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# M/s Essar Shipping Limited v. Commissioner of Income Tax, City III, Mumbai

**Citation:** (2020) 317 CTR (Bom) 25; (2020) 426 ITR 220 (Bom)

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## ABSTRACT

*Over the course of time, Indian Courts are proving to be an essential pillar in modelling the tax laws in the Country. Determination of taxable income is perhaps the primary step that any assessment authority will have to undertake to assess the amount of tax. Section 2(24) of the Act attempts to define the term 'Income'. Section 28(iv) takes into consideration the nexus between the business or profession, and the receipt is considered as an income chargeable to tax.*

*A peculiar scenario that emerged in the light of the above-stated provision was whether the waiver of loan granted to any particular entity carrying out business or profession could be classified as an income chargeable to tax under Section 28(iv). The Supreme Court, in the case of CIT v. Mahindra and Mahindra, ruled that waiver of a loan is not a chargeable income under Section 28(iv).*

*It is to be noted that, although the Supreme Court laid down the above-stated rule in the Mahindra Case, the Bombay High Court in Essar Shipping Ltd has dissected the judgment of the Apex Court and has substantially focussed on its applicability by comparing it with other decisions of High Courts and the Supreme Court, to the extent of overruling one of its earlier judgments. Therefore, the current position of law, including a cumulative understanding of the stand of the Apex Court in various cases in this regard, can significantly be studied by an analysis of the judgment of the Bombay High Court in the case of M/s Essar Shipping Ltd v. CIT*

**Keywords:** *Section 28(iv) of Income Tax Act, Waiver of Loan, Chargeable Income, Subsidy, Benefit, Perquisite.*

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## I. FACTS

### (A) Background

The Appellant is a residential company being assessed as per the Act. It was originally named M/s Karnataka Shipping Corporation Ltd, carrying shipping business. Subsequently, due to the advancements in the relevant previous years, the company amalgamated with Essar Shipping Ltd, Madras, whereafter, it came to be referred to as 'M/s Essar Shipping Ltd'.

### (B) Relevant facts

During the assessment proceedings for the assessment year 1984-85, subsequent to the amalgamation, the appellant assessee filed a revised return of income wherein Rs.2,52,00,000/- was claimed as a deduction for the loan amount given by Karnataka Government, which was later waived, thereby making the amount irrecoverable.

However, the Assessing Officer denied this claim by an order dated 27/03/1987, on the grounds that the loan amount given by the Karnataka Government was essential as a benefit for the Appellant to carry out his business activities, thereby constituting a chargeable income under Section 28 of the Income Tax Act, and accordingly, it should be added as a total income of the assessee.

### (C) Judicial Treatment

Aggrieved by order of the AO, the assessee preferred an appeal before the Commissioner of Income Tax, Appeals-III, Bangalore, who was the first appellate authority in the instant case. It analysed the requirements of Section 28(iv) of the Act and observed that it includes benefits other than in the form of cash. It was held that waiver of the loan amount could not be included as a taxable income, as it would constitute a cash benefit, i.e., it is of capital nature and therefore cannot be included as a prerequisite or benefit under Section 28(iv).

The matter was further appealed to the Income Tax Appellate Tribunal. The tribunal observed that the waived loan amount was inextricably connected with the business of the assessee, and thus it has to be considered as a benefit arising out of business. It was not the loan but the waiver of the loan that was the benefit enjoyed by the assessee, and therefore it cannot be stated that the assessee received cash benefit. Thus, the tribunal set aside the findings of the first appellate authority and upheld the addition of waived amount in the total income of the assessee by the AO by relying upon the decision of *Sahney Steel and Press Works Ltd v. CIT*

Hence, the assessee preferred an appeal before the High Court of Bombay under Section 260A of the Act.

## II. RELEVANT PROVISION OF LAW

Section 28(iv) of the Act is essential in the instant case. According to Section 28(iv):

*“Profits and gains of business or profession.*

28. The following income shall be chargeable to income-tax under the head “Profits and gains of business or profession:-

*(iv) the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession.”*

## III. ISSUES

1. Whether on the facts and in the circumstances of the case and in law, provisions of Section 28(iv) of the Act are attracted where alleged benefit or perquisite is other than cash?
2. Whether the facts of the instant case resonate with that of the *Mahindra and Mahindra Ltd case*?
3. Whether the waived amount of loan partakes the character of an operational subsidy?

## IV. CONTENTIONS

### (A) Appellant’s Contention

The Appellant’s contention can be summarised into three major points:

- i. Benefits and perquisites of business and profession u/s 28(iv) should be other than in the form of cash. The primary contention on behalf of the Appellant was that Section 28(iv) of the Act deals with benefit or perquisite arising out of business or profession, and it does not include any such benefit or perquisite in the form of cash. Waiver of loan, however, is cash benefit and thus, cannot be covered within the ambit of Section 28(iv)
- ii. Such benefits and perquisites u/s 28(iv) should be the ones arising out of such business or profession. The Apex Court in *CIT v. Mahindra and Mahindra* conclusively held that taxable income under Section 28(iv) includes those benefits and perquisites that are only arising out of business or profession, in any form other than cash.
- iii. Reliance on the case of *Sahney Steels and Press Works Ltd v. CIT* by the revenue before the tribunal is totally misplaced

It was also argued that the reliance placed by the revenue on the ruling of the Apex Court in *Sahney Steels and Press Works Ltd v. CIT* case could not be applied in the instant case, whereas the ruling in *Mahindra and Mahindra Ltd* will have to be applied. This was essential because *Sahney Steels case* dealt with whether the subsidy obtained by the assessee from the government can be taxed, which is not the question of law in the instant case.

### **(B) By the Revenue**

The arguments of the revenue can be summarised as follows:

- i. The waiver of a loan is not a cash benefit, and such is enjoyed as a direct consequence of business of the assessee, and therefore, it is taxable u/s 28(iv) of the Act.
- ii. It was argued on behalf of the revenue that when a loan gets waived, it attains the character of an 'operational subsidy'. Emphasis was laid on the term 'Operational' to contend that, when the Karnataka government waived the loan of the assessee, it was an act of providing an operational subsidy to help the assessee to overcome its losses to the extent of loan amount waived. In this context, reliance was placed on *Sahney Steels and Press Works Ltd v. CIT*.<sup>2</sup>
- iii. It was further argued that the factual matrix of *CIT v. Mahindra and Mahindra* cannot be applied to the instant case. Rather, the case of *Protos Engineering Company Private Limited v. CIT*<sup>3</sup>, wherein the Bombay High Court declared the waiver of loan to be a taxable income, was relied upon by stating that the facts of the former are identical to that of the instant case.

## **V. JUDGMENT AND OBSERVATION**

The Judgment of the High Court of Bombay can be divided into three folds

*First*, the Court analysed the ingredients of Section 28(iv) of the Act and pronounced that for any benefit or prerequisite to be considered as a taxable income under Section 28, it should be in any form other than cash, and such benefit or prerequisite should be arising out of the course of business or profession.

*Second*, the High Court compared the factual matrix of the *Mahindra and Mahindra Ltd case*, wherein the Supreme Court had to examine whether the loan amount borrowed by Mahindra and Mahindra, when waived by the lender, can be considered as a benefit or prerequisite under Section 28(iv). It was then held that "*The term "loan" generally refers to borrowing*

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<sup>2</sup> Sahney Steels & Press Works Limited v. CIT, AIR 1997 SC 3968

<sup>3</sup> Protos Engineering Company Private Limited v. CIT, [ 1995 ] 211 ITR 919 ( Bom )

something, especially a sum of cash that is to be paid back along with interest decided mutually by the parties”, and the ‘Right to waiver’ of the lender was also acknowledged. The Supreme Court then proceeded to declare that the amount given as a loan, when waived, is received as cash receipt, thereby failing to satisfy the requirement of Section 28(iv).

The High Court of Bombay, upon referring to the above-stated ruling of the Top Court, declared that the factual matrix of the instant case is identical to that of the case of *CIT v. Mahindra and Mahindra Ltd*, and the ruling propounded by the Apex Court squarely applies to the instant case as well.

Thus it held that the waiver of the loan amount could not be considered as a benefit or perquisite that is taxable under Section 28(iv) of the Act. In furtherance of this proposition, the High Court overruled its earlier judgment in *Protos Engineering Company Private Limited v. CIT* on the grounds that it violated the proposition laid down by the Apex Court in the *Mahindra and Mahindra Ltd case*.

Third, the Court differentiated between the terms ‘Loan’ and ‘Subsidy’ and distinguished the ruling laid down in *Sahney Steels and Press Works Ltd. v. CIT*. The Court observed that in the *Sahney Steels case*, the facts were with respect to subsidy received by the assessee from the Andhra Pradesh government, which was subsequently waived, and the question before the Court was whether such subsidy received was taxable as revenue receipt or not.

In the instant case, the contention that the amount of loan waived partakes the character of operational subsidy was rejected by the Court. The Court differentiated that loan and subsidy are two different concepts and cannot be equated. ‘Loan’ refers to borrowed money that has to be repaid back with interest, whereas ‘Subsidy’ refers to money paid as a grant in furtherance of public interest, and it need not be repaid. The Court conclusively declared that a loan can be waived off for various reasons and cannot partake the character of a subsidy, and thus the ruling laid down in *Sahney Steels and Press Works Ltd v. CIT* does not apply in the instant case.

Ultimately, the Court ruled in favour of the assessee appellant and held that waiver of loan cannot be brought to tax under Section 28(iv) of the Act.

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