IN THE INCOME TAX APPELLATE TRIBUNAL
DELHI BENCHES: 'B', NEW DELHI

BEFORE SHRI N.K.BILLAIYA, ACCOUNTANT MEMBER
AND SMT. BEENA A PILLAI, JUDICIAL MEMBER

ITA No. 4673/Del/2005
AY: 2002-03

M/s Escorts Ltd. 11, Scindia House, C.P. New Delhi 110 001 PAN: AAACE0074B	**vs**.	ACIT Range 11 New Delhi

ITA No. 84/Del/2006
AY: 2002-03

DCIT Central Circle 3 New Delhi	**vs**.	M/s Escorts Ltd. 11, Scindia House, C.P. New Delhi 110 001 PAN: AAACE0074B

ITA No 2350/Del/2010
AY: 2003-04

DCIT Central Circle 3 New Delhi	**vs**.	M/s Escorts Ltd. 11, Scindia House, C.P. New Delhi 110 001 PAN: AAACE0074B

&

ITA No. 5408/Del/2014
AY: 2005-06

DCIT Central Circle 11 (1) New Delhi	**vs**.	M/s Escorts Ltd. 11, Scindia House, C.P. New Delhi 110 001 PAN: AAACE0074B

(Appellant) **(Respondent)**

Department by : Ms. Nidhi Srivastava, CIT, D.R.
Assessee by : : Sh. R.M.Mehta, Adv.
Date of Hearing : 12/02/2019
Date of Pronouncement: 06/03/2019

ORDER

PER BEENA A PILLAI, JUDICIAL MEMBER

Present Cross Appeals for Assessment Year (A.Y.) 2002-03 and appeals by Revenue for Assessment Year 2003-04 and 2005-06 have been preferred against following impugned order:

S.No.	Assessment Year	Date of impugned order	Passed By
1.	2002-03	31/10/05	CIT(A)-14
2.	2003-04	02/03/10	CIT(A)-3
3.	2005-06	30/06/14	CIT(A)-20

For the sake of convenience we shall first take up Cross Appeals filed by assessee as well as revenue for A.Y. 2002-03.

2. A.Y:2002-03

Brief facts of the case are as under:

Assessee is a company and filed its return of income on 31/10/02 declaring business loss of Rs. 53,21,28,126/-and income from capital gain amounting to Rs.5,48,47,495/-. The case was processed under section 143(1) of the Income Tax Act, 1961 (the Act) and subsequently selected for scrutiny. Accordingly notice under section 143(2) of the Act was issued. In response to statutory

notices, representative of assessee appeared before Ld. AO and case was discussed.

2.1.Ld.AO observed that assessee is engaged in business of manufacturing and sale of tractors, shockers, railway equipment etc. and other trading activity.

2.2. After calling for various details and information and considering the same, Ld. AO made following additions in hands of assessee:

Sl. No.	*Additions made*	*Amount-Rs.*	*Amount-Rs*
1.	*Premium on SPNs*		*22,54,277/-*
2.	*Upfront fee*		*3,69,25,000/-*
3.	*Prototype development*		*78,56,810/-*
4.	*Cost of software* *Less: Depreciation*	*699,38,000/-* *41,62,800/-*	*27,75,200/-*
5.	*Prior Period expenses*		*4,89,44,610/-*
6.	*Unutilised MODVAT credit*		*1,75,00,000/-*
7.	*Commission & discount*		*1,18,94,891/-*
8.	*Interest expenses*		*16,55,00,000/-*
9.	*Expenses attributable u/s 14A*		*2,19,36,390/-*
10.	*Interest free loan*		*4,56,00,000/-*
11.	*Write off of inventory*		*4,73,69,355/-*

12.	*Loss on diminution of assets*		*28,56,250/-*
	T o t a l additions made:		*41,14,12,783/-*

2.3. Aggrieved by additions made by Ld.AO assessee preferred appeal before Ld.CIT(A) who partly deleted additions.

2.4. Aggrieved by order of Ld. CIT (A) revenue as well as assessee are in appeal before us now.

3. Following grounds have been raised by assessee against impugned order passed by Ld.CIT(A)-14, vide order dated 31/10/05 for year under consideration:

ITA No. 4673/Del/2005 (Assessee's appeal)

1. That the impugned order passed by the Ld.CIT(A) is bad in law and wrong on facts.

2. That on the facts, circumstances and legal position of the case, the Ld.CIT(A) has erred in law in holding that the software expenses amounting to Rs.69,38,000/- are in the nature of capital expenditure instead of revenue as claimed by the appellant.

3. That on the facts, circumstances and legal position of the case, the Ld.CIT(A) has erred in law in upholding the disallowance of Rs.4,59,928/- on account of prior period expenses.

4.(a) That on the facts, circumstances and legal position of the case, the Ld.CIT(A) has erred in law in confirming following disallowances made u/s 14A of I.T.Act being alleged expenditure apportioned for earning the dividend and interest income claimed to be exempt u/s 10(33) & 10(23G) of the Act respectively:-

i. Interest	*Rs.12,47,239/-*
ii. Admn. Expenses	*Rs. 5,00,000/-*
iii.Personal expenses	*Rs. 16,85,000/-*

	Rs.34,32,239/-
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(b) Alternatively, the disallowance is on higher side and a token amount would meet the ends of justice.
5. That on the facts, circumstances and legal position of the case, the Ld.CIT(A) has erred in law in confirming the disallowance of Rs.4,73,69,355/- being the amount of inventory written off during the year.
6. That on the facts, circumstances and legal position of the case, the Ld.CIT(A) has erred in law in upholding the disallowance of a sum of Rs.28,56,250/- on account of investments written off.
7. That the appellant craves leave to reserve to itself the right to add, alter, amend, substitute, withdraw and/or vary any ground(s) of appeal at or before the time of hearing."

3.1. Ld.Counsel submitted that **Ground No.1** is general in nature and therefore do not require any adjudication.

3.2. He also submitted that **Ground No 2** has been directed by assessee to be 'not pressed', and accordingly said ground stands dismissed as 'not pressed'.

4. Ground No. 3 raised by assessee is in respect of disallowance of prior period expenses amounting to Rs.4,59,928/-.

4.1. Ld.Counsel submitted that Ld.Assessing Officer (Ld.A.O.) disallowed a sum of Rs 21,51,466/- on account of prepaid expenses incurred for purposes of business. He submitted that Ld.A.O. computed expenses disallowed under the head 'prior period expenses'. It has been submitted that these are routine business expenses which are allowable. He submitted that Ld.CIT(A) restricted disallowance to Rs.4,59,928/-, which was crystallised during year under consideration and therefore deserves to be allowed.

4.2. On the contrary Ld.Sr.DR submitted that Ld.CIT(A) upon verifying supporting documents like bills etc. had allowed claim of

assessee partly. He submitted that assessee had not filed any supporting documents regarding remaining payments to establish that expenditure had crystallised during the year. He thus placed reliance upon order passed by Ld.CIT(A). Ld.Sr.DR also placed reliance upon order dated 09/03/18 passed by this Tribunal in assessee's own case for A.Y. 2005-06 in ITA No. 4235/Del/2014, wherein a similar view has been taken.

5. We have perused submissions advanced by both sides in light of records placed before us.

5.1. It is observed that Ld.CIT(A) has called fo details supporting payments being crystallised during the year, and assessee filed documents/evidences in reference to only major items. Ld.CIT(A) on verification of supporting evidences noted that bills in respect of Orient Law Firm, Lovely Industrial Services, Super Auto Forge Ltd., Singh & Co., and Saket Motors Ltd., were dated 28/07/2000, 13/03/1999, 05/08/2000, 14/04/1997 and 09/01/2001 respectively and came to conclusion that, these were liabilities in respect of earlier years, which was crystallised during that period. He thus confirmed disallowance made by Ld.AO to the extent of such amounts, and also amounts, for which no supporting evidences have been filed to substantiate that liability arose and crystallised during year under consideration.

5.2. Before us assessee has not produced any copy of supporting documents in respect of balance payments to establish that expenses had crystallised during year under consideration. We draw support from the order of Coordinate Bench in assessee's own

case for A.Y. 2005-06 (supra) in holding that merely because expenditure has been debited in Profit and Loss account during year neither it becomes expenditure pertaining to this year nor it becomes an expenditure pertaining to prior years. It is the duty of assessee to show that this expenditure has crystallised during the year and therefore are incurred during the year. As adequate details have not been produced before Ld.AO as well as before Ld.CIT(A), we do not find any infirmity in the disallowance made by Ld.CIT(A). Accordingly the same is upheld.

In the result ground no.3 raised by assessee stands dismissed.

6. Ground No. 4 is in respect of 14 A disallowance.

6.1. Ld.Counsel submitted that assessee had shown exempt dividend income under section 10(33) of the Act amounting to Rs.8,22,31,262/-, and interest on bonds exempt under section 10(23G) of the Act, amounting to Rs.11,03,79,241/-. Ld.Counsel submitted that Ld.A.O during course of assessment proceedings computed disallowance at Rs.2,19,36,390/-, and Rs.16,55,00,000/- attributable to earning of dividend and interest income respectively. It has been submitted that assessee had given interest-bearing loan of Rs.45.9 crores to Escotel a subsidiary of assessee during Financial Year 1997-98 and interest as per agreed terms were charged on such loans. He submitted that since Escotel is an infrastructure capital company as per provisions of section 10 (23G) of the Act, and approved by Government of India for said purposes, interest income earned by assessee on said loan was claimed exempt under the provisions. He submitted that no expenses could

be attributed towards earning of this interest income from Escotel and like dividend income. He further submitted that, dividend has been earned from investment in shares, which were made in earlier years, and not during year under consideration. He submitted that Ld. AO was not right in estimating the proportionate disallowance at 25% of administrative expenses to be attributable to earning of such income.

6.2. On the contrary Ld.Sr.DR submitted that assessee has made investments during year as per order of Ld.CIT(A) which has yielded dividend income also. He submitted that it cannot be accepted that no expenditure could be attributable for earning of exempt income as section 14 A is triggered the moment there is exempt income earned during year by assessee. Further placing reliance upon decision of *Hon'ble Supreme Court* in the case of *Maxopp Investment Ltd. vs CIT* reported in *(2018) 91 taxmann.com 154(SC*). Ld.Sr.DR submitted that strategic investments would also fall within the ambit of disallowance

7. We have perused submissions advanced by both sides in light of records placed before us.

7.1. Admittedly, present year under consideration is 2002-03 and therefore the disallowance cannot be made as per formula given under Rule 8D of Income tax Rules, 1963.

7.2. Under such circumstances when there is an exempt income earned by assessee during year, disallowance needs to be made under section 14 A, being expenses attributable to earning of such exempt income. Ld.CIT(A) has observed that proportionate

disallowance has been always made in hands of assessee in preceding assessment years. It has been recorded by Ld.CIT(A) that investments made during year under consideration has been partly made out of borrowed funds and interest works out to be Rs.12,47,239/-. Ld.CIT (A), restricted disallowance for earning exempt income under section 10 (33) of the Act to Rs.12,47,239/-. Ld.CIT (A) observed that personal expenses cannot be entirely attributed towards earning of exempt income as it includes expenditure incurred on employees of manufacturing unit. He thus restricted proportionate disallowance at Rs.16.85 Lacs and confirmed addition to the extent of Rs.34.72 lakhs (Rs.5 lakhs + Rs.16.85 lakhs + Rs.12.87).

7.3. Ld.Counsel argued that, disallowance though restricted by Ld.CIT(A) to Rs.34,32,239/-, is still on higher side. Alternatively, he suggested for disallowance of token amount would meet ends of Justice.

8. We have considered argument alternatively presented by Ld.Counsel, apart from main argument, that no disallowance is to be made under section 14 A.

8.1. At the outset we reject the argument that no expenditure could be attributed to earning of exempt income as section 14 A is automatic and comes into operation without any exception as soon as exempt income is claimed by assessee.

8.2. It is observed that total exempt income claimed by assessee amounts to Rs.19,26,10,503/-, against which disallowance restricted by Ld.CIT(A) is Rs.34,32,239/-. It is observed that

Ld.CIT(A) records that proportionate expenses being considered for disallowance, has been incurred mainly for employees of manufacturing unit which cannot be related to earning of exempt income. Under such circumstances allocation of personal expenses towards earning of exempt income should not have been made. We therefore grant further relief to assessee by excluding personal expenses amounting to Rs.16,85,000/-, from disallowance computed under section 14 A. We thus direct Ld.AO to restrict the disallowance at Rs.17,47,239/-.

Accordingly this ground raised by assessee stands allowed partly.

9. Ground No. 5 is regarding disallowance of Rs.4,73,69,355/- being amount of inventory written off during the year.

10. Ld.Counsel submitted that assessee had telecommunication division which was acquired from Escort Communication Ltd. It was submitted that telecommunication division of assessee company was hived off and was taken over by a 100% subsidiary of assessee company i.e. Escorts Communication Ltd. w.e.f. 01/10/1994. Ld.Counsel submitted that during financial year 2000-2001 M/s L.G.Information and Communication Ltd., bought business of WLL, and old business of manufacture and sale of EPPBX, Key telephone system, etc. was purchased by assessee as per agreement dated 20/12/2000. He further submitted that quotations were called to realise best price, but it was opined that inventory is consisting of electronic components which was not foolproof, and has to be disposed off on 'as is where is' basis.

Ld.Counsel submitted that doing so would have involved a risk being used of inventories in the market as spares, which would have brought bad name to the company and therefore it was decided balance inventory should be destroyed. Under such circumstances a sum of Rs.4,23,00,000/-, has been claimed.

10.1. On the contrary, Ld.Sr.DR submitted that assessee has not established exact value of stock, though slow-moving and obsolete, which is against principles of accounting. It has been submitted that as unit has been closed down, write off of inventory relating to that division is not an admissible deduction He placed reliance upon order passed by Ld.CIT (A) in support of his argument.

11. We have perused submissions advanced by both sides in the light of records placed before us.

11.1. It has been submitted by assessee that once telecommunication division was hived off from assessee, inventory became unusable.

11.2. It is observed that Ld. CIT (A) decided the issue as under:

"12.3. It is settled law that the closing stock is to be valued at market price or cost price as decided by the appellant company. In the case of the appellant company, instead of valuing the stock at market or cost price whichever is lower, the appellant company had taken the value at nil more so when the fact that in December 2000 only the appellant company had taken over this inventory of stock from escort's communication Ltd at a value of Rs. 4,73,69,355/-. The cost of the inventory is Rs. 4,73,69,355 and the appellant company has not been able to establish that the market value of the stock has

become nil, the AO has rightly disallowed the expenditure. The action of the AO is confirmed."

11.3. Even before us, Ld.Counsel was unable to establish market value of stock to be at 'nil', and therefore we do not find any infirmity in the order of Ld.CIT (A) and the same is upheld.

Accordingly ground no.5 raised by assessee stands dismissed.

12. Ground No. 6 is in respect of disallowance of Rs.28,56,250/- on account of investments written off.

12.1. Ld.Counsel submitted that assessee during year under consideration was owning shares worth Rs 28,56,250/- in Escorts Overseas Pvt. Ltd. It has been submitted that, these were doubtful of recovery, and hence provision was made in the financial year 1999-2000. Ld.Counsel submitted that Registrar of Companies, Singapore dissolved Escorts Overseas Pvt. Ltd., on 23/09/20 01 and therefore the same has been claimed as a loss.

12.2. Ld.Sr.DR submitted that profit and loss on investment are dealt with in accordance with provisions of section 45 to section 55A of the Act. It has been submitted that these sections clarify that loss on investment can be allowed only on sale or transfer of investment. Ld.Sr.DR submitted that assessee in present case has not sold or transferred investments. He placed reliance upon orders of authorities below.

13. We have perused submissions advanced by both sides in light of records placed before us.

13.1. Assessee placed reliance upon page 197 of paper book which is issued by the Registrar of Companies and Business. It is

observed that assessee is a shareholder which is apparent from page 199. There is a categorical observation by Ld.CIT (A) that assessee has neither transferred shares, nor has sold and therefore loss arising on this transaction cannot be allowed under the Act. Ld. CIT (A) decided the issue by observing as under:

"13.3. There is no doubt that neither the investment in the overseas company has been transferred by the appellant company nor it has been sold therefore the loss arising on this transaction cannot be allowed under the act. It has not been substantiated that what was the value of the asset liquidation of the company. It can also not be allowed as a business loss because for computing the business income, the same is to be computed as per the provisions of section 28 to 41 of the act and this amount invested as an investment is not allowable under any of the above mentioned section, hence, it cannot be said that it is incidental to the existing business. The same has been rightly disallowed by the AO. The action of the AO is confirmed."

13.2. Assessee before us has not been able to establish how the company was dissolved, and manner in which its assets/liabilities have been dealt with. Before us, assessee has not been able to establish value of shares on or before date of dissolution of company. Even if it has to be considered as capital loss, assessee has not provided any relevant details regarding same. Under such circumstances we do not find any infirmity in order of Ld.CIT(A) and same is upheld.

Accordingly ground no.6 raised by assessee stands dismissed.

14. In the result appeal filed by assessee stands partly allowed.

15. ITA No. 84/Del/2006 (Revenue's appeal)

Grounds raised by revenue in this appeal are as under:

1. On the facts and circumstances of the case and in law. the Ld.CIT(A) has erred in deleting the disallowance of Rs. 22,54,277/- made by the A.O. on account of redemption of SPNs.
2. On the facts and circumstances of the case and in law, the Ld.CIT(A) has erred in deleting the disallowance of Rs. 3,12,75,000/- being the upfront fee paid to the banks.
3. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the disallowance of Rs. 78,56,810/- on account of development of the existing products and prototype products ignoring that such expenditure imparted a benefit of enduring nature and as such was of capital nature. The Ld.CIT(A) also ignored that the assessee had separately claimed deduction of Rs.2,98,46,839/- as capital R&D expense and treated this expenditure of Rs.78,56,810/- only as pre-operative expense.
4. On the facts and circumstances of the case and law. the Ld.CIT(A) has erred in deleting disallowance of Rs. 16,91,538/- made by the A.O.. on account of prior period expenses ignoring that the assessee company was following the mercantile system of accounting and as such prior period expenses could not be allowed as deduction in computation of assessee's total income for the instant A.Y. 2002-03.
5. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the disallowance of expenses of Rs. 1,18,94,891/- made by the A.O., on account of expenses claimed under the head commission, discount and brokerage on sales made to Government parties ignoring the provisions of Explanation to sub-section(T) of section 37 of the I.T. Act. 1961.
6. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting disallowance of Rs. 4,56,00,000/- on account of interest on interest free loan given by the erstwhile Escorts Tractor Ltd. to its subsidiary company M/s Escortac Finance & Investment Ltd., prior to its amalgamation with the assessee company in F.Y. 1995-96.

7. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting disallowance of Rs.1,94,64,390/- and of Rs.16,42,52,761/- out of the total disallowance of Rs.2,19,36,390/- and Rs.16,55,00,000/- made by the A.O. u/s 14A of the I.T. Act, 1961."

15.1. At the outset, Ld.Counsel submitted that issues raised by revenue in the appeal are squarely covered by orders of this Tribunal in assessee's own case for preceding assessment years.

16. Ground No. 1 raised by revenue is against deleting disallowance of Rs.22,54,277/-, made on account of redemption of SPNs.

16.1. Brief facts relevant for this ground are that during year under consideration assessee claimed deduction towards premium payable on SPNs on accrual basis commencing from financial year 1994-95. Assessee claimed expenditure amounting to Rs.15,57,61,488/- during year on actual payment made. Ld.AO added sum of Rs.22,54,277/-. It was submitted by assessee that the said sum was never reduced from computation of income and was claimed by way of a note in return of income, and therefore amounts to double addition. It was also submitted that full claim claimed by assessee, becomes infructuous as in previous years, same has been allowed by Ld.CIT (A) on accrual basis as claimed by assessee.

16.2. Upon appeal before Ld.CIT (A), addition was deleted by observing as under:

"3.3. The contention of the appellant counsel has been found to be correct that the premium payable on SPNs have been allowed by the

CIT(A) on accrual basis. The observation made by the AO that no claim was made is also incorrect as it is found to be correct that the claim for the entire amount was claimed by way of a note in the return of income filed by the appellant company at point No.8 in which all the facts have been disclosed by the appellant company. In any case, during year the SPNs have been redeemed and there is no reason for disallowing the amount claimed by the appellant or alternatively the AO should have allowed a sum of Rs.15,57,61,488/- being the actual payment of premium made during the year. Taking into consideration this issue has already been decided in the earlier years by the CIT(A) in favour of the appellant, following the order of the CIT(A) in earlier years, the disallowance made by the AO is deleted and otherwise also even if the stand taken by the AO is considered then also during the year actual payment has been made."

16.3. Ld.Sr.DR placed reliance upon order of Ld. AO but could not controvert findings of Ld CIT(A).

17. We have perused submissions advanced by both sides in light of records placed before us.

17.1. It is observed that identical issue has been decided by this Tribunal consistently in year 1998-99 as well as assessment year 2001-2002. Copy of the order of this Tribunal in ITA No. 1841/Del/02 for assessment year 1998-99 and ITA No. 567/Del/2005 and 1562/Del/2005 for assessment year 2001-02 has been referred to in the order for assessment year 1999-2000 in

ITA No. 3581/Del/02 and CO no. 245/Del/06 in assessee's own case as under:

"Having considered the rival stands and the fact situation, the issue, in our view is squarely covered by the decision of the Hon'ble Supreme Court in the case of madras Industrial Corporation Ltd. (supra). The assessee has raised funds by way of issuance of SPNs which are redeemable at a premium partly at the end of 4th, 5th, 6th and 7th year. There is no dispute that the funds so raised have been utilised by the assessee for the purposes of its business as we do not find any finding or even the allegation by the revenue to the contrary. Thus, the liability to pay the premium amount over and above the face value of SPNs on redemption is a liability incurred by the assessee for the purposes of its business by generating funds which were utilised for the business activities. Thus, such an expenditure is an allowable expenditure. Now, with regard to year of allowability, it is evident that the payment of premium results in securing or benefit over a number of years. The benefit is spread over the entry period of 7 years. The expenditure is therefore allowable over the entire period of the SPNs the redemption having regard to the party of reasoning enunciated by the Hon'ble Supreme Court in the case of Madras Industrial Corpn. Ltd. (supra). The assessee, therefore, correctly claimed deduction only in respect of the proportionate premium relatable to the year in question."

Respectfully following the decision, this ground raised by revenue stands dismissed.

18. Ground No. 2 raised by revenue is in respect of deleting disallowance of Rs.3,12,75,000/- being upfront fee paid to banks.

18.1.It is submitted that assessee claimed upfront fees paid to ICICI bank, Bank of India, SBI and IDBI amounting to Rs.3,69,25,000/- during year under consideration. It is also submitted that the issue has been dealt with by this Tribunal in assessee's own case for preceding assessment years. Assessee has placed before us order passed by this Tribunal in assessee's own case for assessment year 1999-2000 in ITA No. 3581/Del/02 and CO no. 245/Del/06, wherein it has been held as under:

"7. Before us it is not in dispute that in the A.Y 1998-99 the Tribunal had an occasion to decide an identical issue in ITA 1841/Del/02 for A.Y. 1998-99. The Tribunal relied on the decision of Hon'ble Supreme Court in case of India Cements Ltd. Vs. CIT, 60 ITR 52 (S.C.) wherein the Hon'ble Supreme Court has held that any expenditure incurred for obtaining loan is also allowable as revenue expenditure even if the loan is intended for acquiring a capital asset. The Tribunal accordingly allowed the claim of assessee. Respectfully following the decision of the Tribunal referred to above, we uphold the order of the CIT(A) and dismiss the second ground of appeal of Revenue."

Respectfully following the same this ground raised by revenue stands dismissed.

19. Ground No.3 has been raised by revenue against deleting disallowance of Rs.78,56,810/- on account of development of existing products and prototype products.

19.1.Assessee submitted before Ld.AO that, these were in the nature of R&D expenses. Ld.Sr.DR submitted that in P&L account R & D expenses of capital nature has been separately claimed by assessee and expenditure incurred on development of prototype is not part of R&D expenses. He submitted that since these expenses have given rise to increase in knowledge, benefiting assessee. He thus submitted that such expenses should be capitalized, as they gave rise to enduring benefit to assessee.

19.2. On the contrary, Ld.Counsel submitted that on identical facts, Ld.CIT (A) in preceding assessment years allowed claim of assessee. He placed reliance upon observations of Ld. CIT (A) in deleting the addition.

20. We have perused submissions advanced by both sides in light of records placed before us.

20.1. It is observed that Ld.CIT(A) deleted addition by observing as under:

"5.3. There is no dispute about the fact that the expenditure incurred by the appellant company of Rs.78,56,810 has been incurred by the appellant company for R&D activities related to the business of manufacture of the appellant. As per the provisions of Section 35 of the Act, the capital expenditure relating to scientific research as mentioned in the section is allowable as an expenditure besides the expenditure which is not capital in nature incurred by the appellant on R&D activities. As the genuineness of the expenditure and for what it has been incurred has not been doubted, the same is clearly

allowable u/s 35 of the Act and the addition made by the AO on this account is deleted."

20.2. It is observed that Ld.AO records that, assessee maintains separate accounts for capital expenditure for R&D purposes, and that expenses on development and prototype is not part of R&D expenses. Thus it is clear that Assessing Officer is not disregarding genuineness of expenditure incurred by assessee. Therefore we do not find any infirmity in the observations of Ld. CIT (A) and the same is upheld.

Accordingly this ground raised by revenue stands dismissed.

21. Ground No. 4 has been raised by revenue regarding deleting disallowance of Rs.16,91,538/-, made by Ld.AO on account of prior period expenses.

21.1. It has been submitted that this ground is connected with Ground No.3 in assessee's appeal, which has been dealt hereinabove in paragraphs 4 and 5. It is observed that Ld. CIT (A) deleted addition in part as assessee had provided certain bills which were relating to year in consideration and was of the opinion that payments crystallised during the year to that extent. Ld.Sr.DR placed reliance upon written submissions filed by revenue wherein reliance has been placed on Section 145 (2) of the Act and submitted that as assessee follows Mercantile system of accounting and therefore these expenses cannot be allowed during the year as these are expenses relating to prior period.

21.2. We do not find any infirmity in the factual observations of Ld.CIT(A) which has been verified by Ld.CIT(A) having regards to documents/evidences/bills etc., filed by assessee. There is nothing contrary to these observations that Ld.Sr.DR has been able to place before us and therefore we do not find any infirmity in the observations of Ld. CIT (A) and the same is upheld.

Accordingly this ground raised by revenue stands dismissed.

22. **Ground No.5** relates to expenses of Rs.1 81,94,891/- on account of commission, discount and brokerage on sales made to government parties.

22.1. Ld.Sr.DR submitted that expenses claimed under the head 'commission, discount and brokerage' amounting to Rs.1,18,94,891/- has been paid to 3rd parties by assessee related to sales made to government. It has been submitted that Ld.AO rightly disallowed commission, as there is no middlemen and commission agents permitted to operate in purchases or perky procurement made by governmen Thus he emphasised that only business expenses can be allowed under section 37 (1) of the Act incurred by assessee.

22.2. On contrary Ld.Counsel placed reliance upon categorical observations by Ld. CIT(A).

23. We have perused submissions advanced by both sides in light of records placed before us.

23.1. Following were factual observations by Ld.CIT(A) regarding disallowance made by Ld. AO:

"9.2. During the course of appellate proceedings, the appellant counsel submitted that complete details of payment along with addresses and PAN were filed during the course of assessment proceedings, therefore, the observation made by the AO that PAN and places of assessment were not furnished is incorrect. It was further mentioned that the details, confirmation and copies of appointment letters along with PAN as filed before the AO are being enclosed. It was further mentioned that identical expenditure has been claimed in the past assessment years and has been allowed by the AO himself as also at the stage of appeals. In the preceding assessment year, the same has been allowed and the facts were identical. It has been further mentioned that the entire payment of commission pertains to Railway Equipment of the assessee company and inasmuch as its operation extent beyond Delhi namely places far away as Guwahati, Calcutta, Barowni, it becomes necessary to obtain the services of the agents instead of posting the employees of the assessee company at various places. The job profile of these agents is procurement of orders from the Government departments and also to follow up for the payments after the supplies. The payments made by the assessee cannot be termed as illegal or violation of law. In the judgment relied upon by the AO in the case of Madivenkak Ram and Company (supra) is clearly distinguishable. In that case, the assessee had carried on its business in violation of provisions of FERA and the lordship of the Hon'ble Supreme Court rejected the claim for deduction on the ground that assessee was expected to

carry on its business in accordance with law and evasion of law could not be a trade pursuit.

9.3. On verification of assessment record, it is found to be correct that the appellant company vide letter dated 13-01-2005 has furnished the details of parties to whom commission has been paid, copies of appointment letters and confirmation from the parties to whom commission has been paid. In the list furnished of the parties at Page No.38 of the letter dated 13-01-2005 are indicated the PAN of the parties. Therefore, the observation made by the AO in the assessment order that PAN/GIR No. was not mentioned is not correct. Though in the confirmations of the parties, the PAN is not indicated but in the list given by the appellant company at Page No.38 of its letter dated 13-01-2005, PAN is clearly mentioned of all the parties to whom commission has been paid. Regarding the objection of the AO that the purpose for which commission has been paid not mentioned in the confirmation filed is also of no consequence because the appellant company had filed the copies of appointment orders for which the commission agents have been appointed. If the AO had wanted confirmations in a particular fashion then he should have asked the appellant company to file the confirmations in a particular fashion. Without telling the appellant company what is further required, the AO has wrongly not considered the confirmations filed by the appellant company.

9.3.1. The AO had relied on the judgment of the Hon'ble Supreme Court in the case of Madivenkak Ram & Co. (supra) for disallowing

the expenditure. The facts and the reasons for disallowing the expenditure claimed in the above mentioned case are noted below:

Facts: The assessee, to start with, was a partnership consisting mostly of family members. In 1965, it was converted into a private limited company to carry on the business of export of tobacco. The first directors appointed at the time of incorporation were to hold office during their lifetime or until they resigned voluntarily. On the basis of the information received, a search was conducted by the Enforcement Directorate in the assessee's business premises. A number of letters and other documents were seized which disclosed that the assessee had indulged in transactions in violation of the provisions of the Foreign Exchange (Regulation) Act.

Issue: Whether the expenses in carried in transactions carried out in violation of the provisions of FERA is deductible.

Finding: No

Reasoning: In the instant case, the assessee had indulged in transactions in violation of the provisions of the Foreign Exchange (Regulation) Act. The assessee was expected to carry on the business in accordance with law. If the assessee contravenes the provisions of the FERA to cut down its losses or to make larger profits while carrying on the business, it was only to be expected that proceedings will be taken against the assessee for violation of the Act. The expenditure incurred for evading the provisions of the Act and also the penalty levied for such evasion cannot be allowed as deduction. The expenditure in this case cannot, in any way, be allowed as

wholly and exclusively laid out for the purpose of the assessee's business.

From the decision of the Hon'ble Supreme Court, it is clear that the expenditure incurred for evading the provisions of the Act and also the penalty levied for such evasion was held to be not allowable as a deduction.

9.3.2. In the AY 2000-01 also, the issue of commission and discount was there and the reasons for which disallowance was made, the submission made by the appellant and why the same was held to be allowable by the undersigned are noted below:

"..... *10.1* *On going through the assessment order, it is observed that the expenditure on above account has increased from Rs.11.20 crores to Rs.21.75 crores. The AO observed that the commission paid to third parties/agents related to sales made to the government has been disallowed by the department, therefore, following the precedent, the commission of Rs.64,95,097 paid to third parties for services rendered in connection with sales made to the government parties is disallowed.*

10.2. The various submissions made by the appellant counsel during the course of appellate proceedings are summarized below:

(i) *In the AY 1998-99, the CIT(A) had considered the issue and decided the same in favour of the appellant. In AY 1999-00, the AO himself considered the issue and allowed the entire claim of expenses to the amount of Rs.40,46,372. The AO while allowing the expenses has himself observed that the authorized representative has filed confirmation in respect of all the cases while in the*

preceding years they were unable to do so, hence, the entire expenditure is allowable.

(ii) *The copies of assignment letters/appointment letters of the agents along with confirmation in respect of the entire payment of Rs.64,95,097 were filed before the AO.*

(iii) *The AO has wrongly observed in the preceding years that the expenses has been disallowed while the fact is that the AO himself in AY 1999-00 have allowed all the expenses and there is no disallowance.*

10.3. Taking into consideration the above facts as the appellant has filed full details along with confirmation before the AO, there was no reason with the AO to disallow the expenditure when specifically in earlier years the disallowance has only been made in respect of the confirmations not filed by the appellant company. In fact, in AY 1999-00, the appellant company was able to file confirmation in respect of the entire expenses and no disallowance was made by the AO. In view of the above, the addition made by the AO is deleted."

9.3.3. The AO while disallowing the expenditure has presumed that this commission has been paid to middlemen for procuring the orders from the Government while there is no proof or evidence in support of the same. Before coming to this conclusion, the AO has not given any opportunity or show cause to the appellant company why it should not be disallowed invoking Explanation to Section 37(1) of the Act. This commission and discount is being claimed by the appellant company regularly and has also been allowed by the AO himself and also at the appellate stage. In view of the above facts, as all the

evidence has been filed by the appellant company and there is no proof that the expenditure is covered under Explanation to Section 37(1) of the Act, the disallowance made by the AO is deleted."

23.2. It is also observed that Ld.CIT(A) had observed that facts in *Madivenkak Ram & Co.,* reported in *229 ITR 534*, decided by *Hon'ble Supreme Court* is different with that of present case. It has been observed that before *Hon'ble Supreme Court*, issue was regarding expenditure incurred for evading provisions of FERA, and penalty levied for such evasion, which was held to be not allowable as a deduction.

23.3. We are therefore of the opinion that Ld.CIT (A) was right in deleting the addition so made and the same is upheld.

Accordingly this ground raised by revenue stands dismissed.

24. Ground No.6 is raised by revenue regarding deleting disallowance of Rs.4,56,00,000/- on account of interest on interest free loan, given by erstwhile Escort Tractors Ltd., to its subsidiary company M/s Escotract Finance & Investment Ltd., prior to is amalgamation with assessee.

24.1. Ld.Sr.DR submitted that assessee had given interest-free loan of Rs.38.01 crores to M/s.Escotract Finance & Investment Ltd. It has been submitted that assessee relied on borrowed funds for its own affairs and granting of interest-free loan thereby artificially increase its expenditure which cannot be allowed as business expenses. It has been submitted that in addition to Rs.5.6 crores at

the rate of 12% on sum advanced as interest-free to sister concern was also added rightly by Ld.AO.

24.2. Ld.Counsel placed reliance upon factual observations made by Ld.CIT (A). He submitted that said loan was given prior to the amalgamation in the year 1995-96.

25. We have perused material placed before us in light of arguments advanced by both sides.

25.1. Admittedly, said loan was advanced by erstwhile company to sister concern in the year 1995-96. Assessing Officer has not been able to establish that said funds have been advanced out of borrowed funds by erstwhile company. Subsequently, company that advanced loan, got amalgamated with assessee. It is for this reason that Ld.CIT (A) deleted addition. Ld CIT (A) observed that, for assessment year 2001-02, identical addition was deleted on similar facts, which is not challenged by revenue.

25.2. Under such circumstances we uphold the view taken by Ld.CIT (A).

Accordingly this ground raised by revenue stands dismissed.

26. Ground No. 7 is on account of partial relief granted by Ld.CIT (A) while computing disallowance under section 14 A of the Act.

We have already considered this issue while deciding ground No. 4 of appeal filed by assessee. Following our view taken hereinabove we dismiss this ground raised by revenue.

Accordingly this ground raised by revenue stands dismissed.

In the result appeal filed by revenue stands dismissed.

Assessment year 2003-04

ITA No. 2350/Del/10 (revenue's appeal)

28. Revenue has raised following grounds for year under consideration.

At the outset both parties submit that **Ground Nos. 5, 6, 7** stands covered with the view taken in revenues appeal for assessment year 2002-03.

1. On the facts and circumstances of the case and in law, the CIT(A) has erred in deleting the disallowance of expenses of Rs. 2,65,46,151/- made by the A.O., on account of expenses claimed under the head commission, discount and brokerage on sales made to Government parties ignoring the provisions of Explanation to sub-section(T) of section 37 of the I.T. Act 1961.

2. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the proportionate disallowance of interest of Rs.13,52,00,000/- on the interest free amounts outstanding against the sister concerns.

3. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the disallowances of interest payment amounting to Rs.72,32,00,000/- on account of investment of Rs.602.66 crs made in shares of group companies.

4. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the disallowances of Rs.32,00,000/- paid as upfront fees ignoring the fact that it will be incurred by the assessee

company as a one time fees charged by the lending bank at the time of granting of loan.

5. (a). On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the disallowances of Rs.35,75,330/- made on account of development of existing products and prototype products ignoring that such expenditure imparted a benefit of enduring nature and as such was of capital nature.

(b) On the facts and circumstances of the case and substantial question of law involved, whether the Ld.CIT(A) was correct in law in deletion of addition of Rs.35,75,330/- on account of disallowance of expenditure for development of existing product by treating expenditure as capital expenditure.

6. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the addition made on account of professional charges of Rs.7,92,67,976/- ignoring the fact that the various expenses incurred by the assessee has enduring benefit and were in the nature of capital expenditure.

7. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the disallowance of Rs.28,07,055/- made by the AO, on account of prior period expenses ignoring that the assessee company was following the mercantile system of accounting and as such prior period expenses could not be allowed as deduction in computation of assessee's total income.

8.The Order of the CIT(A) is erroneous and not tenable in law and on facts."

29. Ground No.1 raised by revenue pertains to deleting disallowance of a sum of ₹ 2, 65, 46, 151/-out of commission expenditure.

29.1. Referring to the assessment order Ld.Sr.DR submitted that assessee was being commissioned to 3rd parties in respect of sales made to Indian Railways from its railway equipment division. He submitted that there was no role of a middleman in the whole process of award of orders by government and there was no scope for any private party to render any services for earning commission thereof. Accordingly learned AO called for assessee to produce the employee of company who deals with the sales et cetera in the railway equipment division. Assessee in compliance to the direction of learned AO produced one Mr Ajay Razdan Sr.Manager Commercial, whose statement was recorded, which Ld.Sr.DR referred to in assessment order at para 2.9. He submitted that on the basis of statement, learned AO took the view that there had been no role of a third party in procuring orders, payment of commission was not justified. He also took note of the fact that one of the commission agent was located at Haryana and other two were based at Kanpur, whereas bills revealed that business came to assessee from all over India. Ld.Sr.DR supported addition by stating that these agents could not handle even follow-up work, if any relating to orders.

29.2. On the contrary, Ld.Counsel contended that, identical payment was made in past assessment years, and has been allowed by Ld.AO himself in assessment made under section 143 (3) of the

Act. It was also pointed out that in certain assessment years disallowances made by Ld.AO has been deleted by Ld.CIT (A) and revenue has either accepted the order, or appeal is pending before the Tribunal.

29.3. Placing reliance upon the submissions made by Ld.Counsel before Ld.CIT (A), it was submitted as under:

29.4. The learned Counsel submitted that complete details of the payment had been filed during the course of assessment proceedings and copies thereof were appended at page 1 to 53 of the Paper Book. It was a matter of record that all payments were made by account payee cheques and at least one party namely R.K. Ispat Ltd. was common to the preceding assessment year where the claim have been allowed. He further submitted that complete details in the form of confirmations along with PAN Nos., names and addresses had also been filed but the AO instead of making a cross verification from the payees, called for and recorded a statement of one of the employee of the company, Mr. Ajay Razdan who was not in a position to give any detailed information since he had gone in a routine manner along with the tax counsel.

29.5. Coming to the statement of Mr.Ajay Razdan, it was submitted that the AO could not find any fact which was adverse to the appellant company and consistent with the similar claim made in preceding assessment year, but goes on to rely heavily on the statement of Mr. Ajay Rajdan and that also picking the words and sentences instead of reading the statement as a whole. That apart, the AO put on the appellant the burden of filing the

acknowledgement receipt of the return filed by the payees whereas it was his obligation to make requisite enquiries.

29.6. The learned counsel further contended that the statement of Mr. Ajay Razdan appended at pages 56 to 57 of documents submitted with written submissions dated 27/3/2007 in fact supports the case of the appellant company if the statement is read as a whole. Mr Razdan has clearly stated that the role of the third party is in the areas of liaisoning, promotion of products, order procurement and payment realization. Mr Razdan has further submitted in an answer to one of the questions, that the agents are involved in realization of payments and promotion of new products of the company and they are also involved in submission of bills and making good any deficiencies in the documents. The Assessing Officer has picked certain sentences from the statement of Mr. Razdan which according to him show that there is no role of a third party in the whole process of procuring business. As regards the role of third party in the evaluation of offers by Railways, it is true that the evaluation of offers is made by the Railways independently but that does not mean that the agent/third party appointed is only for the purpose of getting the orders evaluated. The evaluation of offers is a technical process/matter which is sole prerogative of the Railways. In the Remand Report dated 09/03/2007 the Assessing Officer has not made any adverse comments on the evidence filed in respect of the commission payments, but he has relied heavily on the statement of Mr.Razdan.

29.7. The issue according to the learned counsel is fully covered by the various judgments of the I.T.A.T. and the CIT (Appeals) in appellant's own cases and a reference has been made to the order of the Tribunal for AY 2001-02 in ITA No.567/Del/05 dated 31.3.2006, a copy of which is placed in the Paper Book of judgments. The learned counsel further relied on the orders of the Tribunal for the AYs 1995-96 to 1998-99, copies thereof being provided during the hearing of appeal. In conclusion it was urged that the addition be deleted.

30. We have perused submissions advanced by both sides in the light of the records placed before us. It is observed that Ld. CIT (A) has analysed aforestated submissions of assessee as under:

"4.9. I have carefully examined the facts as also the statement of Mr.Ajay Razdan which has been relied upon heavily by the AO. I would tend to agree with the ld.counsel of the appellant that on a reading of the said statement as a whole there would not remain any doubt about the role of the agent/third party in the whole process. This cannot just be limited to getting orders from railways evaluated which in any case is the sole prerogative of the parties who invite the bids. In the earlier A.Ys also the payments of similar nature have been made but mostly allowed by the AO himself or by the CIT(A) in appeals and the ITAT affirming the decisions of 1st appellate authority. Following the same, the addition on account of payment of commission amounting to Rs.2,65,46,151/- is hereby deleted."

31. We do not find any infirmity in aforestated findings of Ld.CIT (A) which is based on detailed analysis for assessment year 2002-03, Ground no. 5 in revenues appeal on similar facts, addition has been deleted in para 16 to 17.2 hereinabove. Following the same we are inclined to uphold the view taken by Ld.CIT (A).

32. In the result this ground raised by revenue stands dismissed.

33. Ground No.2 raised by revenue relates to deleting of proportionate disallowance of interest amounting to Rs,13,52,00,000/- vis-a-vis, amounts advanced to two group companies, namely Escorts Construction Equipment Ltd., and Escotel Mobile Communications Ltd.

33.1 Ld.Sr.DR submitted that Ld.AO in para 4.1 of assessment order has observed that assessee borrowed huge funds and was paying substantial amount of interest and bank charges, whereas loans aggregating to Rs.112.62 crores had been advanced to group companies. He submitted that Ld.AO therefore made proportionate disallowance amounting to Rs.13.52 crores, by adopting interest rate of 12%, which according to him was reasonable, and which assessee could have saved by using such funds for its own purposes.

33.2. On the contrary, Ld.Counsel placed reliance upon submissions made by assessee before Ld.CIT (A). For the sake of convenience we are reproducing the submissions advanced by Ld. Counsel before Ld.CIT (A) as under:

33.3. The sum of Rs. 112.62 crores subjected to the disallowance contained brought forward opening balance of Rs. 108.67 crores, which could not be taken into account for the said purpose.

In case of Escorts Construction Equipment Ltd., fresh advance made during the year under consideration was to the tune of Rs.5.96 crores, whereas in case of Escotel Mobile Communications Ltd., there was a reduction in lent funds of around Rs.2crores during the year.

33.4. Submissions in other words were that in so far as Escotel Mobile Communications Ltd., was concerned, there could be no disallowance and in respect of Escorts Construction Equipment Ltd., the fresh advances had come out of non-interest bearing funds, and details of which had been provided to Assessing Officer during the course of assessment proceedings, and further details were filed in the course of remand proceedings. It was emphasized by Ld.Counsel that, in remand report dated 27.7.2009, Assessing Officer made no adverse comments on assessee's submissions, and in fact accepted that there were brought forward balances in total amounts advanced. Ld.Counsel with reference to remand report contended that, case of Assessing Officer mainly was that, in case funds had not been diverted to group companies, then these could have been utilized by assessee for its own business purposes, and to that extent burden of interest would have been lower. This aspect of matter was countered by Ld.Counsel by relying on following judgements:

Amna Bai Hajee Issa vs. CIT (1964) 51ITR 835 (Mad.)

Ram Kishan Oil Mills vs. CIT (1965) 56 ITR 186 (MP)

CIT vs. Bombay Samachar Ltd. (1969) 74 ITR 723 (Bom)

Caldern Pharmaceuticals Ltd vs CIT (2004) 265 ITR 244 (Cal)

33.5. Ld.Counsel placed reliance on following judgements for proposition that advances to subsidiaries/group companies were to be considered as commercially expedient and for business consideration unless there was a finding that the amount advanced had been misused or that the transaction was not genuine in nature:-

S.A. Builders Ltd. vs CIT 288 ITR 1 (SC)

C.I.T. vs. Dalmia Cement (Bharat) Ltd., in IT A No.249- 250/1987 passed by Hon'ble Delhi High Court on 24.7.2009

C.I.T. vs. Reliance Utilities And Power Limited (Bom), in IT A No.1398 of 2008 passed by Hon'ble Bombay High Court on 9.1.2009.

Pinnacle Project and Infrastructure Pvt. Ltd.,290 ITR (AT) 45 (Ahmd.)

33.6. Ld.Counsel submitted that since no borrowed funds had been advanced to group companies, and total outstanding contained substantial element of brought forward balances. It was urged that there was no justification either on facts or in law on part of Ld.AO, in making proportionate disallowance.

34. We have perused submissions advanced by both sides in the light of the records placed before us. It is observed that Ld. CIT (A) has analysed aforestated submissions of assessee as under:

"6.2. I have considered the submissions of the learned counsel with reference to the material placed on record in the paper book as also

the details appended to the written submissions and which admittedly have also been filed with the Assessing Officer. The two remand reports of the Assessing Officer have also been taken into account in deciding the present ground along with the counter comments of the appellant.

6.3. As rightly contended by the learned counsel, the Assessing Officer has not made any adverse observation in the remand report dated 27.7.2009 and it may be mentioned as a matter of record that in the remand proceedings the appellant placed on record detailed bank accounts, bank certificates, extracts m audited accounts and funds flow statement in the proceedings conducted y the Assessing Officer in response to the directions given to him in the order dated 3.10.2008 passed u/s 250(4) of the Act.

6.4. In my opinion the disallowance of Rs.13.52 crores is neither justified on facts nor in law since the advances to group/subsidiary companies have been given on grounds of commercial expediency and a substantial portion thereof consists of brought forward opening balances which have no nexus with the funds borrowed during the year under consideration on which interest has been paid. In the case of one of the companies, namely Escotel Mobile Communication Limited there is a reduction of aroundRs.2 crores out of the opening balance itself and no further funds have been advanced to the said company during the year under consideration.

6.5.As regards the advances to Escorts Construction Equipment Limited there is a fresh infusion of funds advanced to the tune of Rs.5,76 crores and in respect of which detailed evidence was filed in

the remand proceedings which has not been controverted by the Assessing Officer in his remand report dated 27.7.2009.

6.6.Following the judgments relied upon by the learned counsel, I delete the adhoc disallowance of Rs. 13.52 crores with the further observation that it is not the requirement of law that an appellant must further show that the borrowing was necessary for business, so that if at the time of borrowing the appellant had sufficient funds of its own, the deduction could not be allowed. Thus, the view that the appellant could have decreased the extent of his borrowing and the burden of interest cannot be sustained CIT vs Bombay Samachar Ltd., 74 ITR 723, 731 (BOM)] .

35. We do not find any infirmity in aforestated findings of Ld.CIT (A) which is based on detailed analysis. Accordingly the same is upheld.

In the result this ground raised by revenue stands dismissed.

36. Ground no.3 raised by revenue pertains to proportionate disallowance of a sum of Rs.72,32,00,000/- out of interest paid during the year under consideration.

36.1.Ld.Sr.DR submitted that Ld.AO in para 4.2 referred to investments of huge sums of money in group companies/subsidiaries by assessee which according to him did not bring in any returns. The amount of investment was a sum of Rs.602.66 crores, out of which fresh investments during previous year under consideration amounted to Rs.168.36 crores. He submitted that assessee on one hand was paying huge amount of interest and bank/finance charges and on the other it placed its

funds in investments which did not generate any income. Ld.Sr.DR submitted that, assessing officer was right in making proportionate disallowance by adopting rate of interest at 12%, which could have been saved in case assessee used the funds for its own business purposes.

36.2.On the contrary, Ld.Counsel placed reliance upon submissions made by assessee before Ld.CIT (A). For sake of convenience, we are reproducing submissions advanced by Ld.Counsel before Ld.CIT (A) as under:

36.3.Ld.Counsel on the other hand submitted that during the course of appellate proceedings, various submissions were made, which were placed on record, and copies thereof were forwarded to Ld.AO for his comments. Ld.Counsel submitted that disallowance had been made without confronting assessee during the course of assessment proceedings, which tentamounted to violation of principles of natural justice. On merits Ld.Counsel submitted that, no funds borrowed on interest had been utilized for purchase of shares of group companies/subsidiaries either in the past, or in the year under appeal. It was submitted that in none of the preceding assessment years Assessing Officer held such investments in shares as being for non business purposes, and in fact he had not even recorded any finding in the year under consideration.

36.4.Ld.Counsel submitted that out of total investments of Rs.602.66 crores in shares of group/subsidiary companies as on 31.3.2003, there was an opening balances on 1.4.2002 to the tune of Rs.516.18 crores. Ld.Counsel submitted that Ld.AO recorded a

finding that investments in question namely, sum of Rs.602.66 crores, did not result in any income to assessee, and in case funds had been utilized by assessee for business purposes, then burden of interest payments would be on lower side. According to Ld.Counsel aforesaid facts noted by Ld.AO were factually incorrect, in as much as, substantial dividend income had resulted from aforesaid investments and duly brought to tax. Further, capital gains arising on sale of some investments in shares had been assessed as capital gains. Ld.Counsel with reference to material and documents placed in paper book contended that dividend income to the tune of Rs.68 crores on shares in question had been brought to tax, as would be evident from page 7 of assessment order it could be noted that, capital gain to the tune of Rs.94.25 crores had been brought to tax. Ld.Counsel there after referred to Profit & Loss Account for year under consideration, contending that net income to the tune of Rs.208.63 crores on the investments had been shown in the accounts. According to Ld.Counsel Assessing Officer in his remand report dated 27.7.2009 had accepted the following facts:-

- That the investments had been made in the shares of subsidiary/group companies.
- Assesssee had been making investments on regular basis from year to year in the shares of group companies and a detailed fund flow statement of such investments from the AY 1996-97 to AY 2003- 04 had been filed.

- It had been accepted by the Assessing Officer that the appellant had not claimed any tax exempt income in its return and therefore no disallowance u/s 14A of the I. T. Act had been made.

36.5. According to Ld.Counsel, no disallowance under aforesaid provision viz, Section 14-A had been made during assessment stage, and rightly so, but on the matter being remanded to Assessing Officer u/s 250(4) of the I. T. Act by the then CIT (Appeals) vide order dated 3.10.2008, Ld.AO was directed to examine its applicability. Ld.Counsel further went on to state that, vide para 2 of the said order Ld.AO had been asked to examine, as to whether any interest bearing funds had been invested in acquisition of shares of group companies. For purpose of carrying out this verification, assessee was asked to file copies of accounts in respect of investment in shares linking the same to bank accounts for relevant periods, *vis a-vis* nexus of funds with investments. According to Ld.Counsel, complete details were furnished to Ld.AO vide letter dated 10.11.2008 to enable Ld.AO to comply with order u/s 250(4) of the Act.

36.6. It was submitted that, assessee furnished complete details of fresh investments made during the period ending 31.3.2003 in shares amounting to Rs.168.36 crores, and had also furnished fund flow statement for the proposition that during previous year under consideration, funds generated by sale of shares of certain companies amounting to Rs.251.42 crores along with dividend

income of Rs.68 crores, aggregating to Rs.319.42 crores, fully covers fresh investment of Rs.168.36 crores.

36.7. As regards issue of interest bearing funds having invested in acquisition of shares of group companies during preceding years Ld.Counsel referred to letter dated 10.11.2008 addressed to Ld.AO, wherein it is categorically asserted that, no interest bearing funds are invested even in preceding assessment years for making investments in shares of group companies. Ld counsel further asserted that, these investments were made out of funds available in business from time to time, by way of sale of investments, dividend received, interest on loans given, and fresh issue of share capital at a premium, and aggregate of such funds in each year were more than adequate, to enable assessee to make investments in shares of group companies from year to year. It was submitted that there were sufficient cash profits from business activities, which were deployed for purposes of investments in shares. Ld.Counsel drew attention to page 4 of letter dated 10.11.2008, contending that all aforesaid submissions were duly supported by evidence in the form of fund flow statement, beginning from AY 1996-97 upto AY 2003-04, which according to him were verifiable from the tax returns and the balance sheets which were already available in the records of the Department.

36.8. With reference to aforesaid factual submissions Ld.Counsel referred to remand report dated 27.7.2009, forwarded by Ld.AO contending that there was no adverse comment. In support of his arguments, he placed reliance on the following judgments

contending that the disallowance not being maintainable both on facts and in law, the same be deleted:

S.A. Builders Ltd. vs CIT 288 ITR 1 (SC)

C.I.T. vs. Dalmia Cement (Bharat) Ltd., in IT A No.249- 250/1987 passed by Hon'ble Delhi High Court on 24.7.2009

C.I.T. vs. Reliance Utilities And Power Limited (Bom), in IT A No.1398 of 2008 passed by Hon'ble Bombay High Court on 9.1.2009.

Pinnacle Project and Infrastructure Pvt. Ltd.,290 ITR (AT) 45 (Ahmd.)

37. We have perused submissions advanced by both sides in the light of the records placed before us.

37.1. It is observed that Ld. CIT (A) decided this issue by observing as under:

"I have carefully considered the submissions of the learned counsel for the appellant with reference to the paper book, written submissions filed from ime to time as also the case laws relied upon. The two remand reports received from the Assessing Officer and the counter comments of the appellant thereon have also been taken into account.

7.7 *I would like to observe that the order of the Assessing Officer has proceeded on erroneous grounds in as much as relevant facts of the case have either been wrongly recorded or not noted at all. This has happened because the appellant was not put on notice during the course of the assessment proceedings leading to the adhoc disallowance in question.*

7.8 *There are two main limbs to the order of the Assessing Officer the first being that the investments are not for business purposes having not brought in any return and the second being that in case the funds had been utilized for business purposes then the burden of interest expenditure would have been lower. The material on record clearly nullifies the first observation since the investments are in shares of group companies and dividend income to the tune of Rs.68 crores have been subjected to tax on these investments as appearing at page 7 of the assessment order. Further, capital gains on some investments sold during the year to the tune of Rs.94.25 crores have also been subjected to tax. It was not the case of the Assessing Officer that Section 14-A was applicable and which was also the observation in the remand report pursuant to the order passed u/s 250(4) on 3.10.2008.*

7.9 *In not bringing on record the relevant and correct facts the Assessing Officer has further included the opening balance of Rs.516.80 crores being the investment in shares of group companies made in several preceding assessment years whereas there could possibly be no nexus between the interest expenditure in AY 2003-04 and the shares acquired before the beginning of relevant previous year, i.e. 1.4.2002. In my opinion the opening balance could not have been the subject matter of the adhoc disallowance.*

7.10 *The investment in shares of group companies made from year to year as also the year under appeal is definitely for in purpose of business and commercial expediency. It has resulted in substantial income to the appellant company in the form of dividend and capital*

gains which have been subjected tax during the year under consideration as is apparent from the appellant's audited accounts, the income-tax return and the assessment order. The Assessing Officer in the two remand reports has not factually or legally contradicted the evidences & material placed by the appellant on record whereby it was shown that the investment in shares even in numerous preceding assessment years had come out of the appellant's own funds and not borrowed funds. The Assessing Officer in his remand report dated 27.7.2009 has not made any adverse comments on the funds flow statement and other documents filed with him by the appellant while accepting at the same time that the investments had been made in the shares of group companies and Section 14A was not applicable since the assessment records showed that there was no tax exempt income during the AY 2003-04.

7.11 *The remand report also does not distinguish the numerous judgments relied upon by the appellant during the course of the remand proceedings. The first of these is the judgment of the Hon'ble Supreme Court in the case of S.A. Builders Limited vs. CIT 288 ITR 1 where the Apex Court held that in a case where money had been borrowed from bank on interest and lent to a sister concern without charging interest there could be no disallowance of the proportionate interest unless there was a finding of mis-use of funds for personal purposes by the directors of the company. It is the stand of the appellant before me that its case stands on a better footing since (i) the investments in the shares of group companies have resulted in substantial income and (2) the investments have not come out of*

borrowed funds but out of the appellant's self generated funds. The other decision relied upon is that of the Hon'ble Delhi High Court dated 24.7.2009 in the case of Dalmia Cement Bharat Limited wherein following the judgment of S.A. Builders (supra) it was held that investment in subsidiary companies was for commercial expediency and on business considerations. The other decisions relied upon were those of the Hon'ble Bombay High Court in the case of Reliance Utilities And Power Limited and a judgment of the Ahmadabad Bench of the I.T.A.T. in the case of Pinnacle Project And Infrastructure Pvt., reported in 290 ITR (AT) 45, the said decision also dealing with interest borrowed money being utilized for purchase of shares in group companies.

7.12 *I have considered the aforesaid judgments and do hold that these are squarely applicable to the facts of the appellant's case more so when the Assessing Officer has not been able to establish any nexus between the funds borrowed during the period under consideration on interest and the investments made in the shares of group companies either in the AY 2003-04 or in any of the preceding assessment years.*

7.13 *As regards the stand of the Assessing Officer that the funds if utilized for business purposes and not invested in shares of group companies would have resulted in a lower interest burden, the argument does not hold good in the light of the view taken that the investments are clearly for business purposes.*

7.14 *In conclusion, I would hold that the Assessing Officer was not justified in making the adhoc disallowance of Rs.72,32,00,000/- both*

on facts and in law in as much as the investment in shares of group companies was on grounds of business expediency and commercial considerations. The disallowance is accordingly deleted.

We do not find any infirmity in aforestated detailed factual analysis carried out by Ld.CIT (A), based upon which, addition has been deleted. We accordingly uphold the view of Ld.CIT (A).

In the result this ground raised by revenue stands dismissed.

38.Ground No.4 raised by revenue pertains to deleting of disallowance amounting to Rs.32,00,000/- paid as upfront fees.

Ld.Sr.DR placed reliance on order of Ld.AO however, he could not controvert submissions of Ld.Counsel.

38.1. Ld.Counsel placed reliance on order passed by Ld.CIT(A).

We have perused submissions advanced by both sides and perused records placed before us

It is observed that, Ld.CIT(A) decided this issue as under:

"8. Ground no.7 pertains to disallowance of a sum of Rs.32,00,000/- as upfront fee paid to banks. According to AO the expenditure was capital in nature whereas the case of the appellant was that it was a revenue expenditure and had been accepted in quite a few preceding AYs. The AO in fact followed the order of his predecessor for AY 1999-2000. The Ld.Counsel for appellant contended that the issue was squarely covered in favour of appellant by judgments of Tribunal for preceding AYs including AY 1999-2000. He placed on record copies of orders for such preceding AYs including 1998-99, 1999-2000 and 2001-02. The Ld.Counsel also placed on record copy of recent order passed by CIT(A)-II, New Delhi for AY 2006-07 wherein

question of upfront fee have been considered taking into account judgment of various High Courts including that of madras High Court in case of CIT vs. Sri Meenakshi Mills Ltd. 290 ITR 107. The issue of upfront fee in view of the aforesaid submission is covered in favour of appellant and disallowance of Rs.32 lakhs is accordingly deleted."

38.2. We have upheld view of Ld.CIT(A) on similar issue in Ground No.2 for A.Y:2002-03, in para 12 herein above. . Following the same we are inclined to uphold the view taken by Ld.CIT (A).

In the result this ground raised by revenue stands dismissed.

39. Ground No.5(a) & 5(b) raised by revenue pertains to deleting of disallowance amounting to Rs.35,75,330/- on account of proto-type development.

39.1. Ld.Counsel submitted that issue was covered in favour of assessee, by order of this Tribunal for Assessment Year 2001-02, which we followed in forgoing paragraphs, while deciding revenue's appeal for assessment year 2002-03. According to Ld.Counsel, there is no change in facts and issue stands squarely covered as contended therein. It was emphasized that Ld.AO in remand report dated 09.03.2007 had not made any comments on written submissions filed by assessee vide letter dated 31.05.2006.

39.2.Ld.Sr.DR placed reliance on order of Ld.AO, however, he could not controvert submissions of Ld.Counsel.

40. We have perused submissions advanced by both sides and perused records placed before us

40.1. It is observed that, Ld.CIT(A) decided this issue as under:

"9.2. After considering the statement of the learned counsel and perusing the material on record, I am of the view that the issue is squarely covered by the order of Tribunal for the Assessment year 2001-02 and in the absence of any change in facts or any adverse comments by the AO the addition of Rs.35,75,330/- is deleted."

We have upheld the view of Ld.CIT(A) on this issue for A.Y:2002-03, which has been consistent in preceding assessment years.

Accordingly this ground raised by revenue stands dismissed.

41. Ground No.6 raised by revenue**,** pertains to deleting disallowance on account of professional charges having been incurred to the tune of Rs.7,92,67,976/- on various projects.

41.1. Ld.Counsel contended that the issue stands squarely covered in favour of assessee, in as much as Ld.AO himself had not made any disallowance in AY 2001-02. Further payments have been made to various professionals for rendering services in many areas such as development of effective distribution net work, developing comprehensive marketing strategies covering products, brands, etc., warehouse management system for overall optimization and cost reduction, as also the designing of sound management information system. The expenditure on these services cannot by any stretch of imagination be called capital in nature. He further contended that benefit of many items of revenue expenses may extend to a period covering more than one accounting year but on that basis such expenses cannot be treated as capital in nature.

41.2.Ld.Counsel submitted that, expenses on account of professional charges were incurred in the course of normal routine

business activities, in its existing line of business. It has been submitted that complete details were filed before authorities below, in support of this claim. He argued that in consistence with past assessments, where no such disallowance has been made on same set of facts, there being no adverse comments on the part of Ld.AO, in remand report dated 9.3.2007, claim has been rightly allowed as revenue expenditure.

41.3. Ld.Sr.DR placed reliance on order of Ld.AO, however, he could not controvert submissions of Ld.Counsel

42. We have perused submissions advanced by both sides and perused records placed before us

42.1. It is observed that, Ld.CIT(A) decided this issue as under:

"10.2. I have carefully considered the submissions and perused the material on record placed on the paper book. The written submissions filed from time to time as also the remand report dated 9.3.2007 have been taken into account The remand report does not make any adverse comments on the claim or for that matter the written submissions of the appellant company filed during the course of hearing. In my view also the expenditure on professional charges paid in respect of day to day activities vis-a-vis the existing business the appellant company cannot be treated as of capital nature and have to allowed as revenue expense. Accordingly, the addition of Rs.7,92,67,976/- deleted."

42.2.We uphold view of Ld.CIT(A), which is based on remand report by Ld.AO.

Accordingly this ground raised by revenue stands dismissed.

43. Ground no.7 raised by revenue pertains to deleting addition of Rs.28,07,055/- on account of prior period expenses.

43.1. Ld.Counsel stated that, although accounts were being maintained on mercantile basis, there were certain items of expenses from year to year, which were booked in the accounts, only after due verification and approval process is completed. It was pointed out that expenditure was revenue in nature, being personnel expenditure, purchase/consumption of raw material and major chunk being sales and administrative expenses to the tune of Rs.24,30,991/- out of total disallowance. A reference was made to pages 159 to 198 of Paper Book with further submissions that verification for payment had taken place during assessment year 2003-04, although bills pertain to preceding assessment year. It was further submitted that, considering huge quantum of volume of business of assessee, it was quite normal for some expenditure items to be left out for consideration in the relevant assessment year due to delayed verification and approval being delayed. Ld.Counsel submitted that Ld.AO in his remand report dated 09.03.2007 had not made any adverse comments and that the issue was in fact covered by order of Tribunal for assessment year 2001-02 in assessee's own case. It was therefore urged that disallowance may be deleted.

43.2. Ld.Sr.DR placed reliance on order of Ld.AO, however, he could not controvert submissions of Ld.Counsel.

44. We have perused submissions advanced by both sides and perused records placed before us

44.1. It is observed that, Ld.CIT(A) decided this issue as under:

"11.1.*After considering the submissions and perusing the material placed on Paper Book, I am of the view that on the facts of the present case it can be assumed that some expenditure items may not have been booked in accounts under the mercantile system of accounting due to various reasons vis. Pending verification, late receipt of bills, delayed approval etc., but the 7VCN expenses nonetheless pertain to business of the appellant. The similar issue had been considered in detail by the Hon'ble Tribunal in A.Y. 2001-02 in the appellant's case and on the facts of the case the disallowance deserves to be deleted. Following the orders of the Tribunal on the same issue the disallowance is not sustainable and accordingly the addition of Rs.28,07,055/- is deleted."*

We do not find any infirmity in the analysis carried out the island CIT (A). We have upheald consistent view of Ld.CIT(A) on this issue for A.Y:2002-03, in preceding assessment years.

Accordingly this ground raised by revenue stands dismissed.

In the result, appeal filed by revenue for assessment year 2003-04 stands dismissed.

A.Y. 2005-06

ITA No. 5408/Del/2014 (Revenue's appeal)

Grounds raised by revenue in this appeal are as under:

1. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the addition of Rs.22,00,00,000/- made out of interest expenses.

2. On the facts and circumstances of the case and law, the Ld.CIT(A) has erred in deleting the addition of Rs.98,25,000/- made by treating 25% of royalty payment as capital expenditure.

3. That the appellant craves leave to add, alter or amend any ground(s) of appeal raised above at the time of hearing.

It is prayed that the order of the Ld.CIT(A)-XX, New Delhi being contrary to the facts on record and the settled position of law, be set aside and that of the A.O.be restored."

46.1. Ground No.1 raised by revenue pertains to deleting addition of Rs.22 crores, made out of interest expenses.

46.2. Ld.CIT.DR submitted that said amount was on account of interest computed by Ld.AO. Placing reliance on observations of Ld.AO, he submitted assessee made investments of Rs. 7.66 Crores and Rs.175.74 crores in Escorts Agri Machinery Incorporated, USA and M/s Idea Mobile Communications Ltd., respectively without charging any interest during the year. Ld.AO observed that assessee debited interest and finance charges to Profit & Loss Account for Rs.94.32 crores and Rs.16.71 crores respectively, during the year. Ld.AO observedthat assessee had sufficient own funds but had borrowed heavily and paid high interest and bank/charges. Ld.AO was of opinion that assessee made above deposits without any interest. Ld.Sr. DR thus submitted that assessing officer was right in computing notional interest of Rs. 22 Crores in the hand of assessee at the rate of interest at 12% on the above investments.

46.3. On the contrary, Ld.Counsel submitted that investment of Rs 175.74 Crores in M/s. Idea Mobile Communication Ltd was from

sale proceeds of investment in M/s Escotel Mobile Communications Ltd (Escotel) for a sum of Rs.278.10 crores. It was submitted that, amount realized on sale of investments was far in excess of fresh investments made during the year. It was submitted that assessee had to recover substantial amount from Escotel on account of loan and other recoverable dues aggregating Rs.175.74 crores. The appellant stated that along with sale of investment in Escotel, recoverable dues were also settled by allotment of unsecured Subordinate Bond of Idea Mobile Communication for a sum of Rs. 175.74 crores and value of the said Bond was reflected under the head 'investment'. The appellant has explained that there was no fresh investment during AY 2005-06 and there was a mere conversion of the existing debt into an investment. As regards investment of Rs.7.66 crores in share capital of M/s Escorts Agri Machinery incorporated in USA. It was submitted that this company is wholly owned subsidiary, and the same has been made to supplement its existing investment. It was submitted that exports of assessee are carried out through company in USA and investment has been made entirely for business purposes. Placing reliance om case of *S.A. Builders Ltd Vs CIT 288 ITR 1*, it was submitted that *Hon'ble Supreme Court* has held that in a case where money had been borrowed from bank on interest and lent to sister concern without charging interest, there could be no disallowance of proportionate interest, unless there was a finding of misuse of funds for personal purpose by the directors of the company.

46.4. Ld.Sr.DR placed reliance on order of Ld.AO, however, he could not controvert submissions of Ld.Counsel.

47. We have perused submissions advanced by both sides and perused records placed before us

47.1. It is observed that, Ld.CIT(A) decided this issue as under:

".....The facts of the present case are exactly similar to the facts as in AY 2003-04. Out of Rs. 183.40 crores, the appellant has explained that the investment of Rs. 175.74 crores in Subordinate Bond of Idea Mobile Communication is only a conversion of existing debts and there was no fresh investment. As regards the fresh investment of Rs.7.66 crore in the share capital of M/s Escorts Agri Machinery incorporated in USA which is the wholly owned subsidiary company, the appellant has explained that the same has been made to supplement its existing investment. Respectfully following the decision of the Ld. CIT(A)-III for AY 2003-04, the AO is directed to delete the addition of Rs. 22 Crores on account of notional interest. This ground of appeal is allowed"

47.2. We have upheld view of Ld.CIT(A) on this issue for A.Y:2002-03, which has been consistently followed in preceding assessment years.

Accordingly this ground raised by revenue stands dismissed.

48. Ground 2 raised by revenue pertain to disallowance of 25% of royalty amounting to ₹ 3.93 crores made to Harprasad & Company Pvt.Ltd., being deleted. Learned senior DR submitted that assessee was found to have debited ₹ 3.90 crores towards royalty during relevant year. Learned AO following the decision of Hon'ble

Supreme Court in case of M/s Southern Switchgear Ltd versus CIT reported in (1997) 232 ITR 359 disallowed 25% of the expenditure and added back to the income. He submitted that assessing officer was right in treating 25% of the expenditure as capital nature and the same is to be upheld.

48.1.On the contrary, Ld.Counsel submitted that, assessee was paying royalty to Harprasad & Company Pvt.Ltd. for use of trade name/trade mark 'Escorts". It has been submitted that this is a recurring issue and this Tribunal for assessment year 2004-05 has deleted the addition which has been followed by Ld.CIT (A) in the year 2006-07. Ld.Counsel submitted that royalty was paid for use of the name "Escorts" for the purpose of selling its product and there was no acquisition of any technical know-how or any other intangible property by assessee.

49. We have perused submissions advanced by both sides, in light of records placed before us.

49.1.It is observed that learned CIT (A) deleted addition by observing as under:

"6.3. The appellant company had debited a sum of Rs. 3.93 crores towards royalty during the year. Following the decision of the Hon'ble Supreme Court in the case of Ms. Southern Switch Gear Ltd. Vs. CIT[1997] (232 ITR 359) the AO has treated 25% of the royalty as capital in nature and disallowed the amount of Rs. 98,25,000/- of the royalty payment. The appellant has explained that the royalty has been paid for the use of trade name 'Escorts' for the purpose of selling the products and there is no acquisition of any technical

know-how or any other intangible property by the appellant. The appellant has also stated that the disallowance of similar nature for A.Y. 2004-05 has been deleted by the Hon'ble ITAT, Delhi. Vide the order dated 25/02/2010 in ITA No.2221/Del/2009 in the appellant's own case for AY 2004-05, the Hon'ble as held that "... From the record, we found that in terms of the agreement executed by the assessee with M/s Harprashad & Co., the assessee was to make recurring payment of royalty every year calculated at the rate of 0.25% of the turnover. Such payment has been confirmed by the deed of confirmation signed between directors of the assessee company and Company Secretary of M/s. Harparshad & Co. The royalty was payable for limited use of trade mark 'Escorts'. The genuineness of the expenditure was admittedly not in dispute. Assessee was making payment of royalty since AY 2001-02 and same was allowed as revenue expenses. Upto the assessment year under consideration, the royalty payment so claimed was allowed under scrutiny assessment u/s 143(3) as revenue expenditure. Only during the year under consideration, the CIT has invoked his powers u/s 263 on the plea that some of the facts are similar to the facts of the case of M/s. Southern Switchgear Ltd. (supra). In this case, Hon'ble Supreme Court affirmed the order of Hon'ble Madras High Court wherein on the finding of fact recorded by tow appellate authorities to the effect that duration of the agreement though of five years, assessee could use technical know-how even after expiry thereof which amounted to acquisition of know-how of enduring nature, part payment of technical know-how fee was held to be capital in nature. However,

the facts in the instant case are distinguishable wherein only during the period of agreement, the assessee was having the right to use the trademark, which did not give any right of enduring nature and since the annual payment of royalty for use of trademark was based on turnover, the expenditure was essentially in the nature of revenue expenditure and not capital expenditure In view of above discussion, we can safely conclude that royalty payment was revenue in nature and no party of it was liable to be disallowed by considering the same as capital expenditure." In AY 2006-07 the Ld. CIT(A) has also deleted the addition on account of royalty payment. Respectfully following the decision of the Hon ble ITAT Delhi for AY 2004-05 and also the order of the Ld. CIT(A) for AY 2006-07,

I hold that the royalty payment is allowable as revenue expenditure. Accordingly, the AO is directed to delete the amount of Rs. 98,25,000/- on account of the royalty payment. This ground of appeal is allowed."

49.2. For the sake of convenience ,we shall also reproduce view taken by this Tribunal in assessee's own case for A.Y. 2004-05 as under:

"5. We have considered the rival contentions, carefully gone through the orders of the authorities below and also deliberated upon the various case laws cited by the learned AR in the context of factual matrix of the case. From the record, we found that in terms of the agreement executed by the assessee with M/s. Harparshad & Co, the assessee was to make recurring payment of royalty every year calculated at the rate of 0.25% of the turnover. Such payment has

been confirmed by the deed of confirmation signed between directors of the assessee company and Company Secretary of M/s. Harparshad & Co. The royalty was payable for limited use of trade mark 'Escorts'. The genuineness of the expenditure was admittedly not in dispute. Assessee was making payment of royalty since AY 2001-02 and same was allowed as revenue expenses. Upto the assessment year under consideration, the royalty payment so claimed was allowed under scrutiny assessment u/s 143(3) as revenue expenditure. Only during the year under consideration, the CIT has invoked his powers u/s 263 on the plea that some facts are similar to the facts of the case of M/s. Southern Switchgear (supra). In this case Hon'ble Supreme Court affirmed the order of Hon'ble Madras High Court wherein on the finding of fact recorded by tow appellate authorities to the effect that duration of the agreement though of five years, assessee could use technical know-how even after expiry thereof which amounted to acquisition of know-how of enduring nature, part payment of technical know-how fee was held to be capital in nature. However, the facts in the instant case are distinguishable wherein only during the period of agreement, the assessee was having the right to use the trademark, which did not give any right of enduring nature and since the annual payment of royalty for use of trademark was based on turnover, the expenditure was essentially in the nature of revenue expenditure and not capital expenditure. On the other hand, Hon'ble Jurisdictional High Court in the case of J.K. Synthetics - 309 ITR 371 held that payment made for acquisition of know-how which facilitated day to day operation of its

business, without transfer of any ownership in such know-how or transfer of patent or trademark was allowable as revenue expenditure. In the instant case also, the right to use the trademark was also limited without transfer of any ownership over the trademark. Thus, the expenditure on royalty which is recurring in nature being paid every year, cannot be said to be capital expenditure. As per our considered view, expenditure incurred towards initial outlay of business would normally be in the nature of capital expenditure, however if the expenditure is incurred while the business is going on, it would have to be ascertained if the expenditure is made for acquiring or bringing into existence an asset or an advantage of enduring benefit for the business, if that be so, it will be in the nature of capital expenditure. However, on the other hand, if the expenditure is for running the business or working it, with a view to produce profits it would be in the nature of revenue expenditure. Furthermore, it is the aim and object of the expenditure which would determine its character. The test of "once and for all" payment i.e. a lump sum payment made, in respect of a transaction is an inconclusive test. In view of above discussion, we can safely conclude that royalty payment was revenue in nature and no party of it was liable to be disallowed by considering the same as capital expenditure. "

Similar disallowance for assessment year 2006-07 has been deleted by the learned CIT(A). The relevant extract of the order is reproduced below:-

"9.3 I have considered the facts of the case. The submissions of the appellant have also been gone through. It is true base on the material submitted by the appellant that the payment of royalty @0.25% of the total turnover is evidenced by Minutes of the Meeting of Board of Directors of Harparshad and Company Pvt. Ltd. held on 1/2/2001 which has been specifically confirmed by way of Deed of Confirmation signed between Shri 'R'ajan Nanda, Chairman and Managing Director of Escorts Ltd. and Shri Kedo jr Nath Sachdeva, Company Secretary for Harparshad and company as a Trade Mark which is evidenced by the Deed of Confirmation. The genuineness of the expenditure is admittedly not under dispute. The claim of appellant is also found correct that this expenditure has been allowed in full in earlier year also. The reasons given by the A.O. for the disallowance is only base on the decision of Apex Court in the case of Southern Switchgear Ltd. Vs. CIT (supra). I have gone through the decision relied upon by the A.O. and on going through the same, I agree with the appellant that this decision is squarely distinguishable and not applicable to the facts of the appellant's case as in that case under the terms of the agreement that company agreed to pay to the foreign company as consideration for the services rendered by it, a royalty on sales and a lump sum for the technical aid, payable in five equal installments, the payment to be spread over a period of time. The Tribunal disallowed 25% of the technical fees and 25% of the royalty paid by the assessee to the foreign company. The Hon'ble Madras High Court has upheld the action of Tribunal of disallowing 25% of the royalty as in that case

the Hon'ble Tribunal held that by making a payment towards royalty the appellant has obtained the technical knowledge which is an enduring advantage and benefits and same will be available to the assessee even after the termination of the agreement. This decision of the Hon'ble High Court has been upheld by the Hon'ble Supreme Court also. But in the instant case, the facts are totally different. Royalty is not being paid for acquiring any technical knowledge which may give any enduring benefit. Rather in this case royalty is being paid only for the use of name "Escorts" which is owned by Harparshad and Company Pvt. Ltd. Therefore, it cannot be said that by making this payment any enduring benefit is being obtained. Thus, the facts are distinguishable and, therefore, the decision is not applicable. In my opinion, this is a clear cut case of revenue expenditure. Not only that, it has been allowed in earlier years also be the A.O. in full as revenue expenditure. Therefore, royalty payment is directed to be allowed in full. The disallowance so made by A.O. of Rs.1,00,75,000/- is directed to be deleted."

49.3. We do not find any infirmity in a consistent view adopted by Lord CIT (A). It has been submitted that the facts are identical to assessment year 2004-05 and 2006-07.

Accordingly, this ground raised by revenue stands dismissed.
In the result appeal filed by revenue for A.Y. 2005-06 stands dismissed.

Order pronounced in the open court on 06th March, 2019.

Sd/-	**Sd/-**
(N.K.BILLAIYA)	**(BEENA A PILLAI)**
ACCOUNTANT MEMBER	**JUDICIAL MEMBER**

Dt. 06th March, 2019

Copy forwarded to: -

1. Appellant
2. Respondent
3. CIT
4. CIT(A)
5. DR, ITAT

- TRUE COPY -

By Order,

ASSISTANT REGISTRAR
ITAT Delhi Benches

	Date
Draft dictated on	20/02 to 26/02
Draft placed before author	27/02 28/02
Draft proposed & placed before the second member	
Draft discussed/approved by Second Member.	
Approved Draft comes to the Sr.PS/PS	
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File sent to the Bench Clerk	
Date on which file goes to the AR	
Date on which file goes to the Head Clerk.	
Date of dispatch of Order.	