



Global Business Tax Alert

Delivering Clarity

Payment made by bank for compensating client's loss to safeguard bank reputation/goodwill, is an allowable expense

Issue no: GBT/03/2019

In this issue:

[Facts of the case](#)
[Issues under consideration](#)
[Ruling of the High Court](#)
[Conclusion](#)
[Deloitte tax@hand App](#)
[Do you know about Dbriefs?](#)

Facts of the case

- M/s Hong Kong and Shanghai Banking Corporation Ltd. (taxpayer or the company) is a bank. In the tax return for the FY 1999-00, the taxpayer claimed loss amounting to INR 35,000,000.
- The taxpayer acted as a mediator and performed several functions on behalf of its client, such as:
 - Hold securities,
 - Collect dividends,
 - Obtain deliveries,
 - Ensure transfer in the name of the client and
 - Deliver the securities when the same are sold by clients.
- One of the clients, Capital Emerging Growth Fund (EMGF) had purchased shares of Zee Telefilms Limited (Zee). These shares were duly registered in the name of EMGF.
- However, subsequently Jas One Diamonds Pvt. Ltd. (Jas One) filed a suit in the Bombay High Court claiming that they sent these shares for registration. However the shares were subsequently stolen and circulated in the market.
- On account of above dispute, the client (i.e. EMGF) and its Global Custodian suffered a loss amounting to INR 35,000,000.
- The company agreed to compensate a sum of INR 35,000,000 by way of loss for maintaining relations with customers in question and to safeguard the bank's interest / goodwill.
- The Assessing Officer (AO) did not allow the deduction of the above loss during the assessment proceedings of HSBC. However, the first appellate authority allowed the above claim. The revenue filed the appeal with a higher forum.
- The Hon'ble Income Tax Appellate Tribunal (ITAT) allowed the appeal in favour of the HSBC. Aggrieved by the order of ITAT, the revenue filed the appeal before the Jurisdictional High Court.

Issues under consideration

Whether disallowance of loss, which was borne by HSBC to safeguard its interest and reputation, is correct given the fact that there was no contractual liability?

Ruling of the High Court

- While analysing the issue, the HC relied on the apex court ruling in case of **Nainital Bank Ltd (1966) [62 ITR 638](SC)** which was also referred to by the ITAT while deleting the addition.

- In the aforesaid ruling of apex court, it was held that the credit of a banking business is very sensitive. It largely thrives on the confidence which its constituents have in its management. To maintain such confidence, the management had to make concessions to preserve the goodwill and relations with its clients. Under such circumstances, the expenditure was allowed.
- In the instant case, the HC noted that that the client of the taxpayer was a regular client and to maintain dignity in the market, despite no contractual obligation, the assessee had made such payment.
- Thus, such loss should be allowed as business expenditure under section 37 of the Act.

Conclusion

The Honourable High Court has held that a payment made by the bank to a client for safeguarding its reputation is an allowable expense. Accordingly, the Hon'ble High Court has affirmed the deletion of the additions made by the AO and dismissed the Revenue's appeal.

Deloitte tax@hand App

Current. Comprehensive. Convenient.

Download [tax@hand](#) app, a secure digital platform for timely global and regional news, perspectives, and resources. Do visit the tax@hand webpage [here](#).



Deloitte.

IOS

Download from App Store

Android

Download from Google Play

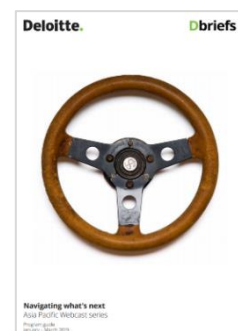
Website

Add to favorites

Do you know about Dbriefs?

Dbriefs are live webcasts that give valuable insights on important developments affecting your business. To register, visit the [Dbriefs](#) page.

Download the report





Deloitte makes an impact that matters

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. Please see www.deloitte.com/about for a more detailed description of DTTL and its member firms.

This material and the information contained herein prepared by Deloitte Touche Tohmatsu India LLP (DTTI LLP) is intended to provide general information on a particular subject or subjects and is not an exhaustive treatment of such subject(s). This material contains information sourced from third party sites (external sites).

DTTI LLP is not responsible for any loss whatsoever caused due to reliance placed on information sourced from such external sites. None of DTTI LLP, Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network") is, by means of this material, rendering professional advice or services. This information is not intended to be relied upon as the sole basis for any decision which may affect you or your business. Before making any decision or taking any action that might affect your personal finances or business, you should consult a qualified professional adviser.

No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this material.

©2019 Deloitte Touche Tohmatsu India LLP. Member of Deloitte Touche Tohmatsu Limited