



**In case of a General Insurance Company, expenditure in relation to the exempt income cannot be disallowed under section 14A because its income would be computed under the specific provisions of section 44 read with the First Schedule of the Act.**

### Background

The Delhi Bench of the Income Tax Appellate Tribunal (the Tribunal) has recently in the case of Oriental Insurance Company Limited<sup>1</sup> *inter alia* held that no expenditure can be disallowed in relation to the exempt income under the provisions of section 14A of the Income-tax Act, 1961 (the Act) because the income of a General Insurance Company would be computed in accordance with specific provisions of section 44 read with the First Schedule of the Act.

### Facts of the case

- The taxpayer, a General Insurance Company, had earned certain exempt income during the relevant year.
- The tax department had disallowed 50 percent of the management expenditure incurred by applying the provisions of section 14A of the Act. The tax department held that the investments made by the taxpayer generate both taxable and tax-free income and that since section 14A has been introduced with a retrospective effect (from 1 April 1962), the same would be applicable to the taxpayer

### Taxpayer's contentions

- The taxpayer contended that income of an Insurance Company would be governed by the provisions of section 44 of the Act read with Rule 5 of the First Schedule and that the business income

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<sup>1</sup> *Oriental Insurance Company Limited v Asstt Commissioner of Income tax (ITA No. 5462 & 5463/D/03), dated 27 February 2009 (Delhi)*

related provisions under section 28 to 43B do not apply to an Insurance Company

- The two presumptions that follow on a combined reading of relevant provisions of the Act<sup>2</sup> are as follows:
  - No head-wise bifurcation is called for while computing the income for an Insurance Company. The income, inter alia, of the business of insurance is essentially, profits disclosed by the annual accounts as furnished to the controller of Insurance under the Insurance Act, 1938, subject to certain adjustments to be made thereunder. The adjustments do not refer to any disallowance to be made under section 14A of the Act.
  - Profits and Gains of business as referred to above have only to be computed in accordance with Rule 5 of the First Schedule.

#### **Tribunal's ruling**

- The Tribunal upheld the taxpayer's contention that computation of profits and gains of insurance business would have to be computed in accordance with Rule 5 of the First Schedule. In view of section 44 having a non-obstante clause, the tax department is not permitted to travel beyond these provisions.
- Section 14A contemplates an exception for deductions as allowable under the Act (sections 28 to 43B of the Act). Section 44 creates a special application of these provisions in the cases of insurance companies.

The Tribunal also dealt with various other issues and held as follows:

<b>Issues</b>	<b>Held by the Tribunal</b>
Disallowance of Investments written off	Based on earlier years order, held in favour of the taxpayer
Disallowance of Guest House expenditure	Based on earlier years order, held in favour of the taxpayer
Addition on account of interest not being accrued on bonds and debentures, recovery of which is outstanding	Based on earlier years order, held in favour of the taxpayer
Disallowance of Provisions made	Based on earlier years order, held in favour of the taxpayer
Depreciation on additions to fixed assets	Since details of additions made to the block of assets were not provided, this was held against the taxpayer
Provision for Unidentified Third Party Claim	Based on earlier years order, held against the taxpayer

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<sup>2</sup> Section 14,14A, 44 and Rule 5 of the First Schedule of the Act

## **Our Comments**

This decision will provide a great relief to all insurance companies since investment is an integral part of the business of insurance companies. Though the decision is in the case of a General Insurance Company, it may equally apply to Life Insurance Companies also.

It is noted that the Bomaby High Court in the case of Life Insurance Corporation of India<sup>3</sup> has held that while computing business income, specific provisions of Section 44 pertaining to Insurance companies, will override only sections 28 to 43B of the Act. However, all the other provisions like section 10, section 79, etc. would be applicable to Insurance Companies. In view of the above decision, it would be interesting to observe how courts will look at this matter when it will reach at a higher level.

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<sup>3</sup> Life Insurance Corporation of India v. CIT [1978] 115 ITR 45 (Bom)

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