

Cit Vs. Eicher Motors Ltd.

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Court : Madhya Pradesh

Decided On : Oct-18-2006

Reported in : (2008)214CTR(MP)629; [2007]293ITR464(MP)

Judge : S.K. Kulshrestha and ;S.K. Seth, JJ.

Appellant : Cit

Respondent : Eicher Motors Ltd.

Disposition : Appeal dismissed

Judgement :

S.K. Seth, J.

1. This order shall also govern the disposal of connected 1 I. T. A. Nos. 27 of 2003 ; 29 of 2003 and 43 of 2003 as these appeals under Section 260A of the Income Tax Act, 1961 (hereinafter referred to as 'the Act' for short), are at the instance of the revenue against the orders of the Income Tax Appellate Tribunal relating to the assessment years 1989-90 ; 1990-91 ; 1991-92 and 1992-93.

2. I. T. A. No. 28 of 2003 was admitted for final hearing on the following substantial questions:

(1) Whether the Income Tax Appellate Tribunal, Indore erred in holding that the amount paid to Mitsubishi Motors Corporation by the assessee as royalty was

allowable as revenue expenditure ?

(2) Whether, on the facts and circumstances of the case, the Tribunal was justified in law in permitting the assessee to raise additional ground relating to funded interest when no such claim was ever made before the assessing officer or Commissioner (Appeals) ?

(3) Whether, on the facts and circumstances of the case, the Tribunal was justified in law in confirming the order of the Commissioner (Appeals) in allowing the depreciation on notional foreign exchange fluctuation ?

3. It is admitted by the parties that the decision on the above questions in this appeal must necessarily govern the other appeals, so we do not propose to say anything about them except to mention that in I. T. A. No. 27 of 2003 the first two questions; in I. T. A. No. 29 of 2003 last two questions and in I. T. A. No. 43 of 2003 only the third question were formulated at the time of admission of appeals. On that premise, we are deciding this bunch of appeals by the common order.

Question No. 1

4. Necessary facts are undisputed. The assessee, a public limited company, is an automobile manufacturer. It entered into a technical assistance agreement with Mitsubishi Motors Corporation (MMC) Japan, for a licence to use and utilize technical know-how and drawings, designs etc. to manufacture the light commercial vehicles (LCVs) and sale thereof under the brand name of MMC in the defined territory during the currency of the licence agreement. It was agreed between the parties that the assessee would pay royalty in periodic instalments at 3 per cent, of MMC FOB Japanese port price, for the use of technical know-how and assistance and information and services provided for manufacture/assembly of licenced products. The assessee, as a licensee, paid royalty under the agreement to MMC in different assessment years as under:

Assessment years	Royalty paid in lakhs Rs.
1988-89	41.00
1989-90	31.18
1990-91	52.23
1991-92	98.08
1992-93	172.27
1993-94	137.57
1994-95	163.18

5. It is not in dispute that for the assessment years 1988-89 and 1989-90, the claim of the assessee regarding royalty payment was accepted by the department as revenue expenditure, however it was disallowed in subsequent assessment years by the assessing officer and the Commissioner (Appeals) on the ground that it was an expenditure capital in nature and the assessee was entitled to only amortization as per law. On appeal, the Income Tax Appellate Tribunal accepted the contention of the assessee and treated it as revenue expenditure. Now, in these appeals, at the instance of the revenue, short question for determination is whether it was admissible for deduction under capital expenditure for acquiring an asset or advantage of enduring nature, or expenditure properly attributable to revenue.

6. Learned Counsel appearing for the revenue submitted that the Income Tax Appellate Tribunal committed serious and grave illegality in treating the royalty payment as revenue expenditure. Referring to the agreement dated 4-10-1982, and various clauses thereof, he submitted that the assessee acquired exclusive right or advantage of enduring nature to exploit the technical know-how and assistance for manufacture and sale of light commercial vehicles (LVC) therefore, it was a capital expenditure and not revenue expenditure as was rightly held by the assessing officer and the Commissioner (Appeals).

7. Learned Counsel for the assessee, per contra, submitted that the Income Tax Appellate Tribunal after analysing various terms and conditions of the technical assistance agreement in the proper perspective rightly held that royalty payment made by the assessee to MMC was a revenue expenditure. According to him, such finding based upon proper appreciation of facts and law, does not call for interference by this Court. He further submitted that the Tribunal arrived at the aforesaid finding of fact on proper appreciation of material and principle of law and as such, this Court could not interfere with such finding. On this score, according to him, there is no merit and substance in these appeals.

8. After having heard the arguments at length, we are of the considered view that the legal position is quite clear.

9. The provisions of the Act require the balance of profits and gains to be found. So, a profit and loss account must be prepared setting on one side income receipts and on the other expenses properly chargeable against them. In so far as the Act prohibits a particular kind of deduction, it must receive effect. Section 37 of the Act, provides that any expenditure laid out or expended wholly or exclusively for the purpose of the business or profession shall be allowed in computing the income chargeable under the head 'Profits and gains of business or profession'. Such expenditure, however, should not be in the nature of capital expenditure or personal expenses of the assessee. Any expenditure incurred by the assessee can, therefore, be claimed as an allowable deduction under the head 'Profits and gains of business or profession', if the expenditure satisfies two terms : (i) that the expenditure laid out or expended is wholly and exclusively for the purposes of the business and/or profession, and (ii) that it is not in the nature of capital outlay. That being so, it shall be always necessary to examine and explain the nature of the expenditure incurred to be an allowable deduction to the assessee under the head of 'Profits and gains of business or profession' in terms of Section 37. Whether a particular outlay of a trader can be set against income or must be regarded as a capital outlay has proved to be a difficult question. As observed by Lord Reid in *Regent Oil Co. Ltd. v. Inland revenue Commissioners* (1969) 73 ITR 301 : (1965) 3 All ER 174

It may be possible to reconcile all the decisions, but it is certainly not possible to reconcile all the reasons given for them. I think that much of the difficulty has arisen from taking too literally general statements made in earlier cases and seeking to apply them to a different kind of case which their authors almost certainly did have in mind?in seeking to treat expressions of judicial opinion as if they were words in an Act of Parliament. Moreover a further source of difficulty has been a tendency in some cases to treat some one criterion as paramount and to press it to its logical conclusion without proper regard to other factors in the case. The true view appears to me to be that stated by Lord Macmillan in *Van den Berghs Ltd. v. Clark* (1935) AC 431: 'While each case is found to turn on its own facts, and no infallible criterion emerges, nevertheless the decisions are useful as illustrations and as affording indications of the kind of considerations which may relevantly be borne in mind in approaching the problem'.

10. It is well established that no strait-jacket blueprint or sufficiently accurate and reasonably comprehensive test to draw any clear line of demarcation to ascertain on which side of the line, the outlay in a particular case might reasonably be held to fall, between capital and revenue expenditure because of infinite variety of situational diversities. However, some broad and general tests have been suggested from time to time. These tests are generally efficacious and serve as useful servants, but as masters, they tend to be overtaxing. The question is ultimately a question of law for the court to decide, but it is a question which must be answered in the light of all the circumstances which it is reasonable to take into account, and the weight which must be given to a particular circumstance in a particular case must depend rather on common sense and business point of view rather than upon the juristic classification of the juristic rights, if any, secured, employed or exhausted in the process

11. When one is dealing with tangible assets, it is generally not very difficult to reach a decision. Things, which the trader uses in his business to produce what he has to sell are part of his fixed capital and their cost is a capital outlay although their useful life may be short. Things, which a trader turns over in the course of his trade, are circulating capital and their cost is a revenue expense. However, when one comes to intangible assets there is much more difficulty. To help the conduct of his business a trader may obtain a right to do something on someone else's property or an obligation by someone to do or refrain from doing something or makes a contract which affects the way in which he conducts his business ; and the right or obligation or the effect of the contract may endure for a short or a long period of years. The question then arises whether the sum, which he has paid for that advantage, is a capital or revenue expense. If the asset, which is acquired, is in its intrinsic nature a capital asset, then any sum paid to acquire it must surely be capital outlay; and we do not see how it could matter that the payment was made by sums paid annually or periodically. It appears to us, however, that an asset, which is nothing more than a right to enjoy a certain advantage over a period, is intrinsically of a different character from a thing, which a person buys and can immediately use or consume in any way he chooses.

12. The case which is generally cited and relied on, often by both sides, is 12 British Insulated and Helsby Cables Ltd. v. Atherton (1925) All ER 623: (1926) AC 205. In order to understand the passage in Viscount Cave L.C's speech, it is necessary to have the facts in mind. In that case, the company laid out a sum to assist in the setting up of a pension fund for its staff. It was intended that the fund would endure for the whole life of the company, and it was not expected that the company would have to lay out any further sum for this purpose. So when Viscount Cave referred to expenditure 'made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade', he was dealing with a case where the payment was made to form a nucleus of a fund to provide pension for its staff. It was literally once and for all expenditure where the asset or advantage was to last as long as the company lasted and therefore, it was held to be a capital payment. The nature or character of the outgoings and the advantage gained tilted the balance in favour of the view that the expenditure was of a capital nature.

13. We have already pointed out that capital and revenue expenditure are 13 distinct and easily ascertainable in obvious cases that lie far from boundary, but the line of distinction is often hard to draw in borderline cases ; and conflicting considerations may produce a situation where the answer turns on question of emphasis and degree.

14. In this bunch, we are dealing with payments made to MMC to secure 14 technical know-how and to sell LCVs under their brand name during the currency of the agreement subject to periodic payment of royalty for using the licence. The Supreme Court in CIT v. Ciba of India Ltd. : [1968]69ITR692(SC) has enunciated the principles applicable to such cases. In that case, the assessee a subsidiary of the Swiss company paid certain payment to Ciba Ltd., Basle (the Swiss company) pursuant to the agreement dated December 17, 1947, whereby the latter agreed for 'technical and research contribution' in so far as they relate to pharmaceutical products which were manufactured, processed and sold by the assessee in India. It was held that the agreement merely give the right to the assessee, without any thing more, to draw upon the technical knowledge of the foreign collaborator for the purpose of carrying on its business and did not acquire an asset or advantage

of enduring nature for the benefit of its business. Considering the effect of payment, it was held to be a revenue expenditure. The same was the situation in *Alembic Chemical Works Co. Ltd. v. CIT* : [1989]177ITR377(SC) . That was the case, where the assessee who was engaged in the manufacture of antibiotics including penicillin, acquired know-how to produce higher yield and sub- culture of strains of penicillin and there was no evidence to indicate that this was not in the line of existing manufacturing operations and, therefore the Supreme Court took the view that the payment was made in the course of carrying on an existing business and the outlay was incurred for the purpose of acquiring the technical know-how in relation to its business and considering the rapid strides in science and technology is to pigeon-holding an outlay, such as in this case as capital. It was on that basis the court held that though a lump sum payment had been made once for all, it was not capital in nature and attracted the deduction under Section 37 of the Income Tax Act. In the light of the law laid down in these two decisions of the Supreme Court, and on a balance of all the material considerations in the case in hand, the scales appear to incline in favour of the expenditure being revenue and not capital outgoings. We think, it is more reasonable to regard the periodic royalty payment to MMC as an outlay for earning profits in the normal course of business than as expenditure with the object of acquiring an advantage or asset of enduring and/or lasting nature for the benefit of the trade. In view of the foregoing discussion, we feel that reliance placed by learned Counsel for the revenue on the decisions of the Supreme Court reported in *Jonas Woodhead and Sons (India) Ltd. v. CIT* : [1997]224ITR342(SC) and *Eimco K. C. P. Ltd. v. CIT* : [2000]242ITR659(SC) is of no avail as these decisions are clearly distinguishable on their facts. In *Jonas Woodhead and Sons (India) Ltd.* : [1997]224ITR342(SC) the assessee made payments under collaboration agreement with foreign firm to set up a factory to manufacture automobiles springs and suspension for road and rail carriages. It was held that the payments made for a new business without embargo on the assessee to continue with manufacture the product in question even after the expiry of agreement. Likewise, in *Eimco K. C. P. Ltd.* : [2000]242ITR659(SC) the court was dealing a situation where the assessee was promoted by two companies, viz., M/s. Eimco Corporation USA and M/s. KCP Ltd., an Indian company. Promoter companies agreed to pay initially certain sum of

money towards their contribution. The foreign collaborator contributed technical know-how consisting of right and licence to commence manufacture and sale of existing Eimco Sedimentation and filtration equipment. The technical know-how was valued at Rs. 2,35,000. The board of directors of the assessee-company allotted the equity shares of Rs. 2,35,000 being the value of technical know-how and claimed deduction as revenue expenditure. It was turned down on the ground that in allotting the equity shares, the assessee reimbursed foreign collaborator exclusively for the purpose of the business of the assessee after incorporation and held to be capital expenditure. The factual situation in the case in hand is quite different as pointed out above. Thus, we have no hesitation to hold that the Income Tax Appellate Tribunal rightly decided the issue relating to question No. 1 in favour of the assessee and against the revenue.

Question No. 2

15. It is admitted that this question pertains to the jurisdiction of the Tribunal to allow the assessee to raise additional ground in appeal. Law in this regard is quite settled. In *CIT v. S. Nelliappan* : [1967]66ITR722(SC) it was held that while hearing an appeal, the Tribunal may give leave to the assessee to urge grounds not set forth in the memorandum of appeal, and in deciding the appeal, the Tribunal is not restricted to the grounds set forth in the memorandum of appeal or taken by leave of the Tribunal. The same view was reiterated in *National Thermal Power Co. Ltd. v. CIT* : [1998]229ITR383(SC) . In that case, the following question was under consideration (page 386):

Where on the facts found by the authorities below a question of law arises (though not raised before the authorities) which bears on the tax liability of the assessee, whether the Tribunal has jurisdiction to examine the same ?

16. Answering the question in the affirmative, it was held (page 386) :16

Under Section 254 of the Income Tax Act, the Appellate Tribunal may, after giving both the parties to the appeal an opportunity of being heard, pass such orders thereon as it thinks fit. The power of the Tribunal in dealing with appeals is thus expressed in the widest possible terms. The purpose of the assessment

proceedings before the taxing authorities is to assess correctly the tax liability of an assessee in accordance with law. If, for example, as a result of a judicial decision given while the appeal is pending before the Tribunal, it is found that a non-taxable item is taxed or a permissible deduction is denied, we do not see any reason why the assessee should be prevented from raising that question before the Tribunal for the first time, so long as the relevant facts are on record in respect of that item. We do not see any reason to restrict the power of the Tribunal under Section 254 only to decide the grounds which arise from the order of the Commissioner (Appeals). Both the assessee as well as the department have a right to file an appeal/cross-objections before the Tribunal. We fail to see why the Tribunal should be prevented from considering questions of law arising in assessment proceedings although not raised earlier.

17. Before us, it is not the case of the revenue that no adequate material 17 was before the Tribunal or the revenue was denied the opportunity of being heard in respect of the new ground raised by the assessee before the Tribunal in appeal. In view of this, we find no merit and substance in the second question.

Question No. 3

18. From the record it is clear that the Commissioner of Income-tax(Appeals) allowed the claim of the assessee following the decision of the Supreme court in CIT v. Arvind Mills Ltd. : [1992]193ITR255(SC) , therefore, the answer to the third question, no longer detains us. We also feel that this is not a substantial question of law in view of the decision of the Supreme court in Santosh Hazari v. Purushottam Tiwari : [2001]251ITR84(SC) , herein it is held that (page 90 of 251 ITR):

A point of law which admits of no two opinions may be a proposition of law but cannot be a substantial question of law. To be 'substantial' a question of law must be debatable, not previously settled by law of the land or a binding precedent, and must have a material bearing on the decision of the case, if answered either way, in so far as the rights of the parties before it are concerned. It will, therefore, depend on the facts and circumstances of each case whether a question of law is a substantial one and involved in the case, or not; the paramount overall

consideration being the need for striking a judicious balance between the indispensable obligation to do justice at all stages and impelling necessity of avoiding prolongation in the life of any lis.

19. In view of the above, we have no hesitation to hold that the third question is not a substantial question of law and the Tribunal committed no error in confirming the order of the Commissioner (Appeals) in allowing the depreciation on notional foreign exchange fluctuation therefore, the answer must be in the affirmative.

20. In view of the foregoing discussion we dismiss these appeals by holding that the affirmative answer to all the three questions must go in favour of the assessee and against the revenue. Let a copy of this order be kept in the record of each connected appeal.

21. Order accordingly with no costs.

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