

INCOME TAX APPELLATE TRIBUNAL
 DELHI BENCH "I-I": NEW DELHI
 BEFORE SMT DIVA SINGH, JUDICIAL MEMBER
 AND
 SHRI PRASHANT MAHARISHI, ACCOUNTANT MEMBER

ITA No. 2941/Del/2011
 (Assessment Year: 2003-04)

Motorola India Pvt Ltd, Motorola Excellence Centre, 415/2, Sector-14, MG road, Gurgaon, Haryana PAN: AAACM9343D	Vs.	ACIT, Gurgaon Circle, Gurgaon
(Appellant)		(Respondent)

ITA No. 3234/Del/2011
 (Assessment Year: 2003-04)

ACIT, Gurgaon Circle, Gurgaon	Vs.	Motorola India Pvt Ltd, Motorola Excellence Centre, 415/2, Sector-14, MG road, Gurgaon, Haryana PAN: AAACM9343D
(Appellant)		(Respondent)

ITA No. 4643/Del/2011
 (Assessment Year: 2004-05)

Motorola Solutions India (P) Ltd, 415/2, Motorola Excellence Centre, MG road, Haryana PAN: AAACM9343D	Vs.	ACIT, Gurgaon Circle, Gurgaon
(Appellant)		(Respondent)

ITA No. 4581/Del/2011
 (Assessment Year: 2004-05)

ACIT, Gurgaon Circle, Gurgaon	Vs.	Motorola Solutions India (P) Ltd, 415/2, Motorola Excellence Centre, MG road, Haryana PAN: AAACM9343D
(Appellant)		(Respondent)

Assessee by :	Shri G.C. Srivastava, Adv Shri Suvinay K. Dash, Adv
Revenue by:	Shri Sanjay I Bara, CIT DR
Date of Hearing	28/05/2018
Date of pronouncement	24/08/2018

ORDER

PER BENCH

1. These are the cross appeals filed by the assessee, M/s. Motorola India Pvt Ltd as well as the Id AO, the Additional Commissioner of Income Tax, Range Gurgaon against the order of the Id CIT (A), Panchkula, passed on 17.03.2011 and 1/8/2011 for the Assessment Year 2003-04 and 2004-05 respectively.
2. The assessee has raised the following grounds of appeal in ITA No. 2941/Del/2011 for the Assessment Year 2003-04.

“1. That on the facts and in the circumstances of the case and in law, the Ld. AO as well as the Hon’ble CIT (Appeals) erred in disallowing the provision for leave encashment of Rs. 4,16,33,651 by invoking the provisions of section 43B(f) of the Income Tax Act, 1961 (Act).

1.1 That the Ld. AO as well as the Ld. CIT (Appeals) erred on facts and in law in not appreciating that the provisions of section 43B(f) of the Act were not applicable in the instant case.

2. That the Ld. CIT(Appeals) erred in remanding back to the Ld. AO the issue of verification of provision for leave encashment reversed during the year of Rs. 3,33,28,504/- when complete details in this regard were produced before the Id. CIT (Appeals).

3. That the Hon’ble CIT (appeals) erred on the facts and in the circumstances of the case, by remanding back for verification, the disallowance made by the AO on account of provision for warranty expenses amounting to Rs. 4,56,36,435.

4. That the Ld. CIT(Appeals) erred in remanding back to the Ld. AO the issue of verification of provision for warranty reversed during the year of Rs. 1,87,15,822/- to the Assessing Officer, when complete details in this regard were produced before the Ld. CIT (Appeals).

5. That the Ld. AO as well as the Hon’ble CIT (appeals) grossly erred on facts and in law in disallowing bad debts written-off of Rs. 23,94,011 being TDS written off by the appellants.

6. That the Ld. AO as well as the Hon’ble CIT (appeals) erred on facts and in law in disallowing Rs. 67,14,164 incurred on acquiring the computer software and treating the same as capital expenditure.

6.1 That the Ld. CIT(Appeals) erred in stating that no details of expenditure on software were submitted despite the fact that no such details were specifically called for by the CIT(Appeals) as well as the AO.

7. *That the Ld. AO as well as the Hon'ble CIT (appeals) have grossly erred on facts and in law in disallowing Rs. 9,55,200 being expenses incurred on late cancellation and holding that the same cannot be treated as business expenditure allowable u/s 37(1) of the Act.*
8. *That the Ld. AO as well as the Hon'ble CIT (appeals) grossly erred on facts and in law in restricting claim of deduction u/s 80HHE of the Act to Rs. 34,54,016 as against the claim of Rs. 36,50,192 made by the appellant in its return of income.*
- 8.1 *That the Ld. AO as well as the Hon'ble CIT (Appeals) grossly erred on facts and in law in computing 'profit of the business' for the purpose of deduction u/s 80HHE of the Act, by reducing 90% of gross rental income without reducing the proportionate depreciation and 90% of gross interest income without reducing interest expenses relatable thereto.*
9. *That the Hon'ble CIT (Appeals) erred in following the order passed by the Ld. AO with respect to transfer pricing adjustment of Rs. 5,46,28,379/-, the same being arbitrary, contrary to law, facts and circumstances of the case.*
- 9.1 *That the Hon'ble CIT (Appeals) erred in following the order of the Ld. AO, since the Ld AO did not exercise his judgment in referring the appellant's case to the Transfer Pricing Officer (TPO).*
- 9.2 *That the Ld. CIT (Appeals) erred in law in relying on the order u/s 92CA(3) of the Act passed by the TPO and Ld. AO's action of confirming the TPO's order, which in itself is bad in law and liable to be quashed.*
- 9.3 *That the Ld CIT (Appeals) grossly erred both in facts and law by upholding the decision of the Ld. AO/ TPO of disregarding the transfer pricing study (TP Study) conducted by the appellant in determining the arm's length price with respect to the international transactions undertaken by the appellant to provide software development services, to its overseas group companies.*
- 9.4 *That the Ld. CIT (Appeals) has erred on fact and law by upholding Ld. TPO's decision of using his own subjective criteria to identify comparables for computing the arm's length price and also has disregarded the comparability analysis undertaken by the appellant.*
- 9.5 *That the Ld CIT (Appeals) grossly erred on facts and in law by confirming the decision of the Ld. TPO of not allowing working capital adjustment to the margins of the comparable to bring them in the line with the working capital requirements of the appellant and in doing so confirming the decision of the Ld TPO that the appellant is engaged in undertaking 'high end' software development activities..*
- 9.6 *That the Ld. CIT (Appeals) has erred by not commenting on the decision of the Ld. TPO of not allowing any adjustment for difference on account of risk undertaken by comparables vis-a-vis appellant which is not a risk bearing entity.*
- 9.7 *That the Ld CIT (Appeals) has grossly erred on fact and law by holding that the benefit of (+/-) 5% range mentioned in the proviso to section 92C, of the, Act is not available as a standard deduction to the appellant for computing the transfer pricing, adjustment.*
- 9.8 *That the Ld. CIT (Appeals) erred in directing the Ld AO/ Ld TPO to verify the value/ Percentage of related party transactions in case of comparables during the year when details in this regard were produced before the Ld. CIT (Appeals) as well as Ld TPO and-in directing the Ld AO/ Ld TPO to re-compute the ALP.*

10. *That the Ld. AO erred on facts and in law in initiating penalty proceedings u/s 271(1)(c) of the Act.*"
3. The revenue has raised the following grounds of appeal in ITA No. 3234/Del/2011 for the Assessment Year 2003-04.
- "1. *On the facts and in the circumstances of the case, the Ld. CIT(A) has erred, both on facts and in law, in giving direction to the AO to verify/re-compute and allow the expenses of;*
- i) *Rs. 3,33,28,504/- disallowed by AO on a/c of reduction of provision of leave encashment reversed,*
 - ii) *Rs. 2,59,30,473/- disallowed by AO on a/c of provision of warranty expenses,*
 - iii) *Rs. 1,87,15,822/- disallowed by AO on a/c of provision for warranty reversed, and*
 - iv) *Addition of Rs. 5,46,28,379 made by AO on a/c of transfer pricing adjustment, when these disallowances/additions were prudently made by the AO while completing the assessment and pointing out specific violations."*
2. *On the facts and in the circumstances of the case, the Ld. CIT (A) has erred, both on facts and in law, in giving directions to the AO to verify/ re-compute and allow the expenses as this would tantamount to examining the issues a fresh. The order is preserve in law as the directions are contrary to the provisions of section 251(1)(a) of the Act. As per provisions of section 251 of the Act, the CIT (A) has the power to confirm, reduce, enhance, or annul the assessment where the appeal relates to an assessment order. The power to set-aside has been omitted by the Finance Act, 2001 w.e.f. 01.06.2001. As the order has been passed by the Ld. CIT(A) on 17.03.2011 therefore, the directions are contrary to the provisions of section 251(l)(a) of the Act."*
4. The assessee has raised the following grounds of appeal in ITA No. 4643/Del/2011 for the Assessment Year 2004-05.
- "1 *That on the facts and m the circumstances of the case and m law, the Ld. AO as well as the Hon'ble CIT (Appeals) erred in disallowing the provision for leave encashment of Rs. 2,28,53,601 by invoking the provisions of section 43B(f) of the Income Tax Act, 1961 (Act),*
- 1.1 *That the Ld, AO as well as the Ld, CIT (Appeals) erred on facts and in law in not appreciating that the provisions of section 43B(f) of the Act were not applicable in the instant case.*
 2. *That the Hon'ble CIT (Appeals) erred on the facts and in the circumstances of the case, by remanding back for verification, the disallowance made by the AO on account of provision for warranty expenses amounting to Rs. 14,68,29,299 when complete details in this regard were produced before the Ld CIT(Appeals) and the Ld. AO.*
 3. *That the Ld. AO as well as the Hon'ble CIT (Appeals) erred on facts and in law in disallowing Rs. 42,00,977 (after giving depreciation @ 60%) on account of software expenses without appreciating that the same was a revenue expenditure and not capital expenditure*

4. *That the Ld. AO as well as the Hon'ble CIT(Appeals) grossly erred on facts and in law in restricting the claim of deduction under section 80HHE of the Act to Rs. 39,90,777 as against the claim of Rs, 41,09,176 made by the appellant in its return of income.*
- 4.1 *That the Ld AO as well as the Hon'ble CIT (Appeals) grossly erred on facts and in law in computing 'profit of the business' for the purpose of deduction under section 80HHE of the Act, by reducing 90% of gross rental income without reducing the proportionate depreciation and 90% of gross interest income without reducing interest expenses relatable thereto.*
5. *That the Hon'ble CIT (Appeals) erred in following the order passed by the Ld. AO u/s 143(3) with respect to the transfer pricing adjustment, the same being arbitrary, contrary to law, facts and circumstances of the case and in doing so:-*
- 5.1 *That the Hon'ble CIT (Appeals) erred in following the order of the Ld. AO, since the Ld, AO did not exercise his judgment in referring the appellant's case to the Transfer Pricing Officer (TPO).*
- 5.2 *That the Ld. CIT(Appeals) erred in law in relying on the order u/s 92CA(3) of the Act passed by the TPO and Ld. AO's action of confirming the TPO's order, which in itself is bad in law and liable to be quashed.*
- 5.3 *That the Ld. CIT(Appeals) has erred by not commenting on the action of the Ld AO of disregarding the objections preferred by the appellant in response to the show cause notice issued by the AO as a consequence of the TPO's order.*
- 5.4 *That the Ld CIT(Appeals) grossly erred both in facts and law by upholding the decision of the Ld, AO/ TPO of disregarding the transfer pricing study (TP Study) conducted by the appellant in determining the arm's length price with respect to the international transactions undertaken by the appellant to provide software development services, to its overseas group companies.*
- 5.5 *That the Ld. CIT (Appeals) has erred on fact and law by upholding Ld. TPO's decision of using his own subjective criteria to identify comparables for computing the arm's length price, relying on the comparables selected in the TP Order for assessment year 2003-04 and disregarding the comparability analysis undertaken by the appellant.*
- 5.6 *That the Ld. CIT (Appeals) has erred by not commenting on the decision of the Ld. TK) of not allowing any adjustment for difference on account of risk undertaken by comparables vis-a-vis appellant which is not a risk bearing entity.*
- 5.7 *That the Ld CIT (Appeals) has grossly erred on fact and law by holding that the benefit of (+/-) 5% range mentioned in the proviso to section 92C of the. Act is not available as a standard deduction to the appellant for computing the transfer pricing adjustment.*
- 5.8 *That the Ld. CIT(Appeals) erred in directing the Ld AO/ LA TPO to verify the value percentage of related party transactions in case of comparables during the year when details in this regard were produced before the Ld. CIT (Appeals) as well as Ld TPO and in directing the Ld AO/ Ld TPO to re-compute the ALP.*
- 6 *That the Ld. AO erred on facts and in law in initiating penalty proceedings under section 271(l)(c) of the Act."*

5. The revenue has raised the following grounds of appeal in ITA No. 4581/Del/2011 for the Assessment Year 2004-05.
- “1 On the facts and in the circumstances of the case, the Ld. Commissioner of Income Tax (Appeals) has erred both on facts and in law, in directing the AO to verify the submissions of assessee and then grant the relief of Rs. 14,68,29,299/- on a/c of warranty provisioning which tantamount to setting aside the case and are contrary to the provisions of the amended section 251(1)(a) of the Income Tax Act, 1961.”
 2. On the facts and in the circumstances of the case, the Ld. Commissioner of Income Tax (Appeals) has erred both on facts and in law, in directing the TPO to exclude M/s AFTEK from comparable on the ground of high margin company. Removing a comparable on the ground of high profit making would neither be as per the Act nor would it be a representative set. The above concept is impliedly approved by the ITAT in the case of M/s SAP Labs India P. Ltd reported at 2010- TII-44-ITAT-Bang-TP. Also the Hon'ble ITAT, Mumbai in the case of EXXON MOBIL COMPANY INDIA PVT LTD (2011-TII-68-ITAT-MUM-TP) has held that 'loss or profit cannot be a criterion for acceptance/rejection of a comparable'."
 3. On the facts and in the circumstances of the case, the Ld. Commissioner of Income Tax (Appeals) has erred both on facts and in law, in directing the TPO to exclude the comparable companies having more than 35% related party transactions. The direction may results in inclusion of companies with predominantly related party transactions which would not represent uncontrolled transactions."
6. Brief facts of the case is that the assessee is a company registered in India as a subsidiary of Motorola Incorporation, USA engaged in software development services, import and resale of mobile phones, installation and commissioning of the cellular network and market support services and distribution of the products. 4 assessment year 2003 – 04 it filed its return of income of 28.11.2003 declared gross total income of Rs. 514706984/-. The assessment u/s 143(3) of the Act was passed on 29.03.2006 determining the total income of the assessee of Rs. 1335780169/-. Several additions and disallowance were made by the ld AO which were contested before the ld CIT(A) who vide order dated 17.03.2011 as well as 1/8/2011 for respective assessment years partly allowed the appeal of the assessee. Therefore, both the parties are in appeal before us on different aspects.
7. First we take up the appeal of the assessee 4 assessment year 2003 – 04 where ground No. 1 is with relation to disallowance of the provisions of leave encashment of Rs. 41633651/- by invoking the provisions of section 43B(f) of the Act. The assessee has made provision of the above sum for leave encashment for the year ended on 31.03.2003. The ld AO noted that until the assessment year 2002-03, the assessee was disallowing the above provision, however, for this year it has not been disallowed, and therefore, the ld AO raised the query. The assessee submitted that the claim of provision leave encashment is actually an estimated value of accrued leave as per policy of the company and only those persons who resign can avail the leave encashment. Therefore as the same has not become payable at the end of the

year, provision of section 43B (f) of the Act does not apply. The assessee further submitted that the provision of section 43B(f) do not apply to the assessee as the provision is towards leave encashment and it is not sum payable in lieu of leave. In nutshell the assessee contested that accrued leave which has not become payable is not hit by the provision of section 43B (f) of the Act. The Id AO rejected the contention of the assessee and disallowed the above sum u/s 43B(f) of the Act. The assessee contested the same before the Id CIT (A) who vide para No. 4.2 has held that the provision of section 43B (f) of the Act are squarely applicable and hence, the disallowance was confirmed. Before us, this ground is agitated.

8. The Id AR vehemently submitted that the issue is squarely covered in favour of the assessee by the decision of the Samtel Colour Ltd Vs. DCIT 157 Taxman 39 (Delhi) and Sitaram Textiles Ltd Vs. DCIT 57 ITD 439. The Id AR submitted that the claim for leave encashment is an estimated value of accrued leave and only the employees who have resigned can take leave encashment. It is not the sum payable and therefore, provision of section 43B (f) does not apply. He submitted that the company does not have a policy whereby, the employees can encash the leave without resigning. Therefore, he submitted that the provisions are for accrued leave but not leave encashment.
9. The Id DR vehemently contested the argument of the assessee as the assessee itself was adding the above sum up to Assessment Year 2002-03. He submitted that even leave encashment provision is also for the purpose of accrued leave. Therefore, applicable the provision of section 43B(f) are applicable to that.
10. We have carefully considered the rival contentions and found that the assessee has made a provision for leave encashment of Rs. 41633651/-. This sum was not paid during the year and therefore, is outstanding as provision for leave encashment payable. The only issue is whether the provision of section 43B(f) applies to that or not. As per provisions of section 43B (f) of the act any deduction otherwise allowable under the act in respect of any sum payable by assessee as an employer in lieu of any leave at the credit of his employees shall be allowed irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him only in computing the income referred to in section 28 of the previous year in which some such sum is actually paid by him. Therefore irrespective of the previous year in which the liability to pay such sum was incurred by the assessee according to the method of accounting regularly employed by him any such provision for leave encashment for accrued leave shall be allowable only in the year in which such sum is paid. According to the assessee the above sum is payable to the employees who leaves the job by resigning. It is not payable to any employees who are working with the company. The assessee claimed that the liability created

would keep getting accumulated and not payable until the employee leaves the company. The Id AR heavily relied upon the decision of the Bharat Earthmovers 245 ITR 428. We have carefully considered the decision of the Hon'ble Supreme Court however, the issue before the Hon'ble Supreme Court was that whether the provision for meeting the liability on earned leave by an employee is an admissible deduction. The Hon'ble Supreme Court has held that the above liability is a provision made by the assessee for meeting the liability incurred by it under the leave encashment scheme proportionate with the entitlement earned by the employees of the company would be allowable as deduction the year in which the provision was made for that liability. It was further held that liability was not contingent liability but accrued liability. The above decision was referred for Assessment Year 1978-79. However, disallowance has been made by the Id AO and confirmed by the Id CIT (A) u/s 43B(f) of the Act. There cannot be any doubt that leave encashment liability is an eligible deduction available to the assessee. But, in view of the clear-cut provisions of the law that from 1 April 2002 leave salary payable by the assessee as an employer to his employees is brought within the purview of section 43B of the act However, the relaxation contained in the 1st proviso is available. On further it is clarified that once deduction of the provision made in an earlier year's is allowed, no deduction is permissible in respect of the same amount once again on payment basis. Therefore, if the assessee has made the provision of leave salary which has not been paid on or before the due date prescribed under the income tax act for filing of the return of income then such provision cannot be allowed as deduction in the year in which the provision is made but the payment has not been made before the due date of filing of the return of income. In view of this, we do not find any infirmity in the order of the lower authorities. Hence ground number 1 of the appeal of the assessee against the disallowance of provision of leave encashment by invoking the provisions of section 43B (F) of the act of Rs. 41633651/- is dismissed.

11. Similarly the ground number 1 of the appeal of the assessee for the assessment year 2004 – 05 except where the disallowance is made of ₹ 2 2853601/-. For similar reasons we also dismiss the ground number 1 of the appeal for assessment year 2004 – 5 of the assessee.
12. Ground number 2 of the appeal of the assessee is with respect to the disallowance of provision of leave encashment reversed during the year, which was referred back to the learned assessing officer by the learned CIT appeal for verification. It was submitted before us that it has been allowed by the learned assessing officer after verification. Therefore, the grievance of the assessee does not survive. In view of the fact that assessee already has the relief, this ground number 2 of the appeal of the assessee does not survive hence is dismissed.

13. The ground number 3 of the appeal of the assessee for assessment year 2003 – 04 is also against the provision for warranty of Rs. 45636435/- remanded back to the learned assessing officer for verification by the learned CIT – A. It was submitted before us that on verification, the learned assessing officer has allowed the claim of assessee and therefore the grievance of the assessee does not survive and hence, ground number 3 of the appeal of the assessee is dismissed.
14. The ground number 4 of the appeal of the assessee for assessment year 2003 – 04 is against the disallowance of provision for warranty reversed during the year which was remanded back by the learned CIT – A to the learned assessing officer for verification. It was submitted that on verification the learned assessing officer has allowed the claim of the assessee of ₹ 1 8715822/- and therefore now the grievance of the assessee has been redressed. In view of this fact, we dismiss ground number 4 of the appeal of the assessee.
15. Similar is ground number 2 of the appeal of the assessee for assessment year 2004 – 05 and therefore it is dismissed.
16. Ground number 5 of the appeal for assessment year 2003 – 04 of the assessee is against the disallowance of the bad that written off . Before the learned assessing officer assessee claimed the bad debts written off being the tax deduction at source by the customers of the assessee for which neither the certificates were received nor claimed as advance tax in the return of income of Rs. 2394011/-. During the course of assessment proceedings it was noted by the learned assessing officer that the assessee has claimed a sum of ₹ 3 4946539/- as bad debts written off. The assessee justified its claim stating that the amount in question is actually written off. However the learned assessing officer allowed the claim of the assessee of ₹ 9 024070/- and the balance claim of Rs. 25922469/- was disallowed. Assessee preferred an appeal before the learned CIT – A allowed the claim of the assessee partly however the learned CIT appeal confirmed the disallowance of the bad Debt , which was arising out of the tax deduction at source written off by the assessee. The learned assessing officer stated that the TDS written off does not constitute a debt related to business of the company. As per the details filed by the assessee the claim is arising out of the tax deduction at source made by the deductible/customer while releasing payment to the appellant which was duly shown as income of the appellant on account of sale made, the credit for which has not been received or claimed by the appellant. However, the appellant has not substantiated the reasons for non-receipt or non-claim of tax deduction at source. It was noted by the learned CIT – A that it can be treated as admissible expenditure only if it is proved that the amount in question could not be claimed as the tax deduction at source was either actually not deducted on after deduction not deposited at all and the tax deduction at source certificate was not issued by

the concerned deductor. Therefore the learned CIT-A also confirmed the disallowance holding that appellant has not cared to take the credit of tax deduction at source deducted and therefore same cannot be, trade debt recoverable from the concerned customers. It was further noted by him that appellant has not filed any details in this regard and therefore the claim of the appellant for bad debts on account of tax deduction at source written off amounting to Rs. 23,94,011/- was rejected.

17. The learned authorized representative reiterated the claim and submitted that tax is deducted at source by the various customers whose income has been shown by the assessee in the profit and loss account and the above sum was neither returned to the assessee by those creditors and no adequate tax deduction at source certificates were issued by them and therefore such sum could not be recovered. He therefore stated that such tax deduction at source not received from the customers is trade debt and if it is written off in the books of accounts, it should be allowed as deduction. He further stated that the complete details were submitted with respect to the claim of the assessee however the learned CIT – A has erroneously stated that if no efforts were made by the assessee it is not allowable as deduction.
18. The learned departmental representative vehemently supported the order of the learned CIT – appeal and submitted that when the assessee has not received the tax deduction at source certificates and could not recover the sum from the various parties it cannot partake the character of debt and therefore same has not been allowed correctly by the learned AO.
19. We have carefully considered the rival contention and perused the orders of the lower authorities. The learned CIT – A has not allowed the claim of the assessee for tax deduction at source not recovered from the various payments of customers as according to him the assessee has not cared to take the credit of the tax deducted at source and therefore the same cannot become a trade debt recoverable from the concerned customer. However the learned CIT – A has mentioned that it can be treated as an admissible expenditure only if it is proved that the amount in question could not be claimed as the tax deduction at source was either not actually deducted or after deduction not deposited at all and the TDS certificates were not issued by the concerned debtor. On the same reasoning had the TDS certificates been issued by the customers or debtors to the assessee the assessee would have claimed the same as tax paid against his liability for payment of tax. In the present case, the assessee has neither presented the tax deduction at source certificates issued by the customers and claim them as tax paid by the assessee nor does the revenue have any evidence that credit of such tax deduction at source has been allowed to the assessee against any tax payable. Therefore, it is apparent that assessee has not been issued the tax deduction at source certificate by the

customers. In view of this, the amount becomes receivable from the debtors only. It is not the case of the revenue that assessee has not shown the income portion arising out of that sum in its profit and loss account for the amount of tax deduction at source not received from the customers of same have not been written off to the profit and loss account. In view of this we do not find any merit in the reasoning of the learned CIT – A that the appellant had not cared to take the credit of TDS deducted and therefore it cannot be recovered from the concerned customer. In fact, unless the tax deduction at source sum is deposited by the debtor then only the above sum is recoverable by the assessee towards his tax liability from the government of India and adjusted against the pre-existing liability, otherwise the same sum is recoverable from the debtor only. In view of this, we find that the assessee should have been allowed the deduction of the amount on account of Tax deducted by the customers towards tax deduction at source but no such deduction certificates has been presented to the assessee as bad debt. In view of this ground number 5 of the appeal of the assessee is allowed.

20. Ground number 6 of the appeal of the assessee is with respect to the disallowance of the expenditure incurred on computer software treating the same as capital expenditure. During the year the assessee has claimed expenditure of ₹ 6 714164/- because of software purchases. The learned assessing officer disallowed the claim of the appellant holding the same to be a capital expenditure and allowed depreciation at the rate of 60%. The assessee challenged the same before the learned CIT – A. The learned CIT – A enquired from the assessee whether the software was used mainly for updating, rationalizing the existing system and the benefit derived is neither permanent nor enduring in the nature. However, the assessee could not submit any further details with respect to this aspect. Therefore, the learned CIT appeal confirmed the disallowance holding that the software so acquired was with regard to the day-to-day functioning of the appellant was not proved by the assessee.
21. Before us the learned authorized representative submitted that assessee has furnished the complete details of the software expenditure incurred by the assessee of ₹ 1 0502442/-. He submitted that assessee has incurred software expenditure amounting to ₹ 6 714164/- and most of such expenditure are the annual maintenance contract expenditure for the various software used by the assessee. He submitted complete month-wise details of those expenditure. Details were also provided to the learned departmental representative. Based on the details it is submitted that assessee has given most of the expenditure on the software maintenance expenditure as annual maintenance of the software and the software licenses, which are time-based and does not have any benefit of enduring nature accruing to the assessee. He therefore submitted that software expenditure is in the nature of the revenue

- expenditure, recurring expenditure, annual maintenance expenditure, and annual renewal of the licenses of the various software and therefore they are not capital expenditure.
22. The learned departmental representative vehemently supported the order of the lower authorities and submitted that when the assessee has not provided the requisite details before the lower authorities about the expenditure incurred by the assessee on software they are correctly held to be capital expenditure and the learned assessing officer and the learned CIT – A has correctly allowed the depreciation at the rate of 60% on those expenditure.
23. We have carefully considered the rival contention and perused the orders of the lower authorities. We have noted the details of the software expenditure produced before us by the learned authorized representative, which was also provided to the learned departmental representative. Out of the total expenditure of ₹ 6 714164/- , most of the expenditure has been incurred by the assessee towards the software annual maintenance charges. The assessee's major expenditure of ₹ 8 36030/- was also because of the annual renewal of the software licenses. Assessee has also made the software development expenditure for bringing up the relevant software used for the day-to-day business needs of the assessee. In view of this, it cannot be said that the software has given any benefit of enduring nature to the assessee or are capital expenditure in nature. In view of this is the expenditure incurred by the assessee on software expenditure is day-to-day routine expenditure and annual renewal charges only, we are of the opinion that it is revenue in nature. In view of this, we direct the learned assessing officer to delete the disallowance of ₹ 6 714164/- made by the learned AO because of software expenditure holding the same to be capital expenditure. He is also further directed to withdraw the allowance of the depreciation at the rate of 60% thereon. Accordingly, ground number 6 of the appeal of the assessee is allowed.
24. Similar is the ground number 3 of the appeal of the assessee for assessment year 2004 – 05 and the disallowance of Rs. 4200977/- on account of software expenses was made. For the reasons given by us in ground number 6 of the appeal of the assessee for assessment year 2003 – 04, we allow ground number 3 of the appeal of the assessee for assessment year 2004 – 05 also.
25. Ground number 7 of the appeal of the assessee is with respect to the disallowance of ₹ 955200 being the expenses incurred on late cancellation charges holding that the same cannot be treated as business expenditure allowable under section 37 (1) of the income tax act. During the year the assessee has incurred expenditure of ₹ 9 55200 because of late cancellation charges. Before the learned AO assessee submitted that these expenditure are compensatory in nature. However, the learned assessing officer disallowed the same. Before the learned CIT – A, assessee stated that the assessee has submitted the ledger account,

however it was disallowed holding that no details have been furnished by the assessee. Even before the learned CIT – A the assessee submitted the same details and therefore the learned CIT – A confirmed the finding of the learned assessing officer. Therefore, the assessee in appeal before us.

26. The learned authorized representative submitted before us that these are the cancellation charges paid by the assessee to the various agencies on account of the general meeting expenditure incurred by the assessee. He submitted that the complete ledger account was provided by the assessee before the learned assessing officer however, the same was ignored. He submitted that these are the expenditure of compensatory nature.
27. The learned departmental representative vehemently submitted that when the assessee has failed to give the complete details of the expenditure that expenditure cannot be allowed to the assessee. It was further stated that before the learned assessing officer as well as before the learned CIT –A, stated that assessee has not furnished any information before the assessing officer or before the learned first appellate authority therefore the claim of the assessee cannot be allowed. He further stated that even before the coordinate bench no such details have been furnished.
28. We have carefully considered the rival contention and perused the orders of the lower authorities. The assessee has debited the expenditure of ₹ 9 55200/- as late cancellation charges under the head of business meeting and conferences. Before the learned assessing officer, the assessee could submit only the ledger account without any further evidences. The claim of the learned authorized representative that the above expenditure is compensatory in nature and therefore when certain meetings etc. are cancelled and the cancellation charges charged by the various agencies these expenditures are incurred. Therefore, these are incurred for the purposes of the business. However, in absence of the proper details of such expenditure whether those are incurred for the purpose of the business of the assessee or not cannot be ascertained. Despite repeated opportunities available to the assessee before the learned assessing officer as well as before the learned CIT – A, the assessee has not submitted the complete details but merely submitted the ledger account of those expenditure. In absence of complete details of the expenditure, the same has rightly been disallowed by the lower authorities. In view of this ground number 7 of the appeal of the assessee is dismissed.
29. Ground number 8 of the appeal of the assessee is with respect to the claim of deduction allowed under section 80HHE of the act of ₹ 3 454016/- against the claim of the assessee of ₹ 3 650192 made by the appellant in its return of income. The assessee submitted that it claimed deduction based on the certificate issued by the chartered accountant in form number

10 CCAF under the provisions of section 80 HHE of the income tax act. The learned assessing officer on examination of the claim of the assessee noted that assessee has reduced the rental income after allowing proportionate depreciation for the space rented out. The learned assessing officer noted that there is no such provision under the income tax act. Therefore, he reduced the whole rental income at the rate of 90% from the profits of the business of the assessee. It was further noted by him that assessee has not reduced the income from interest stating that the expenditure relatable to the interest income exceeds the interest income. Therefore, the learned assessing officer also reduced 90% of the interest income from the eligible profit. In addition, thereby against the claim of the assessee of ₹ 3 650192/- the deduction was worked out at ₹ 3 454016/-. The assessee aggrieved with the order of the learned assessing officer preferred an appeal before the learned CIT – A on the same issue. The learned CIT appeal also rejected the claim of the assessee holding that in view of the decision of jurisdictional High Court in the case of CIT versus liberty footwear private limited 287 ITR 339 (Punjab and Haryana) , which is against the assessee wherein the Hon'ble High Court has decided with respect to the deduction under section 80HH C that it is the gross interest received by the assessee which is to be considered in terms of explanation (baa) to section 80HH C of the act and not the net interest for the purpose of arriving at the profits of the business. Therefore, respectfully following the decision of the Hon'ble High Court the disallowance made by the learned assessing officer was upheld by him.

30. The learned authorized representative submitted before us that the issue is now squarely covered in favour of the assessee by the decision of the Hon'ble Supreme Court in case of ASG associated capsules (P) Ltd versus CIT 343 ITR 89 as well as the decision of the Hon'ble Delhi High Court in case of CIT versus Rama Honda Power equip and others 289 ITR 475. He further submitted that the issue is now also considered by the Hon'ble Supreme Court in case of liberty footwear company versus CIT 67 taxmann.com 55 (SC)
31. The learned departmental representative payment relied upon the orders of the lower authorities and submitted that the issue squarely covered the assessee by the decision of the Hon'ble jurisdictional High Court, which has been considered by the learned first appellate authority.
32. We have carefully considered the rival contention and perused the orders of the lower authorities. The claim of the assessee is that 90% of the rental income to be reduced from the eligible profit of the business should also further be reduced by the proportionate depreciation on the building of the assessee. Further the 90% of net interest income should be reduced and not the gross interest. The above issue has been considered by the Hon'ble Supreme Court in ACG Associated Capsules P Ltd V CIT 343 ITR 89 as under :-

“9. Explanation (baa) extracted above states that "profits of the business" means the profits of the business as computed under the head "Profits and gains of business or profession" as reduced by the receipts of the nature mentioned in clauses (1) and (2) of Explanation (baa). Thus, profits of the business of an assessee will have to be first computed under the head "Profits and gains of business or profession" in accordance with the provisions of sections 28 to 44D of the Act. In the computation of such profits of business, all receipts of income which are chargeable as profits and gains of business under section 28 of the Act will have to be included. Similarly, in computation of such profits of business, different expenses which are allowable under sections 30 to 44D have to be allowed as expenses. After including such receipts of income and after deducting such expenses, the total of the net receipts are profits of the business of the assessee computed under the head "Profits and gains of business or profession" from which deductions are to be made under clauses (1) and (2) of Explanation (baa).

10. Under clause (1) of Explanation (baa), ninety per cent. of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in any such profits are to be deducted from the profits of the business as computed under the head "Profits and gains of business or profession". The expression "included any such profits" in clause (1) of Explanation (baa) would mean only such receipts by way of brokerage, commission, interest, rent, charges or any other receipt which are included in the profits of the business as computed under the head "Profits and gains of business or profession". Therefore, if any quantum of the receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature is allowed as expenses under sections 30 to 44D of the Act and is not included in the profits of business as computed under the head "Profits and gains of business or profession", ninety per cent. of such quantum of receipts cannot be

Page No : 0098

reduced under clause (1) of Explanation (baa) from the profits of the business. In other words, only ninety per cent. of the net amount of any receipt of the nature mentioned in clause (1) which is actually included in the profits of the assessee is to be deducted from the profits of the assessee for determining "profits of the business" of the assessee under Explanation (baa) to section 80HHC.

11. For this interpretation of Explanation (baa) to section 80HHC of the Act, we rely on the judgment of the Constitution Bench of this court in *Distributors (Baroda) P. Ltd. v. Union of India* [1985] [155 ITR 120](#) (SC). Section 80M of the Act provided for deduction in respect of certain intercorporate dividends and it provided in sub-section (1) of section 80M that "where the gross total income of an assessee being a company includes any income by way of dividends received by it from a domestic company, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction from such income by way of dividends an amount equal to" a certain percentage of the income mentioned in this section. The Constitution Bench held that the court must construe section 80M on its own language and arrive at its true interpretation according to the plain natural meaning of the words used by the Legislature and so construed the words "such income by way of dividends" in sub-section (1) of section 80M must be referable not only to the category of income included in the gross total income but also to the quantum of the income so included. Similarly, Explanation (baa) has to be construed on its own language and as per the plain natural meaning of the words used in Explanation (baa), the words "receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits" will not only refer to the

nature of receipts but also the quantum of receipts included in the profits of the business as computed under the head "Profits and gains of business or profession" referred to in the first part of Explanation (baa). Accordingly, if any quantum of any receipt of the nature mentioned in clause (1) of Explanation (baa) has not been included in the profits of business of an assessee as computed under the head "Profits and gains of business or profession", ninety per cent. of such quantum of the receipt cannot be deducted under Explanation (baa) to section 80HHC.

12. If we now apply Explanation (baa) as interpreted by us in this judgment to the facts of the case before us, if the rent or interest is a receipt chargeable as profits and gains of business and chargeable to tax under section 28 of the Act, and if any quantum of the rent or interest of the assessee is

Page No : 0099

allowable as an expense in accordance with sections 30 to 44D of the Act and is not to be included in the profits of the business of the assessee as computed under the head "Profits and gains of business or profession", ninety per cent. of such quantum of the receipt of rent or interest will not be deducted under clause (1) of Explanation (baa) to section 80HHC. In other words, ninety per cent. of not the gross rent or gross interest but only the net interest or net rent, which has been included in the profits of business of the assessee as computed under the head "Profits and gains of business or profession", is to be deducted under clause (1) of Explanation (baa) to section 80HHC for determining the profits of the business.

13. The view that we have taken of Explanation (baa) to section 80HHC is also the view of the Delhi High Court in CIT v. Shri Ram Honda Power Equip [2007] [289 ITR 475](#) (Delhi) and the Tribunal in the present case has followed the judgment of the Delhi High Court. On appeal being filed by the Revenue against the order of the Tribunal, the High Court has set aside the order of the Tribunal and directed the Assessing Officer to dispose of the issue in accordance with the judgment of the Bombay High Court in CIT v. Asian Star Co. Ltd. [2010] [326 ITR 56](#) (Bom). We must, thus, examine whether reasons given by the High Court in its judgment in CIT v. Asian Star Co. Ltd. [2010] [326 ITR 56](#) (Bom) were correct in law.

14. On a perusal of the judgment of the High Court in CIT v. Asian Star Co. Ltd. [2010] [326 ITR 56](#) (Bom), we find that the reason which weighed with the High Court for taking a different view, is that rent, commission, interest and brokerage do not possess any nexus with export turnover and, therefore, the inclusion of such items in the profits of the business would result in a distortion of the figure of export profits. The High Court has relied on a decision of this court in CIT v. K. Ravindranathan Nair [2007] [295 ITR 228](#) (SC) in which the issue raised before this court was entirely different from the issue raised in this case. In that case, the assessee owned a factory in which he processed cashew nuts grown in his farm and he exported the cashew nuts as an exporter. At the same time, the assessee processed cashew nuts which were supplied to him by exporters on job work basis and he collected processing charges for the same. He, however, did not include such processing charges collected on job work basis in his total turnover for the purpose of computing the deduction under section 80HHC(3) of the Act and as a result this turnover of collection charges was left out in the computation of profits and gains of business of the assessee and as a result ninety per cent. of the profits of the assessee arising out of the receipt of processing charges was not deducted under clauses (1) of Explanation (baa) to section 80HHC. This court held that the processing

charges was included in the gross total income from cashew business and hence in terms of Explanation (baa), ninety per cent. of the gross total income arising from processing charges had to be deducted under Explanation (baa) to arrive at the profits of the business. In this case, this court held that the processing charges received by the assessee were part of the business turnover and accordingly the income arising therefrom should have been included in the profits and gains of business of the assessee and ninety per cent. of this income also would have to be deducted under Explanation (baa) under section 80HHC of the Act. In this case, this court was not deciding the issue whether ninety per cent. deduction is to be made from the gross or net income of any of the receipts mentioned in clause (1) of Explanation (baa).

15. The Bombay High Court has also relied on the Memorandum explaining the clauses of the Finance Bill, 1991, contained in the circular dated December 19, 1991, of the Central Board of Direct Taxes to come to the conclusion that Parliament intended to exclude items which were unrelated to the export turnover from the computation of deduction and while excluding such items which are unrelated to export for the purpose of section 80HHC, Parliament has taken due note of the fact that the exporter assessee would have incurred such expenditure in earning the profits and to avoid a distorted figure of export profits, ninety per cent. of the receipts like brokerage, commission, interest, rent, charges are sought to be excluded from the profits of the business. In our considered opinion, it was not necessary to refer to the Explanatory Memorandum when the language of Explanation (baa) to section 80HHC was clear that only ninety per cent. of receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits computed under the head "Profits and gains of business" of an assessee could be deducted under clause (1) of Explanation (baa) and not ninety per cent. of the quantum of any of the aforesaid receipts which are allowed as expenses and, therefore, not included in the profits of business of the assessee.

16. In the result, we allow the appeal and set aside the impugned order of the High Court and remand the matter to the Assessing Officer to work out the deductions from rent and interest in accordance with this judgment. No costs.”

33. Therefore, in view of the decision of the Hon'ble Supreme Court we direct the learned assessing officer to allow the claim of the deduction under section 80 HHE of the income tax act by reducing only 90% of the net interest income and net rental income from the eligible business. In view of this ground number 8 of the appeal of the assessee is allowed.
34. For similar reasons we also allow ground number 4 of the appeal of the assessee for assessment year 2004 – 05.
35. Ground number 9 of the appeal is with respect to the transfer pricing adjustment made by the learned assessing officer/transfer pricing officer of ₹ 5 4628379. The learned authorized representative submitted before us the order passed by the learned assessing officer pursuant to the order of the learned CIT – A under section 250 (6) of the income tax act on 9/3/2012 where the adjustment made by the learned transfer pricing officer of ₹ 5 4628379/-

was made nil. Therefore the total addition on account of the transfer pricing made in the hands of the assessee has been deleted by the learned assessing officer after verification on the direction of the learned CIT – A. Therefore, the above ground of appeal does not survive hence dismissed.

36. For similar reasons we also dismiss ground number 5 of the appeal of the assessee for assessment year 2004 – 05 which is also on the transfer pricing adjustment made by the learned assessing officer which on the direction of the learned CIT A after verification has been reduced to nil. Therefore the grievance of the assessee does not remain hence the ground is dismissed.
37. Ground number 10 of the appeal of the assessee is against the initiation of penalty proceedings under section 271 (1) ©. The above ground is premature at this particular stage and therefore it is dismissed. For similar reasons we also dismiss the ground number 6 of the appeal of the assessee for assessment year 2004 – 05 against the initiation of penalty proceedings.
38. Before us the assessee has also raised additional ground of appeal numbering the is ground number 11 & 12 as under:-

“11. without prejudice to the grounds of appeal already filed by the appellant the learned AO as well as the Hon’ble CIT – A and in not allowing the deduction available under section 10 A of the income tax act on the increased profits of the business of the eligible undertaking on account of various disallowance made.

12. Without prejudice to the grounds of appeal already filed by the appellant, the learned AO as well as the Hon’ble CIT – A and in not allowing the deduction available under section 80 HHE of the act on the increased profits of the business on account of various disallowance is made.”
39. The learned authorized representative submitted that above grounds of appeal are legal in nature does not require any further facts to be investigated and therefore they should be admitted. He further submitted that now the issue is squarely accepted by the Central Board of direct taxes in CIRCULAR NO.37/2016 [F.NO.279/MISC./140/2015/ITJ], DATED 2-11-2016.
40. The learned a departmental representative vehemently objected to the additional ground of appeal and submitted that it is not legal in nature.
41. We have carefully considered the rival contention and find that it is just a computational mechanism that is suggested by the learned authorized representative by raising 2 additional grounds of appeal which has been already accepted by the Central Board of direct taxes in

circular number 37/2016 issued on 2/11/2016. In view of this, the additional grounds of appeal of assessee are admitted and the learned assessing officer is directed to follow the circular number 37/2016 and if the eligible income for deduction increases on account of any disallowance to the business income made by that industrial undertaking, than the learned AO is directed to enhance the deduction proportionately according to the formula prescribed under the respective sections. In the result ground number 11 and 12 of the appeal of the assessee are allowed.

42. In the result, appeals filed by the assessee for assessment year 2003 – 04 and 2004 – 05 are partly allowed.
43. For assessment year 2003 – 04 and 2004 – 05, The learned assessing officer is aggrieved in the grounds of appeal against the direction of the learned CIT – A to the learned assessing officer to verify and recompute the allowance of the expenses with respect to the provision of leave encashment reversed, account of provision for warranty expenses as well as account of provision for warranty reversed and the adjustment of ₹ 5 4628379/- made by the learned assessing officer on account of the transfer pricing adjustment. The main grievance of the revenue is that as per the provisions of section 251 of the income tax act the learned CIT appeal has the power to confirm, reduce, enhance, or annul the assessment where the appeal relates to an assessment order. It is further stated that the power to set aside has been omitted by the finance act, 2001 with effect from 1/6 2001 and therefore the order passed by the learned CIT – A on 17/03/2001 giving the direction to the learned assessing officer are contrary to the provisions of section 251 (1) (a) of the act.
44. The learned authorized representative referred to the direction of the learned CIT – A and it was submitted by him that the learned CIT appeal has given a specific direction to the learned assessing officer to recompute the disallowance after proper verification of the certain aspects which are not available on the record of the learned CIT – A. Therefore there is no infirmity in the order passed by the learned CIT – A.
45. We have carefully considered the rival contention and perused the orders of the lower authorities. We have also perused the orders of the appeal effect order passed by the learned assessing officer which are placed at page number 838/845 of the paper books and also the order of the learned transfer pricing officer dated 9/3/2012 wherein the adjustment and the addition made by the learned assessing officer found not to be sustainable. When the addition itself have been found to be not sustainable by the learned assessing officer while giving appeal effect to the order of the learned CIT – A when merely certain calculations/ or factual aspects are required to be verified. The learned CIT – A is not prohibited in directing the learned assessing officer to verify certain calculations and facts. In view of this we do not

find any infirmity in the order of the learned CIT – A in directing the learned assessing officer for verification of the certain aspects of the computation of the total income. In the result, appeal filed by the revenue is dismissed.

46. The appeal of the revenue for assessment year 2004 – 05 is also on the similar grounds raising the similar contentions. For the reasons given by us for assessment year 2003 – 04, we also dismiss the appeal of the revenue for assessment year 2004 – 05.
47. In the result appeal of the revenue for assessment year 2003 – 04 and 2004 – 05 are dismissed.

Order pronounced in the open court on 24/08/2018.

-Sd/-

(DIVA SINGH)
JUDICIAL MEMBER

-Sd/-

(PRASHANT MAHARISHI)
ACCOUNTANT MEMBER

Dated: 24/08/2018
A K Keot

Copy forwarded to

1. Applicant
2. Respondent
3. CIT
4. CIT (A)
5. DR:ITAT

ASSISTANT REGISTRAR
ITAT, New Delhi