

**(2012) 12 AP CK 0012**

**Andhra Pradesh High Court**

**Case No:** RC No. 58 of 1997

Novopan India Ltd.

APPELLANT

Vs

The Commissioner of Income  
Tax, A.P. Hyderabad and others

RESPONDENT

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**Date of Decision:** Dec. 31, 2012

**Acts Referred:**

- Income Tax Act, 1961 - Section 10(2)(xv), 143(3), 256(1), 30, 31

**Citation:** (2013) 356 ITR 580

**Hon'ble Judges:** M.S. Ramachandra Rao, J; Goda Raghuram, J

**Bench:** Division Bench

**Final Decision:** Allowed

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### **Judgement**

@JUDGMENTTAG-ORDER

M.S. Ramachandra Rao, J.

This Reference has been made by the Income Tax Appellate Tribunal, Hyderabad-A Bench, Hyderabad u/s 256(1) of the Income Tax Act, 1961 (for short "the Act") for the opinion of this Court on the following question of law arising out of its order dated 13.10.1995 in ITA No. 687/Hyd/91 for the assessment year 1985-86 i.e. "Whether on the facts and in the circumstances of the case, the Hon'ble Income Tax Appellate Tribunal, Hyderabad is correct in holding that the daily allowance paid to the employees would partake the character of hotel expenses for the purpose of disallowance u/s 37(3-A) to (3D)?". The assessee M/s. Novopan India Limited, Hyderabad is engaged in the manufacture and sale of plain and laminated particle boards etc. For the assessment year 1985-86, it filed return declaring "nil" income on 30.9.1985.

2. The assessing officer, while completing the assessment u/s 143(3) of the Act, disallowed an amount of Rs. 1,08,915/- representing daily allowance paid to the employees of the assessee u/s 37(3A) to (3D) on the ground that the "daily

allowance" paid to the employees has to be treated similar to "payments to hotels".

3. On appeal, the CIT (Appeals) confirmed the disallowance by order dated 22.1.1991. However, he held that the hotel expenses of Rs. 5,10,899/- included daily allowance of Rs. 1,09,815/- paid to the employees. Therefore he directed that the total hotel expenses should be taken at Rs. 5,10,899/- minus Rs. 1,09,815/- = Rs. 4,01,984/- as against Rs. 5,10,899/- adopted by the assessing authority in the assessment order. But he rejected the contention of the assessee that the daily allowance paid to employees has to be meted out a separate treatment as distinct from payments to hotels on the ground that such daily allowances paid to the employees were meant to take care of their traveling expenses on tour including boarding and lodging. Therefore he confirmed the assessing officer's treatment of "daily allowances" as falling in the same category as "payments to hotels".

4. Aggrieved by the later portion of the order of CIT (Appeals), as mentioned above, the assessee filed ITA No. 687/Hyd/91 to the Income Tax Appellate Tribunal, Hyderabad A Bench, Hyderabad. By order dated 13.10.1995, the said appeal was dismissed holding that the CIT (Appeals) was right in treating such daily allowances paid to the employees as similar to payment to hotels and that even the travel policy manual filed before the Tribunal supports the said conclusion.

5. However, on an application u/s 256(1) of the Act filed by the assessee, the Tribunal felt that a referable question of law as set out above arose out of its order and therefore made the reference. The said reference has been numbered as RC No. 58 of 1997.

6. Heard Sri. Shravan Kumar, learned counsel representing Sri. C. Kodanda Ram, learned Senior Counsel appearing for the petitioner and Sri. S.R. Ashok, learned Senior Standing Counsel for the Revenue.

7. Sri. Shravan Kumar, counsel for the petitioner contended that daily allowances paid by the assessee to its employees is distinct in character from hotel expenses and such daily allowances also should be disallowed in terms of section 37(3A) to (3D) of the Act; that such expenditure incurred by the assessee is an expenditure incurred in respect of "business carried on by the assessee" and therefore is liable to be disallowed u/s 37(3A) to (3D) of the Act; and that the Supreme Court in [Travancore Titanium Products Ltd. Vs. Commissioner of Income Tax, Kerala](#), while considering section 10(2)(xv) of the Act has held that to be a permissible deduction, it is sufficient if there is a direct and intimate connection between the expenditure and the business; it must be incidental to the business and must be necessitated or justified by commercial expediency; and therefore the subject allowances should also have been treated separately from hotel expenses and disallowed u/s 37(3A) to (3D) of the Act.

8. Sri. S.R. Ashok, learned Senior Counsel appearing supports the decision of the CIT (Appeals) and of the ITAT and contends that they have rightly treated daily

allowances paid to the employees as similar to hotel expenses.

9. We have considered the respective submissions.

10. The subject assessment year is 1985-86 corresponding to the previous year 1984-85. With effect from 1.4.1984, the Finance Act, 1983 introduced sub sections (3A) to (3D) to Section 37 of the Act Sub sections (3A) to (3D) of Section 37 were omitted by the Finance Act, 1985 with effect from 1.4.1986.. Thus, at the relevant time, the provision read as follows:

Section 37: General:

(1) Any expenditure (not being expenditure of the nature described in sections 30 to 36 and section 80vv and not being in the nature of capital expenditure or personal expenses of the assessee), laid out or expended wholly and exclusively for the purposes of the business or profession shall be allowed in computing the income chargeable under the head "profits and gains of business or profession".

(2) ....

(3A) Notwithstanding anything contained in sub-section(1), where the expenditure or, as the case may be, the aggregate expenditure incurred by an assessee on any one or more of the items specified in sub-section (3B) exceeds one hundred thousand rupees, twenty per cent of such excess shall not be allowed as deduction in computing the income chargeable under the head "Profits and gains of business or profession".

(3B) The expenditure referred to in sub-section (3A) is that incurred on -

- (i) advertisement, publicity and sales promotion; or
- (ii) running and maintenance of aircraft and motor cars; or
- (iii) payments made to hotels

Explanation - For the purpose of sub-sections (3A) and (3B), -

(a) the expenditure specified in clause (i) to clause (iii) of sub-section (3B) shall be the aggregate amount of expenditure incurred by the assessee as reduced by so much of such expenditure as is not allowed under any other provision of this Act;

(b) expenditure on advertisement, publicity and sales promotion shall not include remuneration paid to employees of the assessee engaged in one or more of the said activities;

(c) expenditure on running and maintenance of aircraft and motor cars shall include -

(i) expenditure incurred on chartering any aircraft and expenditure on hire charges for engaging cars plied for hire;

(ii) conveyance allowance paid to employees and, where the assessee is a company, conveyance allowance paid to its directors also.

(3C) Nothing contained in sub-section (3A) shall apply in respect of expenditure incurred by an assessee, being a domestic company as defined in clause (2) of section 80B, or a person (other than a company) who is resident in India in respect of expenditure incurred wholly and exclusively on -

(i) advertisement, publicity and sales promotion outside India in respect of the goods, services or facilities which the assessee deals in or provides in the course of his business;

Running and maintenance of motor cars in any branch, office or agency maintained outside India for the promotion of the sale outside India of such goods, services or facilities.

(3D) No disallowance under sub-section (3A) shall be made -

(i) in the case of an assessee engaged in the business of operation of aircraft, in respect of expenditure incurred on running and maintenance of such aircraft;

(ii) in the case of an assessee engaged in the business of running motor cars on hire, in respect of expenditure incurred in running and maintenance of such motor cars.

11. A reading of the above provision indicates that where the expenditure or as the case may be, the aggregate expenditure incurred by an assessee on any one or more of the following, i.e. (i) advertisement, publicity, sales promotion (ii) running and maintenance of air craft and motor cars and (iii) payments made to hotels exceeds Rs. 1,00,000/-, 20% of such excess shall not be allowed as deduction in computing the income chargeable under the head "profits and gains of business or profession".

12. Sub Rule (1) of Rule 6 D of the Income Tax Rules, 1962 deals with expenditure incurred by an assessee in connection with traveling by an employee or any other person out side India. We are not concerned with this here. But Sub Rule (2) deals with such expenditure incurred within India, which states as follows:

S.6-D (2): The allowance in respect of expenditure incurred by an assessee in connection with traveling by an employee or any other person within India outside the headquarters of such employee or other person for the purposes of the business or profession of the assessee shall not exceed the aggregate of the amounts computed as hereunder: (a) in respect of travel by rail, road, waterway or air, the expenditure actually incurred; (b) in respect of any other expenditure (including hotel expenses or allowances paid) in connection with such travel, an amount calculated at the following rates for the period spent outside such headquarters; (i) in respect of an employee whose salary is Rs. 1,000 per month or more Rs. 100 per day or part thereof; (ii) in respect of any other employee Rs. 50 per

day or part thereof; (iii) in respect of any other person an amount calculated at the rates applicable in the case of the highest paid employee of the assessee:

Provided that, if the stay of such employee or other person outside his headquarters is at Bombay, Calcutta or Delhi, the amount computed at the aforesaid rate shall be increased by a sum equal to fifty percent of such amount:

Provided further that in a case where such employee or other person on any day of his stay outside his headquarters, stays free of charge in a guest house maintained by the assessee, the amount under this clause shall be calculated at one-third of the aforesaid rates and where the employee or such other person is provided lodging only free of charge, at one-half of the aforesaid rates.

13. Thus Rule 6-D (2) (b) of the rules clearly treats "hotel expenses" and "allowances paid to the employees" similarly and does not treat them distinctly. Therefore, the contention of the assessee that daily allowances paid to the employees u/s 37(3A) to (3D) should be treated separately as distinct from payments to hotels, cannot be accepted. Therefore, we answer the reference in question in the affirmative and hold that the Tribunal was correct in treating the daily allowance paid to employees of the assessee as having the same character as hotel expenses for the purpose of disallowance u/s 37(3A) to (3D) of the Act.

14. As regards the contention of the assessee that such daily allowance is an expenditure incurred in the year of account in respect of the business carried on by the assessee; that it being wholly and exclusively expended for the purpose of the business and is incidental to the business; that it has a direct and intimate connection with the business and therefore should be disallowed u/s 37(3A) to (3D) of the Act is concerned, we hold that the said issue is not the subject matter of the reference to this Court, and as such, we decline to express any opinion on it. The reference is answered as above.