JUDICIAL UPDATE FOR MAY 2025 EXAMINATION

PAPER 4: DIRECT TAX LAWS & INTERNATIONAL TAXATION

1.	**Bank of Rajasthan Ltd. vs CIT [2024] 469 ITR 280 (SC)**	
	Issue	**Facts, Analysis and Decision**
	Whether the interest paid by the banks for broken period on purchase of securities can be claimed as revenue expenditure?	**Facts of the case:** In the present case, the assessee (a Scheduled Bank) involves in purchase and sale of government securities. It classified these securities as stock-in-trade in its books of account. The assessee consistently followed the method of setting off and netting the amount of interest paid by it on the purchase of securities [i.e., interest for the broken period ***(refer note below for the meaning of broken period)]*** against the interest recovered by it on the sale of securities and offering the net interest income to tax. This method was accepted in earlier assessments. However, the Commissioner of Income Tax (CIT) exercised revisional jurisdiction under section 263, holding that

		the broken period interest forms part of cost of acquisition and is not allowed as deduction. **Analysis and Decision:** The Apex Court noted that the banks are required to purchase Government securities to maintain the Statutory Liquidity Ratio. As per RBI's guidelines, there are three categories of securities: HTM (Held to Maturity), AFS (Available for Sale) and HFT (Held for Trading). As far as AFS and HFT are concerned, banks held such securities as stock-in-trade. Therefore, in these two categories of securities, the benefit of deduction of interest for the broken period will be available. The securities of the HTM category are usually held for a long term till their maturity. If it is found that HTM security is held as an investment, the benefit of broken period interest will not be available. Accordingly, the Apex Court held that as the securities were treated as stock-in-trade, the interest on the broken period cannot be considered as capital expenditure and will have to be treated as revenue expenditure, and thus allowed as deduction.

		Note - *When a Bank purchases a security on a date which falls between the dates on which the interest is payable on the security, the purchaser Bank, in addition to the price of the security, has to pay an amount equivalent to the interest accrued for the period from the last interest payment till the date of purchase. This interest is termed as the interest for the broken period.*
2.	**PCIT vs. Adadyn Technologies (P.) Ltd. [2024] 465 ITR 409 (SC)**	
	Issue	**Facts, Analysis and Decision**
	Whether the expenses incurred by the Assessee towards development of software for advertisement, which, due to technological development, had to be abandoned, can be claimed as revenue expenditure allowable?	**Facts of the case:** The assessee is a company engaged in the business of rendering customized internet advertising services to advertisers which could be used on the Desktop. In order to develop its software, assessee had incurred certain expenditure. Due to rapid change in the technology, the application sought to be developed by the assessee had become obsolete and the assessee abandoned further development. **Decision:** The High Court held that since the product having been abandoned, the assessee shall not get any enduring benefit. In substance, assessee has

		incurred expenditure in these two years to develop a software but due to change in technology, it had to abandon the product. In effect, it had lost money spent on this product. Accordingly, the High Court held that the assessee shall not get any enduring benefit and therefore, the expenditure was to be treated as revenue in nature. SLP filed by the revenue against impugned order of the High Court was dismissed by the Supreme Court.
3.	**Johnson Matthey Public Limited Company vs. CIT (International Taxation) (2024) 465 ITR 649 (Delhi)**	
	Issue	**Relevant provision of Law, Analysis and Decision**
	Whether the amount received as "Guarantee Fees" by a foreign company from its Indian subsidiaries fall within the definition of "interest"?	**Facts of the Case:** The assessee was a tax resident of the United Kingdom and engaged in manufacturing specialty chemicals. It entered into global corporate guarantee for the purpose of securing loans taken by its Indian subsidiaries from foreign banks. It received guarantee charges for extending such guarantee. **Relevant Provision:** As per section 2(28A), "interest" means interest payable in

		any manner in respect of any moneys borrowed or debt incurred (including a deposit, claim or other similar right or obligation) and includes any service fee or other charge in respect of the moneys borrowed or debt incurred or in respect of any credit facility which has not been utilized. Article 12(5) of India-UK DTAA defines "interest" to mean income from debt-claims of every kind, whether or not secured by mortgage and whether or not carrying a right to participate in the debtor's profits, and in particular, income from Government securities and income from bonds or debentures, including premiums and prizes attaching to such securities, bonds or debentures but, subject to the provisions of paragraph 9 of this Article, shall not include any item which is treated as a distribution under the provisions of Article 11(Dividends) of this Convention. **Analysis and Decision:** The High Court concur with the views of the Tribunal that the word "interest" as defined in Article 12(5) of the Treaty and section 2(28A) of the Act, shall be understood contextually.

		Article 12(5) of the DTAA and section 2(28A) of the Act extend the scope of such payments. However, payment or re-payment pursuant to any loan to be qualified as "interest", necessarily have to be within the context of loan and shall relate to the parties to the privity of contract. In this context only, the expressions "claims of any kind", "service fee or other charge" have to be understood. The word “interest” does not take into its fold any payments made to stranger to the privity of loan transactions, though such payments have to be made incidentally in relation to such loan. Undoubtedly, assessee is a stranger to the privity of loan transactions in as much as the contract of loan is a different from the contract of guarantee, as such in our considered opinion, the expression of "debt claims of any kind" or "the service fee or other charge in respect of moneys borrowed or debt incurred" does not stand extended to the payment of guarantee commission received by the assessee in India. The expression “interest” is defined to mean amounts payable in respect of any

		monies borrowed or debts incurred. Undisputedly the appellant had not borrowed any monies. The debt, if any, which could be said to have been incurred was clearly not one owed to the Indian subsidiaries. The income that it received from its Indian subsidiaries was solely in consideration of any liability that could possibly befall in case its Indian subsidiaries were to default in their repayment obligations. Accordingly, the High Court held that the guarantee fee would neither fall within the ambit of Article 12 of India-UK DTAA nor section 2(28A) of the Act.