Rs.159.49 crores. The assessee has under cover of its letter dated 28 March 2013 paid an amount of Rs.100 crores under protest.

14 On these facts and for the reasons we have adduced earlier, we hold that the action of the department in adjusting the refunds due to the assessee in the amount of Rs.49.56 crores for Assessment Year 2008-09 and Rs.518.30 crores for Assessment Year 2009-10 was contrary to law. To recapitulate, the impugned order accepts the position that the assessee is covered by the decision of the Commissioner of Income-tax (Appeals) and hence directs that the assessee shall not be treated as assessee in default while at the same time making an adjustment of the refund.

15 In the circumstances, we are of the view that the interests of justice would be served if the department is permitted to make an adjustment to an extent of Rs.60 crores. The balance which is refundable, for Assessment Years 2008-09 and 2009-10 shall be refunded together with interest as admissible in accordance with law within a period of three weeks from the date on which an authenticated copy of this order is produced on the record.

16 Rule is made absolute in the aforesaid terms. There shall be no order as to costs.

(DR.D.Y. CHANDRACHUD, J.)

(A.A. SAYED, J.)