

FAQs on Notification No. 38/2025 [F. No 370142/11/2025-TPL] / SO 1838(E)

Q1. What is section 37 of the Income-tax Act, 1961 ('the Act')?

Ans. Section 37 of the Act provides for allowability of expenditure laid out or expended wholly and exclusively for the purpose of business or profession.

Q2. What is *Explanation 1* of sub-section (1) of section 37 of the Act and its relation with *Explanation 3* thereof ?

Ans. *Explanation 1* of sub-section (1) of section 37 provides that any expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law shall not be deemed to have been incurred for the purpose of business or profession and consequently, no deduction or allowance can be claimed for such expenditure.

Further, *Explanation 3* of section 37 clarifies the term “expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law”

Q3. What is the amendment made in *Explanation 3* vide Finance (no. 2) Act, 2024?

Ans. *Explanation 3* to sub-section (1) of section 37 of the Act was amended vide Finance no. 2 Act, 2024 to clarify that the term “expenditure incurred by an assessee for any purpose which is an offence or which is prohibited by law” will also include any expenditure incurred by an assessee to settle proceedings initiated in relation to a contravention under any law for the time being in force, as may be notified by the Central Government in the Official Gazette in this behalf.

Q4. Which laws been notified under the amended *Explanation 3*?

Ans. Vide CBDT Notification no. 38/2025 dated 23.4.2025 it has been provided that any expenditure incurred to settle proceedings initiated in relation to contravention or defaults under the following laws shall not be deemed to have been incurred for the purpose of business or profession –

- (i) the Securities and Exchange Board of India Act, 1992 (15 of 1992)
- (ii) the Securities Contracts (Regulation) Act, 1956 [42 of 1956]
- (iii) the Depositories Act, 1996 [22 of 1996]
- (iv) the Competition Act, 2002 [12 of 2003].

Q5. What are the implications of this notification?

Ans. Any expenditure incurred by an assessee for settlement of proceedings initiated in relation to contravention or defaults under the abovementioned laws cannot be claimed as a deduction or allowance under the Income tax Act from AY 2025-26 onwards.

Form no. 3CD of the Income-tax Rules, 1962 has also been amended by CBDT Notification no. 23/2025 dated 28.3.2025 to capture details pertaining to such expenses.

Q6. From when has the amendment been made effective?

Ans. This amendment is effective from 1st day of April, 2025 and shall accordingly apply from Assessment Year 2025-26 onwards.