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IN THE INCOME TAX APPELLATE TRIBUNAL, MUMBAI BENCH "E", MUMBAI

BEFORE SHRI P.M.JAGTAP (A.M) & SHRI N.V.VASUDEVAN(J.M)

ITA NO. 4602/MUM/2001(A.Y. 1997-98)

The Addl. CIT, Spl.Range - 34, Aaykar Bhavan, Room No.482, 4th Floor, MK Road, Mumbai - 20. (Appellant)	Vs.	M/s. Nicholas Piramal India Ltd., 4th Floor, Nicholas Piramal Tower, Ganpatrao Kadam Marg, Lower Parel (W), Mumbai - 400 013. PAN: AAACN 4538P (Respondent)

C.O. NO.119/MUM/2002
(Arising out of ITA No.4602/M/01, A.Y. 1997-98)

M/s. Nicholas Piramal India Ltd., 4th Floor, Nicholas Piramal Tower, Ganpatrao Kadam Marg, Lower Parel (W), Mumbai - 400 013. (Cross Objector)	Vs.	The Addl. CIT, Spl.Range - 34, Aaykar Bhavan, Room No.482, 4th Floor, MK Road, Mumbai - 20. (Appellant in appeal)

Revenue by : Shri B.Jaya Kumar
Assessee by : Shri Jehangir D. Mistri

Date of hearing : 26/04/2012
Date of pronouncement :

ORDER

PER N.V.VASUDEVAN, J.M

ITA No.4608/Mum/01 is an appeal by the Revenue against the order dt.23.4.2001 of CIT(A)-II, Mumbai, relating to AY 1997-98. The Assessee has filed C.O. No.119/Mum/02 against the very same order of CIT(A).

2. We shall first take up for consideration ITA No.4608/Mum/01, the appeal by the Revenue.

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3. The First Ground of appeal of the Revenue reads as follows:

> "On the facts and in the circumstances of the case and in law, the ld. CIT(A), Mumbai erred:
>
> 1a) In deleting the addition of Rs.29.26 Crores received from Boehringer Mannheim GmbH, Germany (BMG) ignoring the fact that the above receipt constitute income u/s. 28(iv) of the Income Tax Act 1961 in disregard of Supreme Court's decision of CIT vs. G.R.Karthikeyan, 201 ITR 866.
>
> 1b) In deleting the addition of Rs. 29.26 crores received from Boehringer Mannheim GmbH, Germany (BMG) ignoring the fact that the above receipt were receipt to avoid adverse publicity as is evident from the contents of letter dated 14/11/1996."

4. The Assessee is a company engaged in the business of manufacture of pharmaceutical formulations and bulk drugs. During the previous year a company by name Boehringer Mannheim India Ltd. (BMIL) got amalgamated with the Asssessee as per the scheme of amalgamation approved by the Hon'ble Bombay High Court. As per the scheme the appointed date was 1.4.1996. The effective date for amalgamation was 24.7.97. Boeheringer Mannheim India Ltd. (BMIL) had received a payment of Rs. 29.26 crores from Boeheringer Mannheim GmbH, Germany (BMG) in November, 1996. This amount was credited to the capital reserve in the books of the assessee company. Note No.6 forming part of the accounts states as under:

> "An unconditional grant of Rs.2926.17 lakhs received by the erstwhile BMIL after the appointed date from Boeheringer Mannheim GmbH, Germany has been credited to the Capital Reserve. After the merger, certain non-recurring expenses aggregating to Rs.18.61 crores are determined by the new management as pertaining to the period prior of the effective take-over of the company by the new management or are on account of the Comsat incident and accordingly an equivalent amount has been drawn from Capital Grant Reserve during the year and reduced from Other expenses."

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In a note appended to the computation of income, the aforesaid amount received from BMG was claimed by the Assessee to be a capital receipt and therefore, not offered for taxation. The note further mentions the fact that certain non-recurring expenses aggregating to Rs.1860.84 lakhs were incurred by BMIL are deductible expenditure u/s. 37(1) of the I.T. Act.

5. In the course of assessment proceedings, the Assessee reiterated its stand that the receipt from BMG was a capital receipt not chargeable to tax. The Assessee claimed that the receipt in question is an unconditional grant in appreciation of the efforts and actions taken by the erstwhile BMIL to establish, protect and enhance the goodwill and image of BMG in India. The Assessee further claimed that in the last couple of years BMIL has been making persistent losses, consequent upon which the net worth of that company had eroded considerably. Since BMG had an approximately 64% holding in BMIL, the goodwill and image of BMG in India was also likely to be affected. The Assessee submitted that the payment by the German company BMG had to be viewed in the foregoing context. It was claimed by the Assessee that BMG made the aforesaid payment out of benevolence or compassion, it was a payment made without any legal obligations on its part to do so and that BMIL had no legal right to receive the same from BMG. It was claimed that the amount received was an unconditional grant from BMG which does not relate to any particular source of income or any specific reimbursement of expenditure. It was payment made by BMG, being a substantial stakeholder in BMIL, to rectify the erosion in the net worth of one of its subsidiaries. The Assessee in this regard relied on the following decisions wherein the proposition that payment to subsidiary to rectify erosion in net worth is a capital receipt not chargeable to tax has been laid down.

(a) CIT Vs. Handicraft & Handloom Export Corpn. (133 ITR 190) (Del)
(b) CIT Vs. Indian Textile Engineers Pvt. Ltd. (141 ITR 69) (Bom).

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(c) Padmaraje Kudambanda Vs. CIT (195 ITR 877) (SC)
(d) CiT Vs. Stewart & Lloyds India Limited (165 1TR 416)
(e) H.H. Maharani Shri Vjaykuverba Saheb of Morvi Vs. CIT (49 ITR 594) (Bom)
(f) S.R.Y. Sivaram Prasad Bahadur Vs. CIT (82 1TR 527) (SC)
(g) P.H. Divecha Vs. CIT (48 1TR 222) (SC)".

6. The AO however was of the view that the payment in question though was an unconditional grant without any legal obligation on the part of BMG and without any legal right vesting with BMIL to receive the payment was not conclusive that the same is not chargeable to tax. He held that the amount in question was received by virtue of business connection and therefore taxable and further was of the view that the character of the receipt has to be viewed from the point of the recipient and not the giver. In this regard the AO referred to the decision of the Hon'ble Supreme Court in the case of P. Krishna Menon Vs. ITO 35 ITR 48 (SC) wherein it was laid down that the test is from the stand point of the recipient as to whether he receives it by virtue of his occupation and not whether it is voluntary or otherwise in the hands of the giver. The AO further held that Assessee's statement that BMIL has been making persistent losses and as a 64% stakeholder BMG wanted to reimburse the losses was also factually incorrect. In this regard the AO referred to the fact that BMIL in their letter dated 14/11/1996 addressed to BMIL had clearly stated the purpose for which the payment ws made by them to BMIL as under:

> "We refer to our discussions from time to time about the actions being taken by Boehringer Mannheim India Ltd. to establish, protect and enhance the goodwill and image of the Boehringer Mannheim Group in India.
>
> We appreciate the said efforts and particularly the efforts and actions taken in the recent past in the light of the adverse publicity arising from the problems relating to "COMSAT".
>
> As a token of such appreciation and to encourage such efforts, we have today remitted as unconditional grant a sum of US $8.2 million. Please acknowledge the receipt of the same."

According to the AO it was clear from the above that the payment was not connected at all to repairing the erosion in the net worth of BMIL. The payment has been made in order to promote the image of the BMG group. The AO was of the view that the only test for deciding the taxability of the amount was to see whether the receipt arose out of the assessee's business. In this regard the AO referred to the fact that BMG and its associates held 64% of the share capital in BMIL. BMIL was using the brand image of BMG, making use of the technical know-how of the parent company and was also acting as the marketing agent for BMG for sale of diagnostic products, Bio chemicals and Bio catalysts. In the month of August, 1996, a contaminated batch of "Comsat Forte" formulated at the factory of BMIL was released in the market causing severe illness in many cases and 3 deaths. The food and drug administration directed BMIL to withdraw four batches of "Comsat Forte" and also cancelled the license for manufacture and sale of products out of Thane plant. The incident caused adverse publicity for the BMG group. The above payment was paid to BMIL in lieu of the services rendered by BMIL in terms of protecting and promoting the interests of BMG. The AO held that the receipt arises out of the business activity of the assessee. It was clear that the payment was not made to improve the net worth of BMIL and was not in any way connected with the capital structure of BMIL. Accordingly, the receipt was held to be part of the profits and gains of the business carried on by the assessee. The AO also held that the case law relied upon by the assessee were on their own facts and not applicable to the facts of the Assessee's case.

7. Before CIT(A) the Assessee reiterated submissions made before the AO. It was further submitted that the Assessee had no legal right to receive the money from the parent company. It was argued that the payment was made out of benevolence or compassion. The receipt was an unconditional grant

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which does not relate to any particular source of income and therefore was a revenue receipt not chargeable to tax. The CIT(A) accepted the contention of the Assessee and he held as follows:

> "After considering the facts and circumstances of the case and the rival arguments I am of the view that there is no material to hold the receipt in question was income taxable. under any provisions of the Income-tax Act.
>
> From the point of view of the assesses it was gratuitous payment made by the Parent Company without any legal obligation to do so and with no legal right for the assessee to receive it. The receipt was not related to any business services rendered or goods supplied by the assessee to the German Company. Thus the amount was not received by virtue of the business carried on by the assesses company. As the German Company clarified in its letter dated 14/11/1996 addressed to the assessee, quoted by the A.O. in page 4 of the assessment order, it was an unconditional grant given by it. It was an amount given voluntarily without being solicited by the assesses. If the German Company chose not to pay the amount, the assessee had no legal tight to enforce the payment. The receipt in the hands of the assessee cannot be related to any specific source of income or any specific reimbursement of expenditure. The assessee also did not render any services in expectation of or on the promise of any such payment. The payment was in the nature of gift by the German Company which partakes the character of a capital receipt in the hands of the assesses that cannot be subjected to Income-tax,
>
> The assessee argued that the payment has to be viewed in the context of the assessee making persistent losses consequent upon which the net worth of the company had eroded considerably. As a 64% shareholder of the company, BMG came forward with this voluntary payment to ensure that its goodwill and image in India was not affected. It cannot be denied that the assessee company had made losses but for which the parent company would not have come forward voluntarily to make this payment. This was an obvious inference even though the parent company did not say so explicitly in its letter."

The CIT(A) also held that the Assessee was not in the business of public relations or image building and therefore the efforts taken by it to protect and enhance the goodwill and image of the group cannot be said to be part

of its business activity. The CIT(A) also held that the decision of the Hon'ble Supreme Court in the case of P. Krishna Menon (supra) was not applicable because in that case the Assessee was carrying on the vocation of giving discourse in Vedanta and hence the receipt of money from disciples was held to arise from vocation whereas the Assessee received the money in question for nothing.

8. Aggrieved by the order of the CIT(A), the Revenue has raised Gr.No.1 before the Tribunal. The Revenue vide letter dated 22.6.2010 has sought to revise Gr.No.1. Instead Gr.No.1 referred to earlier, the following Ground is sought to be substituted, viz.,

> "1(a) On the facts and circumstances of the case, the ld.CIT(A) erred in deleting the addition of Rs.29.26 Crores received from Boehringer Mannheim GmbH, Germany (BMG) ignoring the fact that the above receipts constitute income under the head "profits and gains of business or profession", in disregard of Supreme Court's decision in CIT Vs. G.R.Karthikeyan 201 ITR 866"

As can be seen from the revised grounds, the only difference is that originally the sum in question was brought to be taxed u/s.28(iv) of the Act, which lays down that the value of any benefit or perquisite, whether convertible into money or not, arising from business or the exercise of a profession is taxable under the head income from business or profession, whereas the revised ground seeks to bring the sum in question to tax u/s.28(i) of the Act which lays down that the profits and gains of any business or profession which was carried on by the assessee at any time during the previous year is chargeable to tax under the head income from business or profession.

9. The learned DR submitted that the payment in question was for services rendered viz., promoting image of the German company in India and Comsat incident. It was submitted that BMG and BMIL are closely connected. There

was therefore a business connection between the two. He submitted that the definition of the word "Income" u/s.2(24) of the Act is a inclusive definition and has very wide connection. He reiterated the case of the AO by relying on the decision of the Hon'ble Supreme Court in the case of Krishna Menon (supra). His submission was that one has to see the reason as to why the sum in question was paid and not to see as to whether the same was voluntary or not. He drew our attention to the decision of the Hon'ble Supreme Court in the case of G.R.Karthikeyan (supra). The facts of the case were that the Assessee an individual, who had income from salary and business, participated in a car rally during the accounting year relevant to the assessment year 1973-74. The rally was restricted to private motor cars. The length of the rally route was about 6,956 kms. One could start from any one of the cities of Delhi, Calcutta, Madras or Bombay, proceed anti-clockwise and arrive at the starting point. The rally was designed to test endurance driving and reliability of the automobiles. A competitor had to drive his vehicle observing traffic regulations as well as the regulations of the rally committee. The method of ascertaining the first prize winner was based on a system of penalty points for various violations, and the competitor with the least penalty points was adjudged the winner of the first prize. On this basis, the respondent won the first prize and received Rs. 22,000 in all, Rs. 20,000 from the Indian Oil Corporation and Rs. 2,000 from the organisers of the rally. The question was whether the sum of Rs. 22,000 was taxable in the hands of the respondent. The Appellate Tribunal found that (a) the rally was not a race; it was predominantly a test of skill and endurance as well as of reliability of the vehicle; (ii) the rally was not a "game" within the meaning of section 2(24)(ix) of the Income-tax Act, 1961; and (iii) the receipt was casual in the nature and not an income receipt; and held that the amount was not taxable. The High Court, on a reference, upheld the decision of the Tribunal holding that the rally was not a race and that the receipt did not represent "winnings" which had acquired the meaning of money won by

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gambling or betting, and that section 2(24)(ix) could not take in the amount received by the respondent in a race which involved skill in driving. On appeal to the Supreme Court, the Hon'ble Supreme Court reversed the decision of the Hon'ble High Court. The learned DR highlighted the following observations (laying emphasis on the underlined portion) of the Hon'ble Supreme Court:

(i) that since the definition of income in section 2(24) was an inclusive one, its ambit should be the same as that of the word "income" in entry 82 of List I of Schedule VII to the Constitution of India

(ii) **that the definition of "income" in section 2(24) was inclusive, the purpose of the definition was not to limit the meaning of "income" but to widen its net, and the several clauses therein were not exhaustive of the meaning of income; even if a receipt did not fall within the ambit of any of those clauses, it might still be income if it partook of the nature of income.**

(iii) that the rally was a contest, if not a race and the respondent entered the contest to win it. **What he got was a return for his skill and endurance. It was "income" construed in its widest sense. Though, it was casual in nature, it was nevertheless**

(iv) The word "income" is of the widest amplitude and it must be given its natural and grammatical meaning.

10. Our attention was drawn to the decision of the Hon'ble Calcutta High Court in the case of Susil C.Sen In re 9 ITR 261(Cal). The facts of the case were that the assessee, an Attorney and Advocate, acting for one K who was a shareholder in a company, interviewed the Managing Agents of the company, attended a meeting of the shareholders under a proxy from K, made a speech at the meeting and secured a substantial issue of new shares to the public. X, a firm of stock brokers who were also benefitted by the issue of the new shares, paid a sum of Rs. 10,000 to the assessee, even though the assessee had not acted for them and they were not legally bound to pay

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anything to the assessee. The Hon'ble High Court that assuming that the receipt was of a casual and non-recurring nature, it arose from the exercise by the assessee of his profession as a lawyer and Advocate and it was part of the assessee's income which was not exempt from tax under section 4(3)(vii) of the Indian Income-tax Act 1922 which provided that any receipts not being receipts arising from business or the exercise of a profession, vocation or occupation, which are of a casual and non-recurring nature, or are not by way of addition to the remuneration of an employee. Our attention was also drawn to the decision of the ITAT Ahmedabad Bench in the case of ACIT Vs. India Gelatine & Chemicals Ltd. (2011) 47 SOT 134 (Ahd) wherein it was held that compensation for sterilization of a source of income was held to be capital but where assesse continued to remain in business but payments were made to compensate for loss of profit then the same would be revenue receipt chargeable to tax.

11. The learned DR highlighted the fact that the in its letter dt.14.11.1996 BMG had clearly stated that the payment was being made to BMIL for establish, protect and enhance the goodwill and image of BMG in India and the efforts and actions taken in recent past in the light of the adverse publicity arising from the problems relating to "COMSAT". The learned DR highlighted the fact that in note No.6 to the Accounts, the Assessee had clearly mentioned the fact that after the merger, certain non-recurring expenses aggregating to Rs.18.61 crores are determined by the new management as pertaining to the period prior of the effective take-over of the company by the new management or are on account of the Comsat incident and accordingly an equivalent amount has been drawn from Capital Grant Reserve during the year and reduced from Other expenses. Thus the payment was reimbursement of expenses already incurred by the Assessee BMIL on account of Comsat incident which had already been claimed as deduction by BMIL/Assessee and the receipt in question had to be

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considered as income of the Assessee. His submission was that the stand of the Assessee before the Revenue authorities that BMIL was in losses and the payment in question was made to recoup such losses is far from truth and was contrary to the material on record. He highlighted the fact that BMG and its associates held 64% of the share capital in BMIL. BMIL was using the brand image of BMG, making use of the technical know-how of the parent company and was also acting as the marketing agent for BMG for sale of diagnostic products, BIO chemicals and Bio catalysts. In view of the above relationship and also in the light of the help rendered by BMIL in terms of protecting and promoting the interests of BMG in the wake of COMSAT incident, the payment in question was made by BMG and was therefore a payment connected with the business of BMIL and was liable to be taxed u/s.28(i) read with Sec.2(24) of the Act.

12. The learned counsel for the Assessee submitted that the Assessee had no legal right to receive the money from the parent company. It was argued that the payment was made out of benevolence or compassion. The receipt was an unconditional grant which does not relate to any particular source of income and therefore was a revenue receipt not chargeable to tax. It was further submitted that the Assessee was not in the business of public relations or image building and therefore the efforts taken by it to protect and enhance the goodwill and image of the group cannot be said to be part of its business activity. It was further submitted that the decision of the Hon'ble Supreme Court in the case of P.Krishna Menon (supra) was not applicable because in that case the Assessee was carrying on the vocation of giving discourse in Vedanta and hence the receipt of money from disciples was held to arise from vocation whereas the Assessee received the money in question for nothing. He reiterated the stand of the Assessee that where a holding company reimburses losses incurred by a wholly owned subsidiary company, the amount so reimbursed by holding company cannot be treated

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as income. In this regard he drew out attention to the various decisions which were referred to in the submissions made before the AO. The learned counsel also highlighted the fact that the payment in question was made by BMG to BMIL and the Assessee by virtue of Amalgamation took over BMIL. Thus the Assessee had no business relationship with BMG and payment in question cannot be said to be arising out of any business of the Assessee. This argument deserves to be rejected at this stage itself. The Scheme of Amalgamation recognises all business of BMIL will be that of the Assessee. Therefore the character of the receipt in the hands of the Assessee will be the same as it would be had the money been received by BMIL.

13. The learned counsel for the Assessee also distinguished the cases relied upon by the learned DR by pointing out that Krishna Menon's case (supra) was a case where the receipt was linked to a vocation. He submitted that in all other cases there was a connection between the receipt and the business and therefore the same was taxed.

14. We have considered the rival submissions. To appreciate the contentions raised on behalf of the Assessee it is necessary to look into the ratio laid down in the several cases relied upon by the Assessee before the Revenue authorities. In the case of Handicrafts and Handloom Export Corporation (supra), the assessee, a government company, became a wholly owned subsidiary of the STC as a result of the latter acquiring the entire paid up share capital in the assessee in June, 1962. For the assessment years 1964-65 and 1965-66, the assessee incurred losses which were reimbursed by the STC. The question was whether for the purposes of income-tax the losses could be said to be wiped off as a result of the reimbursement by the STC. The Appellate Tribunal held that the amounts reimbursed by the STC could not be taken into account as part of the assessee's trading receipts or for that matter as a part of its total income,

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because the holding company and the subsidiary were distinct entities and what had happened was that the assessee's capital was eroded by the losses and that erosion was rectified by a contribution from the holding company and this was analogous to a sole proprietor introducing additional capital in a business which had been losing or to a holding company diverting some of its surplus funds to the subsidiary to enable it to tide over the loss of capital. On a reference, the Hon'ble Delhi High Court upheld the decision of the Tribunal observing that the receipt was analogous to the case of a person agreeing to meet the losses incurred by another person in carrying on a business and to discharge the debts incurred by him out of affection or regard.

15. In Handicrafts and Handloom Export Corpn. (supra) 140 ITR 532, the facts were the assessee, a wholly owned subsidiary of the STC, incurred loss in its business of export of handloom, etc., for the assessment year 1970-71. The STC agreed to recoup the losses and gave a cash assistance at 6 per cent of the foreign earnings of the assessee, the cash assistance so received by the assessee from the STC was held to be not part of the assessee's trading receipts and was not taxable as its income. The Delhi Hon'ble Court applied its earlier ruling in Addl. CIT v. Handicrafts and Handloom Export Corporation [1982] 133 ITR 590 (Delhi). The Hon'ble Court observed that there was a basic difference between grants made by a government or from public funds generally to assessees in a particular line of business or trade, with a view to helping them in the trade or to supplement their general revenues or trading receipts and not earmarked for any specific or particular purpose and a case of a private party agreeing to make good the losses incurred by an assessee on account of a mutual relationship that subsists between them. The former are treated as trading receipts because they reach the trader in his capacity as such and are made in order to assist him in the carrying on of the trade. The latter are in the nature of gifts or voluntary

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payments motivated by personal relationship and not stemming from any business considerations.

16. In Stewards & Lloyds of India Ltd. 165 ITR 416 (Cal), the facts were S, the assessee, was a wholly owned subsidiary of a foreign company. In December 1963, the assessee entered into a contract with the Indian Oil Corporation at the Baroda Refinery Project. In June, 1965, the assessee was converted into a public limited company but remained a subsidiary of the U.K. company. The assessee incurred a loss in executing the contract with the Indian Oil Corporation. The U.K. company offered to indemnify the assessee against the loss and after discussion with the assessee agreed to pay Rs. 22.5 lakhs. In the assessment year 1969-70, the relevant accounting period ending on September 30, 1968, the assessee credited a sum of Rs. 22.5 lakhs as receivable from the U.K. company. In its income-tax return filed for the said assessment year, the assessee did not, however, include the said amount of Rs. 22.5 lakhs as a receipt under any head of income and claimed that the said amount was not taxable. The Income-tax Officer held that the said amount of Rs. 22.5 lakhs was taxable as a revenue receipt as the said amount had been agreed to be paid to the assessee by the U.K. company to compensate the assessee for the loss sustained by it. The Tribunal, however, held that the said amount did not have the character of income. On a reference, the Hon'ble Calcutta High Court held that the material on record showed that there had been no business transaction between the assessee and the U.K. company after the assessee was converted into a public limited company on June 8, 1965. In the income-tax return filed by the U.K. company in the U.K., the payments made to the assessee were not claimed to be the business expenses of the U.K. company. The said amount of Rs. 22.5 lakhs was paid without any claim from the assessee. There was no evidence that the said payment by the U.K. company to the assessee was attributable to any legal obligation or custom or past practice. It was, therefore, clear that there was no obligation, contractual or

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statutory, to make the said payment to the assessee. It was not the case of the Revenue that the assessee was induced to take up the contract with the Indian Oil Corporation on the expectation that the U.K. company would indemnify the assessee if the assessee suffered a loss in executing the work. No consideration passed from the assessee to the U.K. company for the said payment and no quid pro quo was involved. The fact that, at the relevant time, the assessee was a subsidiary of the U.K. company would make no difference to the legal position. The U.K. company and the assessee at all material times were and remained different entities. Similarly, the fact that there were prior discussions between the assessee and the U.K. company regarding the method and manner of the payment and determination of the quantum to be paid would not affect the character of the receipt. There is nothing to bar consultation and discussion between a donor and a donee. The fact that the amount received from the U.K. company had been shown in the profit and loss account of the assessee for the relevant assessment year under the head "Income from other sources" would also not be decisive in the determination of the character of the receipt. The sum of Rs. 22.5 lakhs receivable by the assessee from the U.K. company with reference to the Baroda Refinery Project was not of the character of income.

17. In Indian Textile Engineers Pvt.Ltd. 141 ITR 69 (Bom), the facts were the assessees, Indian Textile Engineers, Bombay, were agents of PB, a non-resident company incorporated in the U.K. TMM, a company registered in the U.K., carried on the business of manufacture and sale of textile machinery and spare parts. It had a number of subsidiaries including PB. Indian Textile Engineers was the selling agent of PB in India. PB was in receipt of £ 3,00,000 during the assessment year 1966-67 as "subvention payment". Section 20 of the U.K. Finance Act, 1953, made a provision for a subvention payment to one associated company, in respect of losses that may be incurred by it, by other associated companies. Under sub-s. (2), it was stated that the amount which was received by the payee-company as a

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subvention payment was an amount which would not be ordinarily taken into account in computing the profits or losses of the payee-company but for the express provisions of s. 20. s. 20 expressly provided that in computing the profits or losses of these companies for the purpose of income-tax, a subvention payment should be treated as a trading receipt in the hands of the payee-company and as an allowable deduction to the paying-company. Under sub-s. (2), in order that a payment made by one company to the other could be treated as a subvention payment, it was necessary that there should be an agreement providing for the paying-company to bear or share in the losses of the payee-company. Under the provisions of s. 20(2) of the U.K. Act, TMM entered into an agreement dated February 22, 1957, with its subsidiary companies including PB for the making of subvention payments. During the assessment year 1966-67, PB made a provision of £ 3,30,000 for bad and doubtful debts which was a permissible deduction under the law in the U.K. On the allowance of this deduction PB's results turned into a loss. Thereupon pursuant to the agreement dated February 22, 1957, the other associated companies contributed £ 3,00,000 to PB as subvention payment.
The income in India of the assessee-company as agents of PB for the assessment year 1966-67 had admittedly to be determined under the provisions of s. 9 of the I.T. Act, 1961, read with rule 10(ii) of the I.T. Rules, 1962. While determining the income of the assessee for the assessment year 1966-67, the ITO held that the provision for bad and doubtful debts amounting to £ 3,30,000 could not be deducted in computing the total income of PB since such a provision was not a permissible deduction under the I.T. Act. The ITO also treated the receipt of £ 3,00,000, being subvention receipt, as the income of PB. The Tribunal, however, held that the receipt of £ 3,00,000 by PB, being subvention receipt, could not be treated as income in the hands of PB. On a reference, the Hon'ble Bombay High Court held that the amount of £ 3,00,000 had been received by PB towards the loss which is suffered and this loss was on account of certain bad or doubtful

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debts. If the debts, in respect of which payments had been made, could not be considered as deductible under the provisions of Indian I.T. Act, then a payment, which had been made to reimburse the company in respect of such non-allowable bad debts, could not be considered as a trading receipt. The receipt of £ 3,30,000 was intrinsically linked with the loss suffered by the company. If this loss was not to be considered as a trading loss for the purpose of income-tax then the receipt could not be considered as a trade receipt, because the receipt was by way of reimbursement of that loss. The receipt, therefore, was de hors the trading activity of the company as far as the provisions of the I.T. Act, were concerned. Such a receipt could not be considered as a receipt by way of income. From the language of s. 20 of the U.K. Act also, it was clear that a subvention payment was not ordinarily treated as a trade receipt. In fact, the statute laid down that such a payment must be of such a nature as would not ordinarily qualify as a trade receipt. The statute further provided that such a payment, though not ordinarily a trading receipt, would be treated as such. There is no such deeming provision under the I.T. Act. The subvention receipt could not also be regarded as a subsidy. The subvention payment of £ 3.00,000 was not liable to be taken into account in the computation of the profit of PB liable to tax in India under r. 10(ii).

18. In Cadell Weaving Mill Co. Pvt.Ltd. 249 ITR 265 (Bom), it was held that in order to attract section 10(3) of the Income-tax Act, 1961, two conditions are required to be satisfied, viz., that the receipt should be casual and non-recurring and that it should not arise by way of business income, salary income or capital gains chargeable under section 45. In other words, business income, salary income and capital gains chargeable under section 45 stand outside section 10(3) because salary income, business income and such capital gains are chargeable and computable under a different set of sections. Therefore, when the source of a receipt has a link with business

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income or salary income or capital gains chargeable under section 45 then section 10(3) will not apply.

19. In CIT Vs. D.P.Sandhu Bros.Chembur P.Ltd. 273 ITR 1 (SC), the aforesaid principle laid down by the Hon'ble Bombay High Court was reiterated. In the case of Padmaraji R.Kadam Bande vs. CIT 195 ITR 877 the assessee was entitled to monthly payment under orders of ruler native state. The native later merged with Bombay State and the payment was apportion on such merging. The statute abolishing such payment provided for compassionate payment at the discretion of the State Government. The assessee received payment from the State Government on compassionate ground. The Hon'ble Supreme Court held that the receipt was capital and not taxable under the Act. The Hon'ble Supreme Court emphasized the fact that the payment was purely discretionary and that there was no real source of income.

20. Thus it can be seen from all the aforesaid decisions that the common thread of reasoning by the Courts was that the payment are voluntary. It was given to persons whose relationship were either holding or subsidiary company and were given in a situation whether the subsidiary company were making losses and to enable the subsidiary company by offering the losses. Another line of reasoning is that the payments are modified by personal relationship and do not stem from any business consideration. The case of Indian Textile Engineering Pvt. Ltd. (supra) which stand on a totally different footing as they are based on specific context of the UK Finance Act, 1953.

21. In the present case we find that BMG in its letter dated 14/11/1996 addressed to BMIL had clearly explained the purpose of the payment which we have already referred to in the earlier part of this order. It is clear from the aforesaid letter of BMG that the payment is in recognition of the services

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rendered by BMIL to BMG. Moreover business consideration did way for making aforesaid payments. It is also a fact that the assessee had incurred expenses in connection with the effort it had taken to protect and enhance the goodwill and image of PMG in India and those have been claimed as deductible revenue expenditure. Thus the case of the assesse stand on totally different footing from all the cases relied upon by the ld. Counsel for the assessee before us. It is not a payment to enable BMIL to recoup its losses nor is it a payment which did not have business consideration for making such payments. The fact that it was voluntary or that it was an unconditional payment, in our view, will not make it a capital receipt not chargeable to tax. The stand of the Assessee before the Revenue authorities that BMIL was in losses and the payment in question was made to recoup such losses is contrary to the material on record. There was holding and subsidiary company relationship between BMIL and BMG besides business relationship viz., BMIL was using the brand image of BMG, making use of the technical know-how of the parent company and was also acting as the marketing agent for BMG for sale of diagnostic products, BIO chemicals and Bio catalysts. It is only because of such relationship and also in the light of the help rendered by BMIL in terms of protecting and promoting the interests of BMG in the wake of COMSAT incident, the payment in question was made by BMG and was therefore a payment connected with the business of BMIL and was liable to be taxed u/s.28(i) read with Sec.2(24) of the Act. We are of the view that the decision of the Hon'ble Supreme Court in the case of G.R.Karthikeyan would be clearly applicable in the present case. We are of the view that the CIT(A) erred in coming to the conclusion that receipt was not in the nature of income. In fact we find that the CIT(A) has given contradictory finding. On the one hand the CIT(A) says that the assessee was in the business of manufacture and sale of drugs and not in the business of public relation or image building. Thus it is an admitted position that the payment was made for protecting and enhancing the

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goodwill and image of BMG in India. The CIT(A) contrary to the above finding has come to the conclusion that there was no quid pro quo for the payment. As held in the decision of the Hon'ble Supreme Court in the case of G.R.Karthikeyan the payment had all the characteristic of income and was liable to be brought to tax. In our view the CIT(A) erred in reversing the order of the AO. We, therefore, reverse the order of CIT(A) and restore the order of the AO in this regard. Ground No.1 raised by the revenue is accordingly allowed.

22. Gr.No.2 raised by the Revenue reads as follows:

> "2. Erred in a accepting assessee's device of not claiming depreciation ignoring omission of the provisions of Sec. 34(1) of the I.T. Act w.e.f. 01/04/1988 relying on the Hon'ble Supreme Court judgment in the case of M/s. Mahindra Mills Ltd. reported in 243 ITR 56 which pertained to the period prior to the section's omission."

23 As already seen BMIL merged with the assessee company as per the scheme of amalgamation w.e.f. 1/4/96. The assessee has claimed depreciation on the assets taken over as part of the merger. The AO noticed from the schedule of depreciation furnished by the assessee that depreciation was being claimed on the WDV without adjusting for depreciation allowable for A.Y.s 1995-96 & 1996-97 in the hands of erstwhile BMIL. The erstwhile BMIL did not opt to claim depreciation for the assessment years 1995-96 & 1996-97 although assets have been used in the business carried on by BMIL during those years. The AO was of the view that depreciation is not available to the assessee on the WDV without taking into consideration the allowable depreciation on the use of the assets during the assessment year 1995-96 & 1996-97 by BMIL. Depreciation charge being in the nature of a deduction for wear and tear of the assets, it was mandatory that depreciation is charged to arrive at the correct income for any given year. The AO referred to the decision of the Hon'ble Bombay High

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Court in the case of M/s. Premier Automobiles Ltd. 206 ITR 001(Bom), wherein it was held as follows:

> "Under section 32 of the Act, the assessee is entitled to allowance of depreciation. It is for him to claim the same. If he does not claim the same or wants to forgo the same, he is free to do so. This judgement does not say anything about carry forward of depreciation which has not been claimed by the assessee in the particular year. So far as the current year's depreciation is concerned, it is for the assessee to claim the same or not to claim the same. If he does not claim it, he loses the depreciation. There is no question of any depreciation allowable for that year and in that event the question of any unabsorbed depreciation of that year will not arise. This decision, however, cannot be carried any further to contend that the assessee is free not to claim depreciation in the year to which it pertains but carry forward the same to the subsequent year or years as it likes."

It was further held that:

> "what section 32 allows an assessee is the deduction by way of depreciation of an asset of an amount calculated as a percentage of the written down value thereof as may be prescribed. It is for the assessee to claim the same and furnish the requisite particulars. If the assessee does not claim the same, it cannot be allowed. But in that case, there will be no depreciation for that year which can be said to be unabsorbed to be carried forward to a subsequent year u/s. 32(2) of the Act. In other words, an assessee who des not claim deduction for the depreciation allowable to him u/s. 32 of the Act in the particular year loses it once for all."

Accordingly, the WDV in respect of the assets belonging to erstwhile BMIL was adjusted (by reduction of the WDV) for the foregone depreciation for A.Y's 1995-96 & 1996-97.

24. On appeal by the Assessee, the CIT(A) held that depreciation on the WDV as claimed by the Assessee on the assets in question should be allowed. The CIT(A) held that the AO was not correct in reading the judgment of the Hon'ble Bombay High Court in the case of Premier Automobiles (supra) as laying down a limitation that notional allowance has to be reduced from the WDV to arrive at the WDV of the subsequent year.

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The CIT(A) also found that the decision of the Hon'ble Supreme Court in the case of Mahindra Mills Ltd. (supra) clearly lays down the proposition that WDV has to be arrived at only after reducing depreciation actually allowed and in a case where the Assessee has not claimed depreciation it cannot be said that it was notionally allowed. Aggrieved by the order of the CIT(A) the revenue has raised Gr.No.2 before the Tribunal.

25. We have heard the rival submissions. We are of the view that the order of the CIT(A) has to be upheld. The Hon'ble Supreme Court in CIT Vs. Mahendra Mills (2000) 159 CTR (SC) 381 has laid down that the assessee is entitled to exercise his option even through the filing of revised return and that option cannot be denied to him nor can depreciation be thrust on the assessee against his willingness. It was held that until a claim is made for allowing deductions of the nature covered under s. 32 along with necessary particulars, there would hardly be any occasion for the ITO to 'allow' any 'claim'. Two conditions – the making of a claim and the furnishing of particulars – have been read as cumulative conditions by the Hon'ble Supreme Court in Mahendra Mills (supra). If either of the two conditions are not fulfilled the AO cannot force the depreciation allowance on the assessee. It further follows logically that in the absence of a claim by the assessee the allowance cannot be thrust upon him even if the particulars are available to the AO. Therefore, the mere fact that the assessee before us did not make a claim for depreciation places a fetter upon the powers of the AO t allow depreciation.

26. The contention of the Revenue was that after 1st April, 1988, the condition of furnishing the particulars required by sub-sec. (1) and (2) of s. 34 has been done away with and that has altered the effect of the judgment in Mahendra Mills (supra). It is difficult to uphold the contention because not only has the Supreme Court viewed the conditions as cumulative, but more importantly, they have viewed the claim for depreciation as something

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over which the AO has no control and is the choice of none else than the assessee. It would be proper to understand the judgment as also laying down, impliedly, that if there is no claim of depreciation by the assessee, that should be an end of the matter. Therefore, the judgment also lays down in principle that irrespective of whether the statute requires the furnishing of the particulars are not, if there is no claim for depreciation, it cannot be allowed by the AO. The debate, therefore, as to whether the omission of s. 34(1) and (2) and r. 5AA of the IT Rules would change the position prima facie appears to be academic but since it has been raised and that question has also been answered by Mahendra Mills (supra) we proceed to decide the same. The following observations of the Supreme Court in this regard clinch the issue in favour of the position that despite the omission of the above sub-sections of s. 34 and the rule, still depreciation allowance cannot be thrust upon the assessee in the absence of a claim:

> 'The language of the provisions of ss.32 and 34 is specific and admits of no ambiguity. Sec.32 allows depreciation as deduction subject to the provisions of s. 34. Sec. 34 provides that deduction under section shall be allowed only if prescribe particulars have been furnished. We have seen r. 5AA of the Rules which though since deleted provided for the particulars required for the purpose of deduction under s. 32. Even in the absence of r. 5AA, the return of income in the form prescribed itself requires particulars to be furnished by the assessee and no claim for the depreciation has been made in the return. The ITO in such a case is required to compute the income without allowing depreciation allowance. The circular of the Board, dt. 11th April, 1955, is of no help to the Revenue. It imposes merely a duty on the officers of the Department to assist the taxpayers in every reasonable way, particularly, in the matter of claiming and securing relief. The officer is required to do no more than to advise the assessee. It does not place any mandatory duty on the officer to allow depreciation of the assessee does not want to claim that. The provision for claim of depreciation is certainly for the benefit of the assessee. It if does not wish to avail that benefit for some reason, benefit cannot be forced upon him. It is for the assessee to see if the claim of depreciation is to his advantage. Rather the ITO should advise him not to claim our view in the spirit of the circular, dt. 11th April, 1955. Income under the head 'profits and gains of business or profession' is chargeable to income-tax under s. 28 and that income under s. 29 is to be computed in accordance with

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> the provisions contained in ss. 30 to 43A. The argument that since s. 32 provides for depreciation if has to be allowed in computing the income of the assessee cannot in all circumstances be accepted in view of the bar contained in s. 34. If s. 34 is not satisfied and the particulars are not furnished by the assessee, his claim for depreciation under s. 32 cannot be allowed. Sec. 29 is thus to be read with reference to other provisions of the Act. It is not in itself a complete code.'

27. The Supreme Court has observed that even in the absence of the rule, since the return form itself prescribes particulars to be furnished in support of the claim of depreciation, the allowance can be granted on if the assessee makes a claim and the particulars required in the return form are furnished. The ratio of the observations is that in order to obtain an allowance or deduction, it is necessary for the assessee to make a claim and also support it by necessary particulars or evidence. Therefore, the contention on behalf of the revenue that after the omission of sub-sec. (1) and (2) of s. 34 and r. 5AA w.e.f. 1st April, 1988, depreciation has to be mandatorily claimed cannot be accepted. It is further seen that Expln. 5 to 32 was introduced by the Finance Act, 2002 w.e.f 1-4-02 and it provides as follows:

> Explanation 5. – For the removal of doubts, it is hereby declared that the provisions of this sub-section shall apply whether or not the assessee has claimed the deduction in respect of depreciation in computing his total income;

Thus, it can be safely said that omission of section 34 has not affected the assessee's choice to claim depreciation allowance. This choice is, however, expressly taken away by insertion of Explanation 5 in section 32 with effect from 1st April, 2002, from assessment year 2002-03 onwards. In CIT Vs. Sree Senhavalli Textiles (P) Ltd., 259 ITR 77 (Mad), the Hon'ble Madras High Court has held that though after judgment was rendered by the apex Court in CIT Vs. Mahendra Mills [2000] 159 CTR (SC) 381: [2000] 243 ITR 56 (SC), Expln. 5 was inserted in s. 32(1) by the Finance Act, 2001, w.e.f. 1st April, 2002, declaring that 'for the removal of doubts' the provisions of sub-s (1)

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will apply whether or not the assessee claims deduction in respect of depreciation in computing his total income, that Explanation cannot be regarded as taking away the effect of the judgment of the Supreme Court for the years prior to the date of introduction of the Explanation. The law declared by the Supreme Court cannot be regarded as having merely raised doubts. The interpretation of the relevant provisions of the Act by the apex court settles the law, and unless the subsequent amendment to the statute is expressly given retrospective effect, the law laid down by the apex court will remain the binding law for the period to the amendment. The newly added Explanation takes effect only on and from 1st April, 2002, and will not be applicable for prior ye3ars. If claim made in the original return had been given up in the revised return, there was no obligation to consider the claim for depreciation.

27. The Hon'ble Supreme Court in the case of Mahendra Mills (Supra) had made the following observations:

> "....Allowance of depreciation is calculated on the written down value of the assets, which written down value would be the actual cost of acquisition less the aggregate of all deductions "actually allowed" to the assessee for the past years. "Actually allowed" does not mean "notionally allowed". If the assessee has not claimed deduction of depreciation in any past year it cannot be said that it was notionally allowed to him. A thing is "allowed" when it is claimed. A subtle distinction is there when we examine the language used in section 16 and sections 34 and 37 of the Act. It is rightly said that a privilege cannot be to a disadvantage and an option cannot become an obligation. The Assessing Officer cannot grant depreciation allowance when the same is not claimed by the assessee."

28. In the light of the above observations of the Hon'ble Supreme Court, let us see the decision of the Hon'ble Bombay High Court in the case of Premier Automobiles (Supra). The question before the Hon'ble Court and the circumstances under which it arose were as follows:

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> "Whether, on the facts and in the circumstances of the case, the assessee-company could lawfully claim the development rebate in priority to depreciation allowance prescribed under section 32 of the Income-tax Act, 1961, while computing its total income for each of the assessment years 1970-71, 1971-72 and 1972-73?"

As is evident from the question, the controversy related to priority in the matter of set off of unabsorbed depreciation allowance and unabsorbed development rebate. The assessee had substantial amount of unabsorbed depreciation and unabsorbed development rebate which had been carried forward from year to year. The claim of the assessee was that as there was a time limit fixed under the Act for carrying forward of unabsorbed development rebate, it should be set off first against the current year's profit in the respective years and thereafter if any profit is left, the unabsorbed depreciation should be adjusted. According to the Income-tax Officer, under the scheme of the Act, the unabsorbed depreciation had to be adjusted first and then only, if any profits are left, the unabsorbed development rebate can be adjusted. Thus, the question was of priority between carried forward unabsorbed development rebate and unabsorbed depreciation in the matter of set off against the current year's profits. In the light of the above controversy, the Hon'ble Bombay High Court held as follows:

> "Thus, it is clear that what section 32 allows an assessee is the deduction by way of depreciation of an asset of an amount calculated as a percentage of the written down value thereof as may be prescribed. It is for the assessee to claim the same and furnish the requisite particulars. If the assessee does not claim the same, it cannot be allowed. But in that case, there will be no depreciation for that year which can be said to be unabsorbed to be carried forward to a subsequent year under section 32(2) of the Act. **In other words, an assessee who does not claim deduction for the depreciation allowable to him under section 32 of the Act in the particular year, loses it once for all.** He is not entitled to claim the same in a subsequent year though he will again be entitled in that subsequent year to claim depreciation for that year." (underlining by us for emphasis)

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The AO has relied on the underlined portion of the judgment to hold that an assessee who does not claim deduction for depreciation allowable to him under section 32 of the Act in a particular year loses it once for all. The AO has overlooked the fact that the above observation are in the context of priority of claims for development rebate of depreciation under section 32 of the Act. In our view the above observation does not support the case made out by the A.O. We, therefore, uphold the order of the CIT(A) and dismiss the Ground No.2 raised by the assessee.

29. Ground No.3 raised by the revenue reads as under:

> "Erred in deleting addition on account of depreciation claimed by the assessee at enhanced value ignoring that such claim is contrary to the provion of Explanation 1 to Section 43(6) of the Income Tax Act, 1961."

30. Before 1/4/1995 i.e. during the previous year relevant to the A.Y 1996-97 the assessee took over the Bulks Drugs Division(BDD) of Sumitra Pharmaceuticals and Chemicals Ltd.(SPCL) and claimed depreciation on the market value of the assets of the BDD as determined in the scheme of arrangement which was approved by the High Courts of Andhra Pradesh and Mumbai. The A.O. on the other hand, allowed depreciation on the WDV of the assets in the hands of SPCL. The depreciation allowed on these assets by the AO was less than what the assessee claimed. For the A.Y 1997-98 under appeal now, the assessee claimed depreciation of Rs. 8,97,04,377/- on the WDV of the assets of the BDD as on 31/3/1996. This claim was made taking into account the market value of the assets as fixed by Valuation Report at figures higher than the WDV in the books of account of SPCL. The A.O, however allowed the depreciation of Rs.2,41,21,753/- taking into account the WDV of the assets in the books of SPCL as on 31/3/1995 and the depreciation allowed for the A.Y 1996-97.

31. On appeal by the Assessee, the CIT(A) noticed that similar issue came up for consideration in the appeal filed by the assessee for the A.Y 1996-97

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and for the elaborated reasons discussed in the appellate order for the A.Y 1996-97, it was held that depreciation should be allowed on the assets of the BDD taken over from SPCL taking into account the market value of the assets as determined in the valuation report, as per the scheme of arrangement, which was approved by the High Court of Andhra Pradesh and Mumbai. Following that decision the CIT(A) held for A.Y 1997-98 that depreciation should be allowed on the assets of BDD taking into account the market value of the assets as on 1/4/95 fixed by valuation report a reduced by the depreciation allowable for the A.Y 1996-97 as per the appellate order for A.Y 1996-97 mentioned above. Accordingly he held that the assessee is entitled to depreciation of Rs. 8,97,04,377/- as against Rs. 2,41,21,753/- allowed by the A.O.

32. Aggrieved by the order of CIT(A), the revenue has raised Gr.No.3 before the Tribunal. It is not in dispute before us that identical issue came up for consideration in assessee's own case in A.Y 1996-97 in ITA No.4601/Mum/01 and this Tribunal held as follows:

> " 3. As regards ground No.1 brief facts of the case are that the assessee company which is engaged in the business of manufacturing of pharmaceuticals products filed its return of income on 30/11/97 declaring a loss of Rs.70,67,21,243/-. Subsequently, assessee filed a revised return of income on 30/3/98 revising the loss figure to Rs.70,66,81,323/-. During the assessment proceedings u/s. 143(3), the AO noticed that during the relevant previous year the assessee company had taken over the bulk drug unit of M/s Sumitra Pharmaceutical & Chemicals Ltd. [SPCLJ located near Hyderabad and that it is as per the scheme of arrangement approved by the shareholders of both the companies and also by the jurisdictional High Courts of both the companies. He further observed that as per the scheme of arrangement, appointed date for the take over was the first day of April 1995 and accordingly the assessee company has filed the return of income along with the consolidated balance-sheet and profit & loss account incorporating the result of the operations of the bulk drugs unit also. From the details filed along with the revised return of income, the AO observed that the assessee company has taken over the assets and liabilities of the bulk drugs unit at their estimated market value as on the appointed date after making all the necessary

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provisions for the appreciation, increase or efficiency, diminution in the value of any asset or for the anticipated short-fall in realization of any assets or for any dividend or other liability or obligation transferred to the assessee company in pursuant to the scheme of arrangement but not provided for in the books of SPCL. He observed that the assessee company claimed depreciation on the revalued figures of depreciable assets instead of the corresponding figures of the written down value in the books of SPCL as on 31-3-95. The AO asked the assessee company to explain as to how the depreciation under the Income Tax Act is allowable on the revalued figures. The assessee company submitted that all the assets and liabilities of SPCL have been taken over as per the scheme of arrangement approved by the Hon'ble High Courts of Andhra Pradesh and Bombay and as per clause-10 of the scheme, the company was required to record the assets taken over at their estimated market value and accordingly the valuation report of M/s Sabnis & Co., dated 20-12-95 was obtained and the assets have been revalued and the depreciation is accordingly claimed on the revalued figures. It was also submitted that the written down va1ue of the assets in the hands of SPCL has no relevance to the cost of the same in the assessee company's hands for the purpose of depredation allowance u/s.32 of the Act. it was stated that "cost" for the purpose of depreciation allowance should relate to the person who owns it and not with respect to his predecessor. In this connection, assessee placed reliance upon the following decisions:

a) CIT v. Solomon 1 ITR 324 [Rangoon High Court J
b) CIT vs. Groz Packert Saboo Ltd. 116 ITR 135 [S.C]
c) Francis Vallbhyar vs. CIT 40 ITR 426 [Mad]

The AO, however, was not satisfied with the assessee's explanation and held that the written down value of the depreciable assets in the hands of the previous owner is to be adopted as the value of assets in the hands of the assessee for the purpose of claim of depreciation. He, accordingly, reworked the depreciation allowable on the basis of written down value at Rs.2,98,85,394/- as against the claim of the assessee of Rs.11,48,96,238/-. Aggrieved, assessee filed an appeal before the CIT[A) who allowed the same holding that the cost of appreciation of the assets of the bulk drugs unit in the hands of the assessee was the market value of the assets entered into the books of the assesee on the basis of the valuation report as approved by the High Courts of Andhra Pradesh and Bombay and also by the shareholders of both the companies and, therefore, for the purpose of allowing depreciation this valuation is to be taken. Aggrieved by the same, the revenue is in appeal before us.

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5. The ld. DR strongly supported the order of the AO and submitted that the scheme of arrangement as approved by the High Courts of Andhra Pradesh and Bombay is only with regard to the transfer of assets and liabilities -and not with regard to the valuation of assets and liabilities as adopted by the two companies. According to him, the correctness or otherwise of the valuation of assets has not been gone into by the respective I-Ugh Courts and therefore the valuation cannot be said to be genuine. Further, he submitted that the legislative intention as can be perused from various Explanations on "actual cost" incorporated in the Act is to allow depreciation on the original written down value of the depreciable assets even when the ownership is transferred unless actual cost can be directly determinable with reference to any specific asset. He placed reliance upon the following decisions in support of his contentions

I. CIT vs. Poulose & Mathean Pvt. Ltd., 236 ITR 416 [Ker.]
ii. Dalmia Ceramic Industries Ltd. vs. CIT, 277 ITR 219 [Del]

6. The Id. counsel for the assessee, on the other hand, supported the order of the CIT[A} and reiterated the submissions made before the authorities below. He submitted that the assessee company is in no way related to SPCL and therefore the market value of the assets as approved by the Hon'ble High Courts of Andhra Pradesh and Bombay, being at arm's length has to be adopted for the purpose of claiming depreciation thereof.

7. Having heard both the parties and having considered their rival contentions, we find that sec.32 of the Income Tax Act provides for depreciation on tangible and intangible assets. It is also provided that in the case of block of assets, depreciation shall be allowed on the written down value thereof as may be prescribed.

Explanation 2 to sub-sec.[1] of sec.32 provides that for the purpose of this sub section, "written down value of the block of assets" shall have the same meaning as in clause [c] of sub-section [6] of section 43.

Sub-section [6] of section 43 defines written down value to mean.

a) In the case of assets acquired in the previous year, the actual cost to the assesse;

b) In the case of assets acquired before the previous year, the actual cost to the assessee less all depreciation actually allowed to him under this Act, or under the Indian Income Tax Act, 1922

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or any Act repealed by that Act, or under any executive orders issued when the Indian Income Tax Act, 1886 was in force

c) In the case of any block of assets

[i] in respect of any previous year relevant to the assessment year commencing on the 1 day of April, 1988, the aggregate of the written down values of all the assets falling within that block of assets at the beginning of the previous year and adjusted.

A..........................
B..........................
C..........................

Explanation 1- When in a case of 'succession in business or profession, an assessment is made on the successor under subsection [2] of section 170 the written down value of "any asset or any block of assets" shall be the amount which would have been taken as its written down value if the assessment had been made directly on the person succeeded to.

Explanation 2.- Where in any previous year, 'any block of assets is transferred, -

a) by a holding company to its subsidiary company. or by a subsidiary company to its holding company and the conditions of clause [iv] or, as the case may be, of clause [v] of section 47 are satisfied; or

b) by the amalgamating company to the amalgamated company in a scheme of amalgamation, and the amalgamated company is an Indian company,

then, notwithstanding anything contained in clause [1], the actual cost of the block of assets in the case of the transferee company or the amalgamated company, as the case may be, shall be the written down value of the block of assets as in the case of transferor-company or the amalgamating company for the immediately preceding previous year as reduced by the amount of depreciation actually allowed in relation to the said preceding previous year.

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From the above provisions, it is clear that in the following cases the written down value of the assets or block of assets in the hands of the Transferor company has to be adopted for the purpose of. grant of depreciation in the hands of transferee company.

1) where the transfer of block of assets is by a holding company to the subsidiary company or by a subsidiary company to holding company;

2) by the amalgamating company to the amalgamated company in a scheme of amalgamation, and the amalgamated company is an Indian company

In all other cases clause [a] of sub-sec.[61 of sec.43 applies, i.e. the actual cost to the assessee. In the case before us the bulk drugs unit of SPCL was taken over by the assessee company. It is not the case of the revenue that it is the transfer of assets by a holding company to a subsidiary or by a subsidiary to the holding company or that it is a case of amalgamation. The AO has observed that the facts of the assessee's case are in a sense akin to a case of full fledged amalgamation and that the scheme of arrangement has been designed in such a manner so as to escape the definition of amalgamation but the substantial conditions have been fulfilled. He also observed that it is obvious from the scheme that the shareholders of SPCL holding not less than 9/10th in value of shares have to be shareholders of MPIL and that all fixed depreciable assets are secured loans and unsecured loans and most of the current assets and liabilities have been taken over and what is left behind is only a husk of the corporate entity. He has held that a miniscule portion of the assets and liabilities are retained by SPCL and therefore the scheme is nothing but the amalgamation though it does not cover the definition of amalgamation u/s.2[B] of the Act. This observation of the AO cannot be accepted. To consider a transaction as amalgamation, there has to be a complete merger of one or more company with another company or merger of two or more companies to form one company in such a manner that all the properties and liabilities of the amalgamating companies become the properties or liabilities of the amalgamated companies as defined I n sub-sec.[1B) of sec.2 of the Income Tax Act. From the above it can be observed that in the case of an amalgamation the amalgamating company looses its identity and independent existence. All the assets and liabilities also have to be transferred. In the case before us, the assessee company has taken over the assets and liabilities of only one division of SPCL and SPCL has not lost its identity or independent existence. Therefore, it does not satisfy the conditions of amalgamation as laid down under sub-

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sec.[1B] of sec.2 of the Act. Before the takeover of the bulk drug unit there is no connection whatsoever between the two companies and the market value of the block of assets has been arrived at as per the valuation report of M/s Sabnis & Co. Therefore, it cannot be said that it is not genuine or is not at arm's length. In such a case, the written down value of the assets has to be the actual cost to the assessee. The decisions relied upon by the Id. DR are not applicable to the facts of-the case before us, as they are cases relating to transfer of assets by a subsidiary company to its holding company and incorporation of a partnership firm into a limited company. In view of the same, we do not see any reason to interfere with the order of the CIT[A] and this ground of appeal is rejected.

33. The facts and circumstances under which the addition was deleted by CIT(A) in the earlier A.Y. and the present AY being identical, respectfully following the decision of the Tribunal, we uphold order of CIT(A) and dismiss Gr.No.3 of the Revenue. Consequently Ground No.3 raised by the revenue is dismissed.

34. Ground No.4 raised by the revenue reads as follows:

> "4 Erred in holding software development product expenses as revenue expenditure allowable u/s. 37(1) of the I.T.Act ignoring that these are for enduring benefit and falling within the definition of plant."

35. During the previous year relevant to this A.Y. 1997-98 the assessee incurred as expenditure of Rs. 32.90 lacs for acquiring and implementing software programme known as known as ERP package MFG Pro-version 7.4 f. The assessee claimed it to be a revenue expenditure whereas A.O treated it as capital expenditure resulting in enduring benefit to the assessee. The A.O also observed that the recent amendment made in the I.T.Act providing for one time exception with regard to expenditure towards Y2K compliance makes it clear that the intention of law is to treat software expenditure to be capital in nature. The assesse contended before CIT(A) that because of very high degree of obsolescence of computer software it cannot be said that anybody gets enduring benefit by acquiring the software programme. The

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Assessee relied on print-out taken from the official web site of QAD, the original developers of MFG Pro software, in which it was clearly mentioned that MFG Provision 7.4 is currently in a retirement phase and urges its customers to upgrade this software in view of the fact that this version of the software is no longer being sold and it can be provided limited standard support on a best effort basis. It was submitted that the assessee company had to migrate from version 7.4 of the ERP software MFG Pro to version 9.1 (eB version) within a span of 4 years. In support of the contention that such software expenditure is revenue in nature the Assessee relied on the following case laws:

i. Forbes Campbell & Co. Ltd. (ITA No.8489/Bom88 and ITA No.8785/Bom/88 dated 15/4/94)
ii. DCIT vs. Lubi Electricals P. Ltd.(30BCAJ May 98, page 120 - ITAT, Ahmedabad)

36. The CIT(A) was of the view that expenditure incurred for acquiring and implementing the software programme cannot be treated as capital expenditure. Specific amendment made in support of the expenditure relating to Y2K compliance, referred to by the A.O, cannot be taken as a expression of the intention of the legislature to treat software expenditure as capital in nature. He held that any software programme becomes obsolete within a short time which requires to be replaced or upgraded and hence expenditure incurred for acquiring a software programme cannot be said to have conferred advantage of enduring nature to the customers. Regarding the software package acquired by the assessee, the CIT(A) was of the view that as per the information furnished, it became obsolete within a span of 4 years and hence no advantage of enduring nature was enjoyed by the assessee by incurring this expenditure. The A.O was accordingly directed to allow deduction of Rs.32.90 lacs in computing the total income.

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37. Before us ld. D.R submitted that the Special Bench of ITAT, Delhi in the case of Amway India Enterprises, 111 ITD 111 (SB) has laid down principles as to when expenditure incurred on software can be considered as capital or revenue expenditure and the AO should be directed to consider the claim of the assesse in the light of the principles laid down by the Special Bench. The ld. counsel for the assessee on the other hand, relied on the decision of the Hon'ble Delhi High Court in the case of CIT vs. Asahi India Safety Glass Ltd., 202 Taxman 277 (Del) and CIT vs. Southern Roadways Ltd,, 304 ITR 84(Mad). According to him the Hon'ble Delhi High Court in the case of Asahi India Safety Glass Ltd.,(supra) held that installation of software application for assistance in areas related to financial accounting, inventory and purchase was revenue expenditure. It was also submitted by him that the Hon'ble Delhi High Court in the case of Amway India Enterprises, ITA No.1344 & 1363 of 2009 by judgment dated 13/9/2011 followed the decision in the case of Asahi India Safety Glass Ltd (supra) and held that expenditure incurred on purchase of MS Office software, Antivirus software, lotus notes software and message exchange application were revenue expenditure.

37. We have considered the rival submissions. In our view the nature of the software and the purpose that the software will serve in the business of the assessee are important criteria laid down by the Special Bench of ITAT to decide whether expenditure on purchase of computer software is capital or revenue expenditure. Therefore, the nature of the software and its role in business of the assessee have to be considered. The decision relied upon by the ld. counsel for the assessee were rendered in the context where there was no dispute that the software were used for the better running of the business of the assessee. We are, therefore, of the view that it would be appropriate to set aside the order of the CIT(A) on this issue and remand the

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same to the AO for fresh consideration in the light of the principles laid down by the Special Bench in the case of Amway India Enterprises (supra).

38. Ground No.5 raised by the assessee reads as follows:

> "Erred in directing deletion of loss of Rs.5.7 crores from the computation of profit u/s. 115JA ignoring the computation made by the assessee as per Company's Act."

38. Sec.115JA(1) of the Act provides that where in the case of an assessee, being a company, the total income, as computed under this Act in respect of any previous year relevant to the assessment year commencing on or after the 1st day of April, 1997 is less than thirty per cent. of its book profit, the total income of such assessee chargeable to tax for the relevant previous year shall be deemed to be an amount equal to thirty per cent. of such book profit. Sec.115JA(2) of the Act provides for the manner in which Book Profits have to be calculated for the purpose of Sec.115JA(1) of the Act. For AY 97-98, the total income of the Assessee computed under the normal provisions of the Act was less than the book profits computed as per Sec.115JA(2) of the Act and therefore the said book profits will be the total income of the Assessee chargeable to tax. The dispute raised by the revenue in the aforesaid ground of appeal is with regard to the computation of book profits u/s.115JA of the Act.

39. The Assessee computed book profits as per Sec.115JA of the Act at Rs.39,32,12,671/- The AO noticed from the published accounts prepared as per schedule VI of the Companies Act that the profit after tax was Rs.45.02 crores. However, another set of accounts had been prepared and enclosed to the return of income along with a certificate from the Auditor. The certificate explains the computation of book profits at Rs.39,32,12,671/- as follows:

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> "NIPL has acquired Bulk Drug Division of Sumitra Pharmaceutical and Chemicals Ltd. of Hyderabad. As per the court orders the effective date of such acquisition was on 19/6/96. In the annual accounts of NPIL , the income and expenses in respect of B.D Division for the period from 1/4/1996 to 18/6/1996 (pre-acquisition period) were adjusted against general reserve and were not incorporated in the Profits and loss account of NIPL. For the purpose of submission to the income tax authorities, NIPL has prepared a revised Profit and loss account for the year ended 31/3/1997, incorporating the income and expenses of B.D.Division for pre-acquisition period. We have verified the revised profit and loss account given in Annexure-I and we state that the account gives a true and fair view of the profit of NIPL (after incorporating the income and expenses of B.D. Division for the period from 1/4/96 to 18/6/96) for the year ended 31/3/1997".

40. On perusal of the above, the AO was of the view that the assessee has adopted different accounting practices when it came to furnishing of the financial results for the year to Income tax. In this regard the AO referred to the fact that in the notes to the published accounts the losses of bulk drug division which is acquired w.e.f 1/4/1995 (appointed date) have been set off against time revaluation reserve in the annual accounts put before the annual general meeting and submitted to all the other authorities. When it came to submission of the accounts to Income tax, the accounting policy itself has been changed and the loss of the BDD of SPCL between the appointed date and the effective date had been incorporated in the profit and loss account and thus the profit as per profit and loss account stood reduced. According to the AO, doing so was not in accordance with the provisions of Sec.115JA of the Act. Therefore, the AO called upon the assesee to explain the basis for such a change in computing the income u/s. 115 JA.

41. In reply the Assessee submitted that clause (i) of the explanation to section 115 JA (2) provides that any amount withdrawn from any reserves or provisions, if any such amount is credited to the Profit and loss account shall reduce the "book profits". It was submitted that the accounting effect of withdrawal from the General Reserve for crediting it to the Profit & Loss

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account was achieved by the Assessee by reducing losses amounting to Rs.570.30 lacs directly from the General Reserve account which otherwise would have been debited to the company's published profit and loss account. The Assessee explained that this was done to give effect to the specific provision for the Scheme of Arrangement whereby BDD of SPCL was taken over by the Assessee. The Assessee reiterated that the Profit and loss account showing a profit of Rs.3932.11 lacs has been prepared in accordance with the provisions of section 115 JA(2). The Assessee further brought to the notice of the AO proposed amendment in the Finance Bill 2000 wherein u/s. 115JB it was proposed that the annual accounts including profit and loss account - (i) the accounting policies; (ii) the accounting standards followed for preparing such accounts including profit and loss account; (iii) the method and rates adopted for calculating the depreciation, was required to be the same as has been adopted for the purposes of preparing such accounts including profit and loss account and laid before the company at its annual general meeting in accordance with the provisions of section 210 of the companies Act. 1956. Such a rigorous requirement is not available in section 115JA. So long as the accounts are prepared in accordance with Schedule VI part II and III of the Companies Act, 1956, the requirement of section 115JA are met with. The Profit and loss account showing the "book profit" of Rs.3932.11 has been made up keeping the existing provisions and requirements of section 115 JA(2). The Assessee thus claimed that the book profits for the purpose of calculation of MAT should be Rs.3932.11 lacs as shown in the computation of income.

42. The AO did not accept the Assessee's argument. He rejected the claim of the Assessee that the accounting effect of withdrawal from the general reserve for crediting it to the P&L A/c. has been achieved by reducing the losses directly from the general reserve account as factually incorrect. He held that the losses of BDD of SPCL between the appointed date and effective date have not been recognized in the corporate accounts. Such losses have

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been set off against the revaluation reserve created during the take over of the BDD from SPCL. He held that revaluation reserve created was a mere book entry and withdrawal from the said reserve for crediting it to the P&L Account does not arise for consideration at all. He was of the view that the Assessee was attempting to frustrate the intention of law. He held that the corporate accounting should he in accordance with the provisions of part II and III of Schedule VI to the companies act and the assessee is bound to adopt the same. He further held that the object of the legislation was only to find out the book profits according to the system adopted by the asessee. That can be achieved only if the profit and loss account is prepared in accordance with the method adopted by the assessee for corporate accounting. If the other method is permitted then the object of the act would be frustrated.

43. Before CIT(A) the assessee submitted that under scheme of section 115JA of the Act there was no prohibition for having two different accounts one for the purpose of Companies Act, 1956 and the other for the purpose of section 115JA of the I.T. Act. The only requirement under section 115JA(2) is that the P&L Account prepared for the purpose of section 115JA should be in accordance with the provisions of Part II & III of Schedule VI of the Companies Act 1956. It was argued that under the provisions of MAT the legislature never intended that the P&L Account prepared for corporate accounting has to be adopted in toto for the purpose of section 115JA of the Act.

44. The CIT(A) was of the following view:

> "18.2 As per the original provisions of Sec.115J, a company was free, to adopt either straight line method or W.D.V. method of calculating depreciation to work out the figure of book profit. In the case of Nippon Denro Ltd. (62 ITD 205), the Calcutta Bench of the ITAT upheld this position. It was only after introduction of Sec,115JA(2) with effect from 1/4/1997 that a company is required to follow the same method of calculating depreciation to arrive at Book profit for purpose of Sec

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115JA as the method adopted for company law. It is significant to note that this amendment still left upon the possibility of following different accounting policies in respect of other incomes and expenses. It is only by introducing Sec.115JB, in the place of Sec115JA w.e.f. 1/4/2001 that it was made mandatory to follow the same accounting policies both for the Companies Act and MAT under the Income -tax Act. The A.O. was not correct in holding that the provisions of Sec.115JB were implied in Sec.115JA.

18.3 The possibility of companies following different accounting policies in separate P&L accounts prepared for the companies Act and prepared for Section 115J of the I.T.Act have been recognized by the ITAT in the following cases:

i) Bell Ceramics Ltd. (69 ITD 150)(Ahmedabad)
ii) Nippon Deuro Ltd. (62 ITD 205)(Calcutta)
iii) Modern Woollens Ltd. (47 ITD 154)(Mumbai)

In the case of Nippon Beuro Ltd., the Calcutta Bench noted the contrary view of the Pune Bench of the ITAT in the case of Sudarshan Chemicals Ltd. (60 ITO 629), referred to by the A,0. and concluded that Sec.ll5J nowhere provides that net profit shown in the P&L Account for corporate accounting should be adopted. The same principle applies with respect to Sec.I1SJA also. In any case the decision in Sudarshan Chemicals Ltd, was based on a concession by counsel for the appellants' in that case and hence cannot be applied in other cases.

19, In the light of what is discussed above, the assessee was justified in claiming the loss of is. 5,70,29,630/- in the computation of book profit u/s. ll5JA, even-though the same adjusted against the General reserve in the published accounts represented before the share holders. The A.O. is directed to compute the book profit u/s.115JA accordingly.

45. Aggrieved by the order of the CIT(A) the revenue has appreciated Ground No.5 before the Tribunal.

46. The ld. D.R strongly placed reliance on the decision of the Hon'ble Supreme Court in the case of Apollo Tyres, 255 ITR 217 (SC) and submitted that the P&L Account prepared for the purpose of the approval of the AGM of a company is conclusive for determining book profits under section 115JA

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of the Act. The ld. Counsel for the assessee on the other hand submitted that section 115JA (2) clearly lays down that every assessee being a company shall for the purposes of section 115JA prepare its P&L Account for the relevant previous year in accordance with the provisions of Part II & III of Schedule VI of the Companies Act, 1956. He pointed out that the proviso to section 115JA(2) only lays down that in such P&L Account so prepared the depreciation shall be calculated in the same method and rates at which it is calculated while preparing the P&L Account laid before the Company at its AGM in accordance with the provisions section 210 of the Companies Act 1956. His submission was that preparation of a separate P&L Account for the purpose of section 115JA is not prohibited and it is not necessary that the very same P&L Account prepared for the purpose of laying before the company at this AGM under section 210 of the Companies Act should be adopted for the purpose of section 115JA of the Act also. The only condition required to be complied as laid down in proviso to Sec.115JA(2) is that while preparing the profit and loss account for the purpose of Sec.115JA of the Act, the depreciation shall be calculated on the same method and rates which have been adopted for calculating the depreciation for the purpose of preparing the profit and loss account laid before the company at its annual general meeting in accordance with the provisions of section 210 of the Companies Act, 1956 (1 of 1956). He further pointed out that section 115JB of the Act, which was introduced by the Finance Act 2000 specifically provides in the second proviso to sub-section (2) thereof that the accounting policies and accounting standards adopted for preparing such accounts and P&L Account and the method and rates adopted for calculating depreciation shall be the same as is adopted under the Companies Act 1956. The ld. Counsel for the assessee pointed out that this deliberate departure in section 115JB only goes to show that under section 115JA the accounting policies and the accounting standards adopted under section 115JA can be different from the one adopted for the purpose of the Companies Act 1956. It was his

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further submission that the Hon'ble Supreme Court in the case of Apollo Tyres (supra) does not lay down any prohibition on having two accounts or two P&L Account but only lays emphasis on the condition that the same should be prepared in accordance with the provisions of the Companies Act 1956. The ld. Counsel for the assessee in this regard referred to the decision of the Hon'ble Supreme Court in the case of Marshall Sons & Company (India) Ltd. vs. ITO, 223 ITR 809 (SC), wherein the Hon'ble Supreme Court held that when a scheme of amalgamation is sanctioned by Court the effective date from the amalgamation shall take place is specified. Where such date is not specified but the scheme is sanctioned by the Court the date of amalgamation is the date specified in the scheme as date of transfer. The ld. Counsel for the assessee submitted that the date of transfer in this case was 1/4/1997 but the effective date from which the business was actually transferred was 19/6/1997. Therefore, for the period from 1/4/1997 to 18/6/1997 the losses of the amalgamated company namely M/s. Sumitra Pharmaceuticals' & Chemicals Ltd. (SCPL) ought to be treated as losses of the assesee and this was correctly given effect to in the P&L Account filed by the assessee for the purpose of section 115JA of the Act. Our attention was also brought to the fact that such P&L Account was duly certified as true by the auditors.

47. The ld. Counsel for the assessee drew our attention to the decision of the Hon'ble Gujarat High Court in the case of DCIT vs. Arvind Mills, 314 ITR 251(Guj), wherein the Hon'ble Gujarat High Court took the view that P&L Account prepared in accordance with Part II & III of Schedule VI to Companies Act, 1956 for the purpose of section 115JA of the Act which is different from P&L Account placed before AGM is permissible. The Hon'ble Gujarat High Court considered the decision of the Hon'ble Supreme Court in the case of Apollo Tyres (supra) while so holding. The following other

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decision laying down similar proposition were also referred to by the ld. Counsel for the assessee.

(1) CIT vs. Surat Textile Mills Ltd., 317 ITR 367 (Guj)

(2) CIT vs. Prakash Industries Ltd., 324 ITR 391

(3) Swan Mill Ltd. vs. ACIT (2006) 6 SOT 420 (Mum).

48. We have considered the rival submissions. We find force in the submissions of the ld. Counsel for the assessee . Admittedly the losses of SPCL were for the period from 1/4/1997 to 18/6/1997. As per the scheme sanctioned by the Hon'ble High Court, the date of transfer of SPCL was 1/4/1997 and in accordance with law laid down by the Hon'ble Supreme Court in the case of Marshall Sons & Company(supra) income of the amalgamating company from the date of transfer has to be assessed in the hands of the amalgamating company. Accordingly the loss of SPCL for the aforesaid period had to be taken into consideration. In the P&L Account prepared in accordance with the provisions of companies Act 1956 the assessee has not shown this loss in the P&L Account. In the P&L Account and appropriation account a sum of Rs. 1.00 crores was transferred to general reserve account in the balance sheet. From this general reserve the loss incurred by SPCL from 1/4/1997 to 18/6/97 was reduced. The effect of such book entries according to the ld. Counsel for the assessee would be the same as was done in the P&L Account prepared for the purpose of section 115JA of the Act. We do not wish to go into this aspect regarding the effect of such accounting entry as there was a revaluation reserve created on amalgamation. We are of the view that the P&L Account prepared by the assessee for the purpose of 115JA of the Act has been duly certified by the Chartered Accountant. There is no complaint that the same is not in accordance with provisions of part II & Part II of Schedule VI of the Companies Act 1956. As rightly pointed out by the ld. Counsel for the

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assessee the only restriction in 115JA(2) is regarding the depreciation which has to be in conformity with the method adopted under Companies Act. There is however, departure in section 115JB(2) of the Act which provides that the accounting policies and accounting standards adopted while preparing P&L Account for section 115JB of the Act should correspond to the one adopted for the purpose of Companies Act 1956. In that view of the matter we are of the view that the order of the CIT(A) has to be upheld. Accordingly Ground No.5 raised by the revenue is dismissed.

49. Ground No.6 raised by the revenue reads as follows:

> "Erred in directing to reduce an amount of Rs.98.35 lakhs transferred to the reserves while computing profits u/s. 115JA ignoring the computation made by the assessee as per Company's Act."

50. In computing the book profit the assessee had reduced an amount of Rs.98,50,000/- from profit as per Profit and Loss Account. This sum was shown as transfer to reserve in the Profit and Loss Appropriation Account. It was the claim of the Assessee that this sum was transferred to the Reserve Account to meet liability on account of redemption of debentures issued by the Assessee. According to the AO since the said amount was appropriation of the profits and since it was in the nature of application of income, the assessee was asked to explain as to how such an appropriation can be claimed as deductible from book profits for the year.

51. The Assessee submitted that during the F.Y. 1996-97, the Assessee company made a provision for transfer of a sum of Rs.98,50,000/- in respect of its ascertained future liability to redeem debentures issued by the company. The Assessee pointed that in accordance with explanation to sub-section 2 of section 115 JA, "Book Profits" means the net profit as shown in the Profit & Loss Account for the relevant previous year prepared in accordance with the provisions of Parts II and III of Schedule VI of the

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Companies Act, 1956. If the Book Profits are arrived at after reducing amounts set aside to provisions then, such profits as per the explanation shall be increased by the amount or amounts set aside to provisions made for meeting liabilities, other than ascertained liabilities. Thus, in arriving at "Book Profit", if the profits does not include any amounts set aside for ascertained liabilities, the same shall have to be reduced from such book profits to arrive at the figure of chargeable book profits u/s. 115JA. Since the aforesaid sum of Rs.98,50,000/- has to be set aside to meet the liability on account of redemption of debentures to the debenture redemption reserve, it is for meeting ascertained liability to redeem/repay the debentures issued by it in the past and therefore it has to be reduced from the profits to arrive at book profits u/s.115JA of the Act. These debentures are redeemable in future and our company's liability to do so on specified dates in future is ascertained in accordance with the terms of redemption of these debentures. The Assessee claimed that explanation to section 115JA (2) clearly permits reduction of the amounts transferred to debenture redemption reserve in arriving at the chargeable "Book Profits" under the said section. The Assessee further pointed out that the term ascertained liabilities is not specifically defined in section 115 JA and therefore its meaning will have to he gathered from the meaning attached to it by the Companies Act, 1956. The words "provision" and "reserve" have been defined in part III of Schedule VI to the Companies Act, 1956. The definition clearly indicates that if an amount is retained by way of providing for any known liability, that amount shall not be treated as reserve". Assessee also cited the decision of Supreme Court in the case of National Rayon Corporation Ltd. Vs. CIT (227 ITR 764).

52. The AO however did not agree with the above submissions of the Assessee. He was of the view that the sum in question was transferred to reserve as part of the appropriation account. He did not agree with the

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contention of the Assessee that the debenture redemption reserve is not a reserve as per the definition under part III of schedule VI of the Company's Act. He held that Part Ill of Schedule VI to the Companies Act, 1956 provides the definitions for the purpose of interpretation of part I and Part II of the said schedule. He referred to Part III of Schedule VI to the Companies Act, 1956 wherein it was stated as under:

> "7(1) For the purpose of part I & II of this Schedule, unless the context otherwise requires:
>
> (b) The expression "reserve" shall not, subject as aforesaid, include any an: amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets or retained by way of providing for any known liability".
>
> Where as, Part II of the Schedule deals with the requirements as to Profit and loss account and it is provided in clause 3 (vii) that the P & L A/c. shall disclose:
>
> > "('vii) The amount reserved for -
> >
> > (a) repayment of share capital; and
> > (b) repayment of loans."

Based on the above, the AO was of the view that the amount set aside for redeeming the debentures is after all repayment of loan and therefore it is a reserve as per part II and III of Schedule VI of Companies Act. Therefore, assessee's contention that it was not a reserve was rejected by the AO. He further held that as per explanation to section 115 JA (2) of the Income tax Act, the book profit has to be adjusted by increasing the net profit by "the amounts carried to any reserves by whatever name called". He also held that the Assessee's reliance on the Supreme Court decision was also misplaced because the decision is with regard to the provisions of Companies (profits) Sur tax Act, 1964. Accordingly, the book profit was recomputed by disallowing the amount transferred to debenture redemption reserve.

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53. Before CIT(A), the Assessee pointed out that as per the various debenture trust deed, the assessee was required to create a Debenture Redemption Reserve of Rs. 1055.80 Lacs for meeting its ascertained liability in future for redeeming the debentures. The assessee had created a reserve of Rs, 957.45 Lacs upto 313.96. For the year ended 31.3.97 the assessee transferred further sum of Rs. 98.35 lacs to this reserve. In the published accounts for the year this was shown as appropriation from the profits and loss accounts. In the computation of book profit for purpose of Sec.115JA, the assessee reduced this amount from the book profit. According to the assessee this was nothing but a provision made to meet the ascertained liability in future and hence should not be included in the book profit.

54. The CIT(A) agreed with the contention of the Assessee that the provisions of Parts-II and III of Schedule VI to the Companies Act, relied upon by the A.O., do not support his finding that the amount in question was a reserve. Part - III clearly laid down that “reserve” shall not include any amount retained by way of providing for any known liability. The amount of 98.35 Lacs transferred to the DRR was the amount retained by way of providing for the known liability of repayable debentures in future. He was of the view that liability on account of redemption of debentures was known liability of the assesse. Therefore the amount of Rs. 98.35 lacs cannot be characterized as reserve within the meaning of Part-III of Schedule- VI of the Companies Act. He also held that Part- II of the Schedule, quoted by the A.O. in the assessment order, deals with what should be disclosed in P&L Account and does not say what constitute a reserve. He also agreed with the submission of the Assessee that the amount transferred to DRR represented the provision made for meeting an ascertained liability, namely the debentures. He was of the view that the decision of the Supreme Court in the case of National Rayon Corporation Ltd. Vs. CIT (227 ITR 764) supported the claim of the Assessee. He held that the basic principle laid

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down in that case was that liability on account of redemption of debentures was a known liability and that any amount retained by way of providing for such known liability will not be "reserve". That principle applies would apply to the case of the Assessee and if the liability on account of redemption of debentures in question are treated as ascertained liability, the amount transferred to the DRR should be treated as provision made for known liability but not a reserve created. Therefore the amount of Rs.. 98.35 Lacs should be excluded from the book profit as provided in clause (c) of the Explanation to section 115JA of the I.T. Act. The A.O. was directed to compute the book profit accordingly.

55. Aggrieved by the order of the CIT(A), the revenue has raised Gr.No.6 before the Tribunal. We are of the view that the order of the CIT(A) on this issue has to be upheld and the reliance placed by the DR on the order of the AO cannot be accepted. As rightly held by the CIT(A) the amount in question cannot be said to be a reserve but was only a provision. The liability for which such provision was made was an ascertained or known liability and, therefore, amount was to be reduced from the profit as per P&L Account prepared in accordance with provisions of Company Act 1956 to arrive at the book profits under section 115JA of the Act. Consequently Ground No.6 raised by the revenue is dismissed.

56. Ground No.7 & 8 raised by the revenue reads as follows:

> 7) "Erred in deleting addition of Rs.44.06 lakhs on account of security deposit taken on the account of bogus lease transaction disclosed by the assessee under VDIS & KVSS Scheme by admitting fresh grounds of appeal."
>
> 8) "Erred in directing to delete provisions for leave encashment while computing profits u/s.115JA ignoring that these are unascertained liabilities."

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57. Before CIT(A) the assessee raised the following additional grounds of appeal in the course of hearing of the appeal:—

> i) That the A.0. erred in not excluding Short term capital gain of s, 44,O6,6l5/- being capital gains arising on sale of assets leased in pursuance of lease agreement which was held to be not operative.
>
> ii) That the A.O. erred in computing the book profit as per Explanation to Sec. 115JA of the I.T. Act by adding an amount of Rs. 19,02,000/- being provision for leave encashment treating it as contingent liability.

58. The CIT(A) forwarded the additional grounds to the A.O for his comments. After taking into account the comments of the A.O and the argument of the assessee on the additional grounds of appeal, the CIT(A) gave the following findings as given below:

<u>59. Short Term Capital Gain:</u>

The assesee had entered into certain lease transaction during the F.Y 93-94 relevant to the A.Y 94-95. The details of these lease transactions were as under:-

a) Cost of the assets leased	Rs. 1,04,48,708/-
b) Date of purchase	25/9/93
c) Outstanding security deposit in respect of the lease during F.Y. 1996-97 (A.Y.1997-98)	Rs. 44,06,615/-
d) Depreciation claimed	50% in A.Y 1994-95 50% in A.Y 1995-96

60. Treating the lease transaction to be not genuine the A.O disallowed depreciation on the leased assets for the A.Y. 94-95 which was confirmed by the CIT(A). However, availing of the KVSS Scheme, 1998 for the A.Y 1994-95

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and VDIS Scheme, 1997 for A.Y 1995-96, the assessee offered for assessment the amount of depreciation claimed on the asset in question. In other words, the assessee withdrew the claim of depreciation mentioned above for these two assessment years. Consequent to that the assessee terminated the lease agreement during the A.Y. 96-97 and forfeited the outstanding security deposit of Rs. 44,06,615/- as on the date of termination of the lease agreement.

61. By the time the original return of income for A.Y 1997-98 was filed on 31/12/97, the security deposit of Rs. 44,06,615/- was forfeited as a result of terminating the lease agreement on 11/3/97. However, by that time the assessee had not offered for assessment the depreciation claimed for assessment years 1994-95 & 95-96 under the KVSS & VDIS Schemes mentioned above. Therefore, in the return of income the forfeited security deposit of Rs, 44,06,615/- was offered for assessment as Short term capital gain as per provisions of Sec.50 of the I.T. Act since the W.D.V. of leased assets became Nil after claiming 100% depreciation. The Assessee claimed that since the entire lease transactions had been reduced as inoperative and the entire depreciation on the leased assets claimed earlier were offered to tax by availing of the KVSS & VDIS Schemes, the forfeited outstanding security deposit of Rs. 44,06,6l5/- was nothing but return of the assessee's capital on which levying of Short term capital gain did not arise. In this view of matter the assessee argued that the Short term capital gain of Rs. 44,06,615/- should be de1eted from the total income assessed. In his assessment order the A.O, stated that there was no case to exclude this short term capital gain, arising out of the forfeited outstanding security deposit, from the total income assessed. The A.O. observed that the assessee was not clear in his contention that the lease agreement was inoperative. According to the A.O the Short term capital gain was leviable because "as per

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the assessee's books the assets existed, they were sold and the assessee received payment by cheque.

62. On the above facts and stand of the AO, the CIT(A) was of the view that there was no question of levying any Short term capital gain on the forfeited amount of outstanding security deposit after the assessee offered for assessment the depreciation claimed for the assessment Years 94-95 & 95-96 under the KVSS & VDIS Scheme respectively. When the depreciation was not allowed on the assets in question and the assessee was not held to be the owner of the assets, the question of charging Short term capital gain on sale of the assets, by way of forfeiting the outstanding security deposit did not arise. Charging Short term capital gain on the assets in question runs counter to the Scheme of KVSS & VDIS under which the assessee paid taxes by withdrawing the claim for depreciation on the assets. The AO was, therefore, directed to exclude Short term capital gain of Rs.44,06,615/- from the total income assessee.

63. Aggrieved by the order of the CIT(A), the Revenue has raised Gr.No.7 before the Tribunal.

64. Provision for Leave Encashment on Computation of Book Profit u/s. 115JA: The claim of the Assessee was that the liability on account of provision for leave encashment was a known and ascertained liability in view of the Supreme Court decision in the case of Bharat Earth Movers Ltd., vs. CIT 243 ITR 428 (SC), and provision for leave encashment cannot be treated as contingent liability. The CIT(A) agreed with the stand of the Assessee and held that the said liability should be treated as allowable deduction from the profits of the assesse and consequently in computing the book profit u/s. 115JA also it should be treated as allowable deduction and hence should be

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excluded from the book profit. The AO was directed to allow deduction of Rs. 19,02,200/- in computing the book profit for purpose of 115JA.

65. Aggrieved by the order of the CIT(A), the revenue has raised Gr.No.8 before the Tribunal.

66. We have heard the submissions of the learned DR as well the learned Counsel for the Assessee on Gr.No.7 and 8. The ld. D.R could not controvert the factual position as emanating from the order of the CIT(A) as far as Ground No.7 is concerned. As far as Ground No.8 is concerned provision for leave encashment is ascertained liability as held by the Hon'ble Supreme Court in the case of Bharat Earth Movers Ltd. vs. CIT, 245 ITR 428 (SC). We, therefore, do not find any ground to interfere with the order of the CIT(A). Consequently Ground No.7 & 8 of the revenue are dismissed.

67. C.O. No. 119/MUM/2002:

Ground No.I raised in the Cross Objection reads as under:

"1. The CIT(Appeals) erred in upholding the disallowance of Rs. 67,91,000/- claimed as Project Expenses."

2. The Appellant prays that aforesaid expenditure may be allowed as a deduction in computation of the taxable income."

68. The following expenses incurred by the assessee were claimed as revenue expenditure whereas the A.O treated it as capital expenditure:-

i) Rs. 44.94 lacs paid to various professional and consulting agencies like National Institute of Technology, obtaining assistance from these institutions in respect of better and improved method of producing Bulk Drugs & Pharmaceutical formulation products.

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ii. b.12.74 lace spent on travelling of Senior Executives to Vietnam fox exploring the preliminary feasibility for setting up the plant there.

iii. Rs,1O.23 lace paid to various professionals for rendering services y way of suggesting improvements in the Bu2lc Drug Plant at Hyderabad.

69. According to the Assessee, the A.O. treated the expenditure as capital expenditure without any discussion or reasons. The assesse claimed before CIT(A) that the expenses of Rs. 44.94. lacs and Rs.10.23 lacs mentioned were incurred to improve the productivity of the manufacturing facilities and hence it should be treated as revenue expenditure. The expenditure for travel to Vietnam was incurred in connection with the plans to expand the existing business of pharmaceuticals by setting up a factory there. It was argued that such expenditure incurred for expanding the existing business should be treated only as a revenue expenditure.

70. The CIT(A) was not convinced with the arguments advanced by the assesse. He held that any expenditure claimed to be revenue in nature should be proved to have been incurred for purpose of the business. But no evidence has been let by the assessee to show that the amounts of Rs.44.94 lacs and Rs.12.74 lacs were expenses incidental to the business of the Bulk Drugs and Pharmaceuticals formulations and hence they were rightly treated as capital expenses. He also held that travelling expenses to Vietnam have also not been proved to have been incurred for purpose of the assessee's business. The disallowances of the these expenses were therefore, confirmed.

71. Aggrieved by the order of the CIT(A), the Assessee has raised Gr.No.1 in C.O. We are of the view that the assessee had not given enough information on the nature of expenses. Admittedly fees were in respect of new project

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and its relevance to the existing business of the assessee could not be established by the assessee. We, therefore, do not find any ground to interfere in the order of the CIT(A). Ground No.1 raised in the cross objection is dismissed.

72. Ground No.II of the Cross Objection reads as under:

> "1. The CIT(Appeals) erred in upholding the disallowance of Rs. 8.19,005/- claimed as Machinery shifting expenses.
>
> 2.The appellant prays that the disallowance be directed to be deleted."

73. It was fairly accepted by the parties that the issue has to be decided against the assessee following the ratio laid down by the Hon'ble Supreme Court in the case of Sitapur Sugar Works Ltd. vs. CIT 49 ITR 160 (SC) wherein it was held that the expenditure incurred on shifting of factory would be a capital expenditure. Consequently ground No.II raised in the cross objection is dismissed.

74. The assessee has filed an application seeking to raised the following additional grounds.

> "1. The DCIT erred in not granting depreciation on Rs.13,73,793/- being amount capitalized in A.Y. 1989-90 out of repairs to building.
> 2. He failed to appreciate and ought to have held that since certain amount of repairs to building were disallowed by treating it as capital expenses, it was incumbent on him to allow depreciation on the same.
>
> 3. The appellant prays that the DCIT be directed to grant depreciation pertaining to repairs capitalized in A.Y 1989-90."

75. The additional ground being purely legal, requiring no examination of new facts and being purely consequential is admitted for adjudication. The

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AO is directed to grant depreciation after considering capitalized value of the repairs of the building after verification.

76. In the result, the appeal by the revenue is partly allowed while the C.O by the assessee is partly allowed for statistical purposes.

Order pronounced in the open court on the 16th day of May 2012

Sd/- Sd/-
(P.M.JAGTAP) (N.V.VASUDEVAN)
ACCOUNTANT MEMBER JUDICIAL MEMBER
Mumbai, Dated 16th May 2012

Copy to: 1. The Appellant 2. The Respondent 3. The CIT City –concerned
4. The CIT(A)- concerned 5. The D.R"E" Bench.

(True copy) By Order

Asst. Registrar, ITAT, Mumbai Benches

MUMBAI.

Vm.